

## CHAPTER 8

### SCOPE FOR ADDITIONAL REVENUE

8.1 Under item (i) of paragraph 4 of the Presidential Order dated the 29th February, 1968, we have to make recommendations on the scope for raising additional revenue by the States from the sources of revenue available to them. A full examination of this question would involve our embarking upon an enquiry which can only be adequately undertaken by a Taxation Enquiry Commission. Apart from limitations of time, we did not have sufficient material supplied by the States on this question. In the views expressed by them, some States like Andhra Pradesh, Assam and Gujarat stated that they had already fully exploited all the sources of revenue available to them, and that there was hardly any fresh avenue left. Some of them referred to the ways in which the Government of India could help them in raising more revenues. The Government of Assam referred to the Centre's unhelpful attitude regarding revision of rate of royalty on crude oil and other minerals and the reimposition of carriage tax on tea and jute. The Government of Gujarat pointed out that the *per capita* incidence of State taxes in Gujarat had increased in recent years and that, unlike other States which had abolished land revenue, it had imposed education cess and raised the rate of local fund cess. They suggested that stamp duties under Article 268 on bills of exchange, cheques, etc., could be increased. Several States like Mysore, Haryana, Punjab and Rajasthan referred to their difficulties in increasing rates of taxes because of lower rates in neighbouring States. Bihar, Kerala, Punjab and Uttar Pradesh had already appointed Taxation Enquiry Committees whose reports were then awaited and Mysore was contemplating the appointment of a similar Committee. Haryana, Madhya Pradesh, Jammu and Kashmir, Rajasthan and Orissa conceded that there was some scope for raising taxes.

8.2 The State Governments had agreed with the Planning Commission to targets aggregating to Rs. 1,109 crores for mobilisation of additional resources during the Fourth Plan. These targets include revenue resources as well as receipts from rural debentures (*vide* Table 10). The representatives of many States told us that they had not had time to work out detailed proposals to achieve these targets. The data available with us are thus mainly limited to comparative yields and rates of some of the different taxes in States, which we compiled and the published material on the subject including recent reports by the Taxation Enquiry Committees of Uttar Pradesh and Kerala. We have, therefore, confined our comments only to a few general features.

8.3 We may begin with a broad picture of the States' tax revenues *per capita* and as percentage of their income (*vide* Tables 14 and 15). Unfortunately, the Central Statistical Organisation has not compiled firm estimates of the States' income on a comparable basis for years later than 1964-65, and we have used the average State

tax would mainly fall on the advertisers and advertising agents and not on the publishers, it is possible that the tax might adversely affect the finances of smaller newspapers. It will, therefore, be desirable to exempt small newspapers and periodicals from such tax. A part of the burden of the tax might indirectly fall on the Government of India and State Governments. Nevertheless, we consider that this is *prima facie*, a reasonable source from which additional revenues assignable to States could conveniently be raised. Taxes on parallel forms of publicity media like film slides, hoardings, etc. are already being levied. A tax levied at suitable rates, with higher rates on some advertisements like those inserted by companies, large business houses, cinema exhibitors, etc. may not be an undue burden if provision is made for exemption of small newspapers. In the absence of requisite data, we could not arrive at a reliable estimate of the likely revenue. But we consider that there is scope for the levy of this tax and we suggest that the Government of India may examine the question of its levy, rate structure, exemptions to be given, and other relevant matters.

incomes for the three years 1962-63 to 1964-65 as the basis of assessing the average incidence of State taxes; tax revenue figures are, however, available for 1967-68. The effect of taking the tax yields of 1967-68 as a percentage of average State incomes of 1962-63 to 1964-65 would naturally be to exaggerate to some extent the tax burden in all the States. The extent of such over-statement can be seen from the fact that the national income of the country increased during the period by 61 per cent. The extent of increase of money incomes for each State would differ as it would not have participated to the same extent in the change in national income.

8.4 Table 14 shows large variations in *per capita* tax revenues from Rs. 12 in Bihar and Orissa to Rs. 37 approximately in Maharashtra and Punjab. The percentages of tax revenue to State income (*vide* Table 12) also show a wide range of variation from 4.3 per cent. for Orissa to 8.7 per cent. for Kerala. The percentages are widely different even among States with a similar level of *per capita* income. For instance, among the States with higher *per capita* income, while Maharashtra and Punjab raised more than 8 per cent. of their incomes as tax revenues, West Bengal with a similar industrial base as Maharashtra obtained only 6.2 per cent. Among the other four States with *per capita* income above the all-India average, Tamil Nadu raised 7.8 per cent., while Andhra Pradesh and Assam got only a little above 5 per cent.

8.5 Table 15 indicates *prima facie* substantial differences between the tax efforts of States which are similarly situated as regards their *per capita* income and economic structure. It would be possible for many States to raise larger resources by studying the tax systems and rates adopted by the more highly taxed States in their own income-groups.

8.6 Table 14 shows Statewise the *per capita* yields of important taxes in 1967-68. The four major State taxes are general sales tax, excise duties, land revenue including agricultural income-tax and taxes on transport. The *per capita* yield of general sales tax among the five States with higher *per capita* income varied from more than Rs. 14 in Maharashtra to less than Rs. 7 in West Bengal and Haryana. In the next group, Tamil Nadu had Rs. 11 per head; while Andhra Pradesh and Assam had Rs. 6.88 and Rs. 5.23 respectively. From the States with *per capita* income below the all-India average, Kerala obtained more than Rs. 10

8.7 In taxes on transport, Jammu and Kashmir derived the highest *per capita* tax revenue of Rs. 9.26 and Tamil Nadu came next; West Bengal with Rs. 3.42 was ninth in rank in this regard.

8.8 The yield of excise duties depends on the States' policy regarding prohibition. In this field, Punjab derived by far the highest revenue of Rs. 11 *per capita* and the next highest was Haryana with Rs. 6.86. Kerala obtained Rs. 4.7, while West Bengal derived only Rs. 3.21. Both Gujarat and Tamil Nadu with prohibition policies obtained less than Re. 0.3 per head; Maharashtra, which has recently relaxed its excise policy, got less than Re. 1. Here again, West Bengal was behind Andhra Pradesh which had a large dry area, Jammu and Kashmir and even Rajasthan

8.9 Land revenue and agricultural income-tax proceeds in different States on a *per capita* basis are not comparable. But considering that these are the only two direct taxes on incomes from agriculture, which constitute more than two-fifths of the total income of all States, their total contribution of Rs. 113 crores to the tax revenue of all States cannot be considered *prima facie* to be very satisfactory. Agricultural income tax contributed on an average only one-tenth of the direct taxes on land in all States; in Kerala it was two-thirds; in Assam one-half; in Tamil Nadu and Mysore one-fifth; and in West Bengal less than one-seventh. Many States do not levy tax on agricultural income.

8.10 As particular taxes are levied on different bases, it would be more useful to assess their comparative burden by taking their yields as percentages of their bases. It has not, however, been possible to quantify the base of each tax. Proceeds from land revenue and agricultural income-tax may be fairly compared with the agricultural incomes of the States. In case of other taxes, State incomes can be considered as broad indicators of their potential productivity. Land taxation in 1967-68 as percentage of State agricultural income in 1962-65 was the highest in Rajasthan, being 2.49 per cent. In the most prosperous agricultural State, Punjab, it was 0.52 per cent., the same as in Bihar and Orissa, the two States with lowest *per capita* income. In Andhra Pradesh the yield was less than one per cent. In spite of the general applicability of land taxes to all land holders, the total revenues in all States were only 1.3 per cent. of the agricultural income as compared with personal income-tax on non-agricultural income which amounted to 2.5 per cent. of such income. As percentage of State incomes (*vide* Table 15), general sales tax proceeds came to 3 per cent. in Kerala and Maharashtra, but only 1.4 per cent. in West Bengal and Haryana. Taxes on transport gave 3.1 per cent. in Jammu and Kashmir, and about 1.5 per cent. in Kerala and Tamil Nadu. State excise duties contributed 2.3 per cent. in Punjab, 1.6 per cent. in Haryana and about 1.5 per cent. in Jammu and Kashmir and Kerala, but 0.7 per cent. only in West Bengal.

8.11 This comparative study of the contribution of important State taxes brings out the importance of indirect taxation in State finances. It also shows the large differences in their exploitation by the States.

8.12 It is unfortunately not possible to get a full picture of the long term changes in the burden of State taxation in relation to their income, as reliable figures of State incomes are not available over a sufficiently long period. It is, however, possible to compare the changes in the combined tax revenues of all States with those in the all-India national income. It will be seen (Table 13) that whereas State tax revenues increased faster than national income in the fifteen years since 1950-51, the percentage of State tax revenues to national income has diminished between 1965-66 and 1967-68 in spite of additional taxation.

8.13 Table 7 gives the yields of different State taxes since 1950-51 for all States together. It shows that the general complaint that the

States' sources of tax revenue are inelastic is not true of all taxes. State tax revenues have increased five-fold during this period, while Union tax revenues have grown nearly six-fold in the same period. There are, however, important State taxes like sales tax and taxes on transport the yields of which have grown more rapidly. The yield of State excise has however not increased proportionately and land revenue has proved stagnant between 1960-61 and 1967-68. The former is due to the policies adopted by different States. As to land revenue, a detailed examination could be made by the States themselves whether it cannot be made more elastic by suitable changes or supplemented by other productive tax devices.

