

MERGER OF ADDITIONAL DUTIES OF EXCISE WITH BASIC DUTIES OF EXCISE

8.1 Under paragraph 7 of the terms of reference we are required to examine the feasibility of the merger of Additional Duties of Excise in lieu of Sales Tax with Basic Duties of Excise and evolve a suitable formula for allocating a part of the duties of excise in respect of goods described in column 3 of the First Schedule to the Additional Duties of Excise (Goods of Special Importance) Act, 1957, for distribution among the States. We did not make any recommendation on the feasibility of the suggested merger in our first report as we wanted to examine the issue in greater depth and complete our discussions with all the States. We were also keen that before we considered this matter, the outstanding issues relating to the operation of the tax rental arrangement should be sorted out to the extent possible in order to create an environment for a dispassionate approach to the issue by the States. We have since completed our discussions with the States and we are now better aware of their views on this matter.

8.2 The concept of merger was mentioned in the Long Term Fiscal Policy (LTFP) announcement of the Central Government. As a measure of simplification of the assessment procedures under Central Excise law, it was suggested in the policy document that Special Excise Duties which were levied as a percentage of the amount of basic duties should be merged with them. The policy document also indicated that the merger of additional duties with basic duties was desirable, though not feasible immediately. There was a commitment to refer the matter to the next Finance Commission. It would be worth mentioning here that the proposed merger of Basic and Special Excise Duties was carried out through the budgetary changes of 1986-87 and 1987-88. In the Budget of 1988-89, however, the Special Excise Duties were brought back as a separate levy.

8.3 Let us turn now to the views of the States. All the States except Arunachal Pradesh, Mizoram, Meghalaya and Goa have opposed the concept of merger. Arunachal Pradesh, Mizoram and Goa are erstwhile Union Territories and the first two are not levying even Sales Tax. States like Andhra Pradesh, Bihar, Haryana, Tamil Nadu and Uttar Pradesh opposed the very inclusion of this subject in the terms of reference assigned to us. The opposition was based on the ground that since Additional Duties of Excise were levied pursuant to the decision of the National Development Council (NDC) in 1956, the matter, in all fairness, should have been first referred to it. Maharashtra also questioned the competence of the Union Government to refer the question to the Finance Commission unilaterally, without the concurrence of the States or the endorsement of NDC. States like Andhra Pradesh, Bihar, Gujarat, Madhya Pradesh and West Bengal also apprehend that the proposed merger would remove completely the identity of Additional Duties of Excise as a separate levy and this would prejudice the interests of the States. Gujarat, Orissa, and Punjab apprehend that the inherent right of the States to re-impose Sales Tax on any of the commodities would be lost totally in the event of the merger.

8.4 Much of the opposition against merger stems from the manner in which the tax rental arrangement was administered in

the past. The States referred particularly to the decision of the National Development Council in December, 1970, under which, within a period of two to three years, the proceeds from Additional Duties of Excise were scheduled to attain a level of 10.8 per cent of the value of clearances and the ratio between the yields from Basic Duties of Excise and Additional Duties of Excise on the three commodities was intended to be brought up to 2:1. While the latter commitment was fulfilled in recent years, the first, which was required to be done within, say, three years of the meeting of the National Development Council in 1970, still remains unrealised. There has been a further complaint that, apart from the fact that the Government of India did not fulfil its promises in regard to realisations from this levy, it had unduly expanded the coverage of the goods by resorting to definitional changes precluding thereby larger areas from the levy of Sales Tax. Many commodities were also subjected to 'nil' rate of duty. These commodities, therefore, were free not merely from the levy of Additional Duties of Excise but they also escaped the liability to Sales Tax which the States were prevented from imposing for fear of forfeiting their share in the proceeds from Additional Duties of Excise. In the context of their unhappy experience with the implementation of tax rental arrangement in the past, some States went to the extent of urging that the arrangement for the levy of Additional Duties of Excise in lieu of Sales Tax should be scrapped altogether and *status quo ante* restored.

