

Tax luxury consumption, not incomes

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When radical reforms take place, no change should be made at least for some time unless found absolutely necessary so that the new structure can stabilise and economic agents get time to adjust. That does not seem to be happening in India. The tax system that was put in place with the reforms carried out in the nineties as part of the economic reform programme undergoes changes almost every year, not all of which seem called for.

There is no denying the fact that the main object of taxation is to collect revenue for the larger public good. Other countries of the world, specially some European ones, have a personal rate of income tax which is much higher than the 30 per cent rate in India.

However, the striking