3.14 After this review of the States' tax structure, we may consider some general problems of State taxation. For this purpose, it is convenient to consider the question separately in relation to the agricultural and non-agricultural sectors. Both these are subject to a number of common levies like sales tax, excise duties, etc. Studies have, however, revealed that the incidence of such common taxation on the two sectors is uneven, largely due to the consumption in kind of the agricultural sector. The agricultural sector naturally pays less *per capita* as indirect taxes than the non-agricultural sector, in which *per capita* incomes are relatively higher, but the same expenditure groups in the rural sector also pay less than their counterparts in urban areas. It is probable that, with greater monetization, more rural prosperity and better integration of the rural and urban economies, this disparity might become reduced.

3.15 But the more important difference between the agricultural and non-agricultural sectors is regarding the different systems of direct taxation to which they are subject. All non-agricultural incomes are subject to a highly progressive personal income-tax. On the other hand, the agricultural sector is, by and large, subject to relatively fixed land taxes levied at proportionate rates, though their level has varied in different regions and also according to the different times when the settlements took place. Apart from a well-designed system of suspensions and remissions, land revenue does not pay regard to the changes in the income of the landholder or his personal circumstances. The only time the land revenue rates are revised is at the time of periodical resettlement, though during this interregnum of thirty to forty years there may be rapid changes in agricultural productivity, terms of trade and farm returns. Even at the time of resettlement, the increase in land revenue is hedged in with various restrictions regarding the permissible enhancement in rates, the treatment of improvements, etc. In a number of States, resettlement has not been attempted since the depression of the nineteen thirties, owing to its time-consuming and complex nature and the general public opposition it has encountered. Some States attempted to supplement land revenue with surcharges on commercial crops, or on bigger holdings. A few States like Maharashtra have adopted a system of substantial proportionate cesses for local purposes. Some States have also levied agricultural income-tax at fairly progressive rates; but a greater part of the proceeds comes from income of plantations which are under corporate management. Direct taxation on agriculturists so far is thus out of accord with modern concepts of progressivity. Whether or not the agricultural

sector should be more lightly taxed than the non-agricultural sector may be a matter of opinion; but it is a fact that the prosperous part of the agricultural sector is now definitely under-taxed. And as agricultural incomes grow, the disparity will become even more pronounced.

8.16 The urgent need for devising an appropriate progressive tax policy for Indian agriculture is obvious. Representatives of many States have expressed the view that the development of the agricultural sector is of the utmost importance for progressing towards national prosperity. A large number of schemes involving considerable expenditure are being taken up for this purpose under the Plan. The benefits of such schemes have been improving the condition of agriculturists in many areas but the smaller cultivators and a large section of the rural community have still to face many difficulties. An extensive area in this field has still to be covered by development schemes. For this purpose greater outlay and investment will have to be undertaken in the coming years. In the context of these difficulties and the need for greater expenditure for the improvement of the agricultural sector, the problem of rural taxation requires to be considered. The more prosperous agriculturists who have derived larger benefits from such schemes would not be reluctant to contribute to the resources needed by the States so that more speedy progress could be achieved, by which they as well as the smaller agriculturists would be able to attain greater prosperity.

8.17 Some valuable light on the revenue potential of the agricultural sector could have been got from departmental statistics compiled for the administration of agricultural income-tax. The material available is, however, incomplete and inconclusive. In the first place, some important States like Andhra Pradesh, Gujarat, Madhya Pradesh, Haryana and Punjab do not levy tax on agricultural incomes, while such tax is levied in Maharashtra only on incomes above Rs. 36,000. Secondly, there is a general feeling that even in States where this tax is levied, it is inadequately enforced.

8.18 The 1961 Census of land holdings carried out by the National Sample Survey shows that, over the country as a whole, land holdings of more than 25 acres accounted for 31 per cent of the area cultivated, and that only two-fifths of the area cultivated was in holdings of less than 10 acres (*vide* Table 59). While the position in each individual State differs in this respect, and figures may have somewhat changed in the interval, these data indicate that there is a good scope for progressive land taxation.

8.19 By and large, the benefits of improvements in farming techniques, organisation and terms of trade tend to go to the larger farmers who have bigger marketable surpluses and more creditworthiness. Technical and organisational developments in the agricultural field have greatly helped the bigger farmers. The problem of rural tax policy is largely one of obtaining some part of the increased incomes of the more prosperous agriculturists for the State revenues so that the facilities which have brought prosperity to the larger farmers could be extended more widely, besides providing more amenities and services to the community in general.