8.5 Most of the States also felt strongly about the low yield from Additional Duties of Excise. Punjab wanted to be compensated for the delay in achieving the incidence of 10.8 per cent of the value of clearances. Andhra Pradesh complained that its Sales Tax revenue increased sixty nine times during 1959-60 to 1986-87 against a three-time growth in its share of Additional Duties of Excise. The position is not much different in the case of Tripura as well, where, according to the State Government, the increase in revenues from Sales Tax in the last 10 years was sixteen times whereas the same from Additional Duties of Excise was three times. Haryana recited a similar experience and, in fact, suggested the scrapping of this tax rental arrangement. From our discussions with the States and also from the memoranda received on this matter it was clear that almost all the States - barring a few exceptions - were opposed to the idea of merger.

8.6 As stated before, the issue of merger has been referred to us with a view to bringing about a certain measure of simplification of and streamlining in the assessment procedure under the Central Excise law. The case for the merger, however, gets substantially weakened when one takes into consideration the fact that the Union Government itself has not made any serious effort to reduce the multiplicity of levies. The Special Excise Duties which were merged with Basic Duties of Excise in 1986-87 and 1987-88 were brought back as a separate levy in 1988-89. The revival of Special Excise Duties as a separate levy after its merger in earlier years robs the concept of merger of its rationale as a tax reform measure. One cannot also ignore that even if the merger is effected, separate imposts in the form of cess would still be leviable on sugar and bidies by virtue of the

Sugar Cess Act, 1982, and the Bidi Workers Welfare Cess Act, 1976, for raising resources for the development of the sugar industry and the welfare of bidi workers, respectively. In respect of fabrics, there would be not one, but two other levies, namely, Handloom Cess and the Additional Duties of Excise (Textile and Textile Articles). We note that while the Eighth Finance Commission recommended the containment of these cesses and the LTFP proclaimed the Government's intention to reduce their number no concrete step appears to have been taken in this regard.

8.7 As the tax rental arrangement was brought into being with the consent of the States, any major modification in the arrangement should also be brought about with the consent of all the parties. But almost all the States have strongly opposed the issue of merger. As a matter of fact, the proposal for merger is perceived by the States as a threat to their financial interests and a further irritant in the Centre-State fiscal relations. The reservations of the States on this point were also expressed at the meeting of the Chief Ministers on financial matters convened by the Union Government on February 9-10, 1989, at New Delhi. We, therefore, do not recommend the merger of Additional Duties of Excise with Basic Duties of Excise.

8.8 We would like to now touch upon the issue of the incidence of Additional Excise Duties. The incidence of Additional Excise Duties should be brought up to 10.8 per cent by

the end of 1989-90. We have been informed by the Ministry of Finance that the incidence had reached 10.7 per cent at the end of 1988-89. We would expect that the committed level of 10.8 per cent would be actually achieved by the end of 1989-90. We recommend that during the report period, if in any year the ad valorem incidence of Additional Duties of Excise falls short of the level of 10.8 per cent of the value of clearances, the shortfall should be made good (as soon as accounts are available) by Government of India by providing equivalent amount by way of grant-in-aid to be distributed amongst the States and the Union Territories in the same manner as worked out for sharing the proceeds in paragraph 5.20.

8.9 As a follow-up of our recommendation in paragraph 7.16 of our first report, the Central Government has asked the National Institute of Public Finance and Policy to conduct a study to assess the revenue loss suffered by the States on account of exemptions of Additional Duties of Excise allowed by the Central Government.

It has also undertaken to review these exemptions to ascertain whether there is adequate justification to continue them. The feasibility of converting the rates of Additional Duties of Excise which are now specific into ad valorem is also under examination by the Central Government. We have no doubt that appropriate action, in due course, will be taken by Government of India to redress the grievances of the States.