8.20 The best way to secure a share of the increased margins in the agricultural sector would be to levy an effective income-tax. A tax like land revenue based on the potential ability of a factor of production has the advantage of certainty and fixity and has to be based on some objective tests like size and average productivity of land holdings. It is neutral in its incidence as regards the farmers' willingness to work and earn more. It works well in a simple society with a small degree of differentiation. But where the standards of cultivation differ widely or where there are rapid changes from year to year, such system would only be tolerated if the rate is low. In course of time as the agricultural economy loses its distinct and separate structure and farming becomes more and more a method of earning in the general economy, the separation of agricultural incomes from other incomes loses its significance. Under the present system, the division of total income into two fragments is an important factor in determining the burden of taxation, and this gives scope for considerable evasion. A single income-tax levied both on agricultural and non-agricultural incomes will have the advantage of a unified system, leaving no scope for evasion by showing greater income under less-taxed or non-taxed sections; it will also be in line with the practice of other advanced countries of the world.

8.21 There is another reason why agricultural prosperity should be taxed. A number of services, Central and State, have to be rendered to the agriculturists free or at concessional rates; rural electrification, distribution of improved seeds, pesticides, fertilisers, rural pumpsets and implements, rural credit, etc., have been, at one time or another, subsidized with a view to stimulate their use and increasing agricultural production. It is not our purpose to question the policy of subsidies and free services. It is perfectly legitimate to charge lower rates for a while to encourage the adoption of better practices and the use of services which improve agricultural production, or to subsidize handicapped farmers even as a long-term policy. However, the former objective has been largely achieved except in some areas. If it is not practicable to charge differential prices to more prosperous farmers, that is an additional reason for levy of a tax on their incomes.

8.22 The Taxation Enquiry Commission (1953-54) had recommended that the eventual aim should be to merge agricultural income with non-agricultural income and levy one income-tax. But under our Constitution, the power to levy tax on agricultural income is assigned to the States, while the power to levy taxes on income other than agricultural income is assigned to the Union. Thus, the powers to tax agricultural income and income other than agricultural income fall under two separate spheres of legislative competence. This separation of agricultural income and non-agricultural income for the purpose of taxation is perhaps unique in this country. It is unnecessary to refer to the circumstances that have led to this dichotomy. In order to make a tax on agricultural income effective, some have suggested a Constitutional amendment while others have expressed the view that the States could delegate their tax power to the Union so that it can levy tax on agricultural income along with non-agricultural income, and distribute among the States their due share relating to agricultural incomes generated in their

jurisdiction. This would depend upon an agreement being reached by the States to have recourse to Article 252 of the Constitution as in the case of estate duty on agricultural land. Apart from possible legal difficulties, it appears to us that the States may be hesitant to delegate their power to the Union unless a large national consensus is achieved in this behalf. It seems to us *prima facie* that, even without such unified levy of income-tax, the States could derive larger revenue from the tax on agricultural income if, for the purpose of determining the rate of assessment on such income, the total income of the assessee including the non-agricultural income is taken into account. Such a procedure will not be open to the objection that the State is levying tax on non-agricultural income. All that it would mean is that the non-agricultural income would be taken into account only for the purpose of fixing the rate of tax on the agricultural income as is now being done in regard to income accruing outside India in the case of non-residents under the Indian Income-Tax Act. For many years, non-residents have been taxed on their income in India at rates applicable to their "total world income". We, therefore, suggest that this line of approach may be pursued by the States.

8.23 It has been argued that while in principle an agricultural income-tax looks attractive, the proposal does not take into account practical difficulties due to peculiarities and conditions of the Indian farmer. Hitherto, income tax has been confined to a few assessees at limited centres accustomed to a highly monetized system, and even so there are many complaints of vexation and harassment. The Indian farmer, it is urged, is largely accustomed to the direct tax on land with a simple fixed liability. He is not used to keep detailed accounts or to face inquiries regarding his production, prices and farm expenditure. These difficulties, however, may not be applicable to the more prosperous agriculturists. The number of farmers who are likely to become subject to agricultural income-tax constitute only a small percentage of the farming community, and their conditions and ability are not greatly different from those of smaller assessees in urban areas. Presumptive rules regarding income per hectare from particular crop under different types of agriculture by regions would minimise inconvenience; seasonal variations in different years may be met by suitable changes in such rules. Even in the case of non-agricultural income-tax, such rules have been adopted for small or illiterate assessees.

8.24 Some States like Jammu and Kashmir and Maharashtra have pointed out that the amounts which they can raise at present from the agricultural income-tax could be more than made up by alternative levy of other taxes like land cesses or taxes on movement of goods. We however feel that the potential yield from a properly devised and enforced agricultural income-tax has been greatly under-estimated. The present proceeds are hardly an indication of the revenue potential of a proper agricultural income-tax in the near future with fast-changing techniques. Further, as compared to tax on agricultural income, the incidence of other taxes would fall in a different manner on different groups, and it is very unlikely that such incidence would prove to be progressive or obtain a suitable share of the incomes of better-off farmers. In



view of the need for more resources, it should be possible to adopt a combination of both these alternatives, which would bring in much larger sums to the State revenues.

8.25 Some State Governments, however, have stated that agricultural income-tax cannot be levied by them for administrative and other reasons, and that in any case they would like to wait till they are reasonably sure that agricultural production has turned the corner. As an alternative, we would suggest in case of such States the levy of crop taxes at differential rates and levy of progressive surcharges on larger landholdings. Both the U.P. and Bihar Taxation Enquiry Committees, which did not see any immediate scope for agricultural income taxation, have recommended the levy of surcharges. These have, however, all the defects of land revenue on which they are based, the incidence of which involves large regional disparities. We feel that such alternative levies would to some extent introduce progression in taxation of the agricultural sector.

8.26 In the last few years, several States have taken measures to exempt small landholdings from land revenue, and have given up land revenue income, wholly or partially. The types of concessions given by different States vary in their coverage and detailed application. In some cases, no distinction is made between irrigated and un-irrigated lands for purposes of exemption (*vide* Table 27). These exemptions will cost the States Rs. 78 crores during the Fourth Plan period. The economic justification urged for exemption is that the smaller farmers are living below the subsistence level and, therefore, they have no taxable surplus. In a country with low national income, trying simultaneously to develop its economy and to provide for better social welfare, it may not be entirely possible to avoid taxation of persons with low incomes. A part of land revenue may be justified on the ground that the State has to incur considerable expenditure for maintaining up-to-date records of land rights. There is enough material to prove that the cultivator greatly values this service and regards land revenue receipts as evidence in his possession of his title to land. The Uttar Pradesh Taxation Enquiry Committee has mentioned that none of the farmers giving evidence before it had demanded abolition of land revenue.

8.27 If land revenue is an important source of revenue, the question also arises as to whether the present systems of levy can be so changed as to be more equitable among different areas, and to keep in step with changes in the value of money or the profitability of crops. Periodical revisions of land revenue settlements provide one method for achieving this, but they are cumbersome and unduly costly in money and time. Such costly procedure may be worthwhile only in areas which have not been properly settled yet. As the Taxation Enquiry Commission suggested, surcharges could be levied in areas where the land revenue burden is low. It may also be examined whether some *ad hoc* increase in surcharges is not possible periodically to bring them in line with price and productivity increases. The rates of tax could also be increased on lands used for non-agricultural purposes, including industrial and commercial users, particularly in larger urban centres and developing industrial areas.

8.28 As we have said earlier, the incidence of State excise largely depends on the States' policy. Some State Governments have stated that the economic and social advantages of prohibition are sufficient to justify the loss of revenue. Unlike other measures of tax reduction, a successful prohibition policy reduces spendings on drink and adds to the incomes available for other uses. Although it would not be possible to tax additional expenditure at the same rate as on liquor, it should be possible by an elastic tax policy to make good a large part of the revenue loss. However, it would be necessary to ensure that the policy does not fail for lack of proper implementation. It seems, therefore, desirable that State Governments which have adopted a policy of prohibition may review its working and may continue it only if it is serving its real purpose.

8.29 As far as other States are concerned, they could examine the policy of their excise arrangements to ensure maximum and stable revenue and minimum evasion. Some States pointed out to us that the supply of alcohol and molasses had become difficult. If regular official supplies cannot be maintained, irregular channels are likely to spring up. Also, licensed dealers are often under temptation to deal in non-taxed illicit liquor. To make them stick to sales of supplies from official agencies a system of auctions of liquor shop licences with a small *ad valorem* tax on liquor is more helpful than a system of small licence fees coupled with a heavy *ad valorem* tax on liquor. The former system has worked successfully in Punjab. This policy has also been commended by the Uttar Pradesh Taxation Enquiry Committee.\* We feel this matter could be considered by other States with advantage.

8.30 We may now make some general observations regarding other taxes like sales tax, motor vehicles tax, entertainment taxes, etc. Tables 20 to 26 give the variations in rates of different taxes among States and indicate that a review by the State Governments of the rates levied in their States in the light of rates in different States may be useful. Apart from the question of rates, the collection and evaluation of relevant statistics so as to determine the sources of evasion and avoidance, and their magnitude and direction may help to plug the loopholes. It appears that as regards sales tax definite information about the production, sales and yield of tax in respect of individual commodities is not available. Such information would be useful for taking policy decisions. There is evidence to indicate that evasion exists to a large extent in the case of sales tax. For instance it is stated in the report of the Uttar Pradesh Taxation Enquiry Committee that the State Government raised 53 per cent more from sales tax in 1967-68 over 1965-66 without any increase in rates of tax, mainly as a result of improvement in administrative efficiency. The Kerala State Taxation Enquiry Committee estimated the evasion of sales tax on certain commercial groups on the basis of their marketable surplus and the portion which paid sales tax. It was calculated that about half of the taxable transactions in copra and its products and a similar amount of arecanut evaded tax.\*\* It is likely that

\*Report of the U. P. Taxation Enquiry Committee, p. 46, para 22 : "It is certainly surprising that a small State like Punjab can consume 120 L. P. litres of country spirit while consumption in U. P. is only 146 lakh L.P. litres".

\*\*Report of the Kerala Taxation Enquiry Committee, Appendix X, pp. 506-511.

similar problems exist in regard to other commodities and in other States also. It is important to undertake detailed investigations on such lines to ascertain the magnitude of evasion. This would help further studies to locate the likely points of evasion for working out suitable remedial measures. It has also been suggested that greater co-ordination with and supply of information by road, railway and air authorities regarding bulk movements of goods, and their consignees would be of great use to sales tax authorities.

8.31 Several States have urged before us that in determining their tax rates they had to take into consideration the rates which are in operation in other States, especially in neighbouring States. While some variations in tax rates among neighbouring States are only to be expected, large variations in some types of taxes may make resource mobilisation by the States more difficult. In land revenue and betterment duties, the effects are only psychological as there is no mobility of the object taxed. Variations in rates of taxes on sales of final consumption goods of daily use may not be of great practical consequence as the consumers cannot generally shift their site of purchase from one State to another. The possibilities of avoidance are, however, greater in the case of durable and more expensive consumer goods. The States have, therefore, arrived at an agreement regarding certain minimum rates of tax on such articles. Similar scope also exists in bulk commodities and industrial raw materials and intermediate goods. Unfortunately similar agreement has not been reached for such goods except those covered by the Central Sales Tax Act. Several States, on the other hand, offer competitive concessions and exemptions to industries in order to make it more profitable for them to be located within their borders. There is always the risk that industries might sell goods outside the State or make their purchases from outside on a consignment basis. Since local consumption is the basis of sales tax, the former practice cannot be properly objected to. But the latter can affect the basis of State taxation adversely. To promote necessary coordination in tax policies, the neighbouring States should be prepared to adjust their tax rates and for this purpose it will be useful if the Government of India can also give its assistance and support. It has been represented to us, however, that in a few cases the Centre has not given a favourable response. It is stated that the Union territory of Delhi adopted the policy that its sales tax rates must be at least one point lower than those in neighbouring States. The Uttar Pradesh Taxation Enquiry Committee has pointed out several instances where the rates in Uttar Pradesh had to be reduced in order to put its industries on a par with those in Delhi.\* We are of opinion that this matter deserves to be examined early.

8.32 The Uttar Pradesh Taxation Enquiry Committee has also remarked that in many cases transactions shown as consignments and works contracts, which are not liable to States' sales taxation, were not genuine and that they were manipulated to hide the real nature of sales transactions. It is desirable that the Government of India as well as State Governments may consider what measures could be devised to meet this situation.

\*Report of the Uttar Pradesh Taxation Enquiry Committee, pp. 64-65.

8.33 Collection of past arrears is as much an addition to current resources as tax revenues. We, therefore, tried to obtain from State Governments detailed information about their tax arrears. These amount to Rs. 186 crores (*vide* Table 17). It is likely that a large part of such arrears may not be recoverable and some of them may be the subject of appeal or revision proceedings. But the size of realisable arrears would still seem to be very large. A further analysis was made of the land revenue and sales tax arrears, which account for about nine-tenths of the total tax arrears, and it showed that these arrears had increased from Rs. 106 crores in 1963-64 to Rs. 146 crores in 1967-68. In the case of land revenue, we found that the arrears, which naturally varied from year to year due to differences in the season, were consistently more than 30 per cent of current dues in the case of a few States (*vide* Table 18). While there were no similar annual variations in the case of sales tax arrears, there were a few States with more than one-fifth of their current dues as arrears (*vide* Table 19). We feel that the magnitude of arrears can be considerably brought down by State Governments.

8.34 Non-tax revenues (excluding grants) are a significant portion of the total revenues of States accounting for more than one-third. In the case of some States like Jammu and Kashmir, Nagaland and Orissa, they account for more than one-half (*vide* Table 11). Some of these receipts, like forest revenue, are dependent on the natural resources of the States and the extent to which these are properly exploited. Some items, like departmental receipts, depend on the scale of services provided and policy decisions regarding charges to be levied for the services. These could be reviewed periodically so as to reduce the net cost of such services. Some other items like receipts from mining royalties depend on policies and decisions of the Government of India. We shall confine our remarks here to receipts of interest on loans advanced by State Governments, returns on departmental commercial schemes and dividends from investments.

8.35 The value of assets owned and amount of loans advanced by the State Governments at the end of 1968-69 totalled Rs. 8,400 crores of which Rs. 3,200 crores was loans, and Rs. 5,200 crores direct investments (*vide* Table 41). Multipurpose river schemes and commercial irrigation accounted for one-fourth of the capital outlay, and loans to Electricity Boards and investment in electricity schemes for an equal amount. Investments in industrial and economic development amounted to Rs. 500 crores, and loans to others (excluding Electricity Boards) Rs. 1,200 crores. Capital outlay on assets like roads and buildings, non-commercial irrigation, public health and agriculture accounted for another Rs. 2,200 crores.

8.36 Out of the productive capital outlay, that on multipurpose river schemes and commercial irrigation presents certain difficulties in the matter of obtaining adequate returns. In 1967-68, the losses on multi-purpose river schemes, after taking into account the interest liability, amounted to Rs. 24 crores of which Andhra Pradesh accounted for more than Rs. 8 crores. In commercial irrigation, the gross receipts did not cover even the working expenses; there was a net loss of Rs. 52 crores (*vide* Table 34) in that year after providing for interest charges.

8.37 The Committee (known as Nijalingappa Committee) which was appointed by the Government of India in 1964 to suggest ways and means of improving financial returns from irrigation projects recommended a levy at the rate of 25 to 40 per cent of the net benefits accruing due to irrigation, and where such net benefits were not ascertainable, a rate of 5 to 12 per cent of the value of gross produce. It found that the prevalent water rates were much lower. It recommended a quinquennial revision of rates in accordance with price changes. A comparison of the irrigation rates charged at present on rice, wheat and sugarcane shows wide variations between States (vide Table 23). In some States water rates which were fixed long back have not been raised in spite of higher prices and costs, and improved techniques. A statement prepared by the Ministry of Irrigation and Power estimated that if water rates on rice, wheat and sugarcane were increased to 12 per cent of the gross benefit, which is the maximum recommended by the Nijalingappa Committee, the receipts would increase to Rs. 187 crores a year (Table 60).

8.38 Losses on irrigation schemes can be due to various reasons, such as low water rates, inability or unwillingness to revise them, faulty planning, lack of ability to take follow-up measures, bad water management, etc. They can only be made more paying if remedial action is taken regarding these matters. We hope the State Governments concerned will examine the importance of such factors in the case of their schemes and take necessary steps to improve the returns from them.

8.39 The State Electricity Boards are expected to conduct their working on business principles without loss. By and large, electricity is either an item of domestic consumption or it is used by medium and large industries which should be in a position to pay for it. Rural electrification has just become important and in some States it is being subsidised directly and forms an item of the States' expenditure. The Committee on the Working of State Electricity Boards (known as Venkataraman Committee), visualised two phases during which they should improve their working and earn 9.5 per cent on their capital base, besides 1½ per cent in the form of electricity duties. According to the Committee, the immediate objective of the State Electricity Boards should be to achieve self-sufficiency which implied net receipts of 6.5 per cent on the total capital invested after meeting working expenses and provision for depreciation. This return was to be utilised for meeting interest charges (6 per cent) and for contribution to the general reserve fund (0.5 per cent). In the second phase, the Boards were expected to be able to secure an additional net return of 3 per cent on the capital base. The Committee opined that the Boards which have already achieved the first stage should take steps to realise the second phase immediately, and the remaining Boards should achieve the first stage in 3 to 5 years and the second stage within 3 to 5 years thereafter. By now, the first phase should have been completed for almost all the Boards.

8.40 The Committee visualised that in order to achieve this end, suitable upward revision of power tariff rates and maximum economy in the working expenses would be essential. An undertaking to take such measures has also been given by the State Governments to the

World Bank. In spite of this, the working of the Electricity Boards for 1968-69 shows that some Boards do not have enough surplus to pay the interest due on State loans given to them (Tables 36 and 37). Some of them have large arrears of interest to clear up. With some more effort and improved management, the Boards should be able to attain much better results.

8.41 The rates charged for electricity vary widely according to the purposes for which it is used. Electricity for domestic use attracts the highest rate. Often, the charge varies according to whether the use is for lighting or heating. Large industrial users and agriculturists are charged lower rates. The weighted average of the rates charged for separate uses varied widely from 6.4 paise per unit in Mysore to 13.4 in Punjab and 16.4 in Andhra (excluding electricity duty). In the case of some Electricity Boards making losses, the rates were lower and could *prima facie* be increased. Efforts could also be made to reduce disparity of rates in neighbouring States by consultations between States on a regional basis.

8.42 Loans to third parties other than Electricity Boards fetched interest at a low average rate of 3.7 per cent in 1967-68, the State-wise figures varying from about 5 per cent to 1 per cent. There were interest arrears of Rs. 19 crores excluding those due from displaced persons. With a firmer and more businesslike policy, higher recoveries could be expected.

8.43 Investment in Road Transport Corporations yields a good rate of return even now. The problem of subsidising them is confined only to urban areas. Other investments seem to be yielding much less. An average return of only 1.35 per cent was earned on State investments in 1968-69 (*vide* Table 42). Among the States the returns varied from 3.37 per cent to less than 1 per cent. It should be possible to step up the returns substantially. The States should be able to cover lower returns from some investments by higher returns from others, so as to realise an average return not less than the interest on their own borrowings.

8.44 In order to make certain levies more acceptable to the people paying them, the proceeds are sometimes earmarked for purposes of special interest to those on whom the incidence of such levies falls. Education is one of such purposes which can evoke a favourable response. In recent years, the policy of free and compulsory education is being extended to cover children beyond the primary stage and tuition fees are being exempted on a large scale. In one State education even at the University level is free. The Constitutional directive requires provision of free and compulsory education for children upto the age of fourteen years. Expenditure on education is bound to increase particularly if the recommendations of the Education Commission regarding minimum salaries of school teachers are implemented. Education for children upto fourteen is an objective in which every citizen would be interested, and the improvement of the pay of teachers would also find general support. Some States already levied education cess on land revenue and tax on property. We suggest that other States may also consider the possibility of taking similar action.

## CHAPTER 9

### SUMMARY OF RECOMMENDATIONS

9.1 Our recommendations to the President in regard to devolution of taxes and grants-in-aid of the revenues of the States are set out below:—

#### I—Income-tax :

- (a) In respect of distribution of the unadjusted balance of advance tax collections upto the year 1966-67:
  - (i) Out of the amount of such advance tax collections, as determined by the Comptroller and Auditor-General of India, a sum equal to  $2\frac{1}{2}$  (two and a half) per cent thereof be deemed to be the portion which represents the proceeds attributable to Union territories, as constituted immediately prior to the Punjab Reorganisation Act, 1966;
  - (ii) The percentage of the amount of advance tax as determined by the Comptroller and Auditor-General of India except the portion attributable to Union territories, to be assigned to the States should be 75 (seventy-five) per cent;
  - (iii) The distribution among the States *inter se* of the share assigned to the States should be made on the basis of the percentages recommended by the Fourth Finance Commission, with appropriate adjustments in regard to the share of reorganised Punjab and Haryana States and Union territories in accordance with the Punjab Reorganisation Act, 1966;
  - (iv) The share of each State should be paid to the State Government in three equal annual instalments during the years from 1971-72 to 1973-74.
- (b) In respect of distribution between the Union and the States of the net proceeds of income-tax in the years 1967-68 and 1968-69, there should be no change in the distribution as prescribed in the Constitution (Distribution of Revenues) Order, 1965, in the event of the said net proceeds being certified by the Comptroller and Auditor-General of India on the revised basis;
- (c) In respect of the distribution of net proceeds of income-tax in the financial years from 1969-70 to 1973-74;
  - (i) Out of the net proceeds of taxes on income in each financial year, a sum equal to 2.6 per cent thereof be deemed to be the portion which represents the proceeds attributable to Union territories;
  - (ii) The percentage of the net proceeds of taxes on income, except the portion which represents proceeds attributable to Union territories, to be assigned to the States should be 75 (seventy-five) per cent; and

(iii) The distribution among the States *inter se* of the share assigned to the States in respect of each financial year should be made on the basis of the following percentages:—

State	Percentage
Andhra Pradesh . . . . .	8.01
Assam . . . . .	2.67
Bihar . . . . .	9.99
Gujarat . . . . .	5.13
Haryana . . . . .	1.73
Jammu and Kashmir . . . . .	0.79
Kerala . . . . .	3.83
Madhya Pradesh . . . . .	7.09
Maharashtra . . . . .	11.34
Mysore . . . . .	5.40
Nagaland . . . . .	0.08
Orissa . . . . .	3.75
Punjab . . . . .	2.55
Rajasthan . . . . .	4.34
Tamil Nadu . . . . .	8.18
Uttar Pradesh . . . . .	16.01
West Bengal . . . . .	9.11
TOTAL . . . . .	<u>100.00</u>

### 11.—Union Excise Duties :

- (a) During each of the years 1969-70 to 1971-72 a sum equivalent to 20 (twenty) per cent. of the net proceeds of Union duties of excise on all articles levied and collected in that year, excluding special excises, regulatory duties and duties and cesses levied under special Acts and earmarked for special purposes, should be paid out of the Consolidated Fund of India to the States;
- (b) during the years 1972-73 and 1973-74, a sum equivalent to 20 (twenty) per cent. of the net proceeds of Union duties of excise on all articles levied and collected in the respective year, including special excises, but excluding regulatory duties and duties and cesses levied under special Acts and earmarked for special purposes, should be paid out of the Consolidated Fund of India to the States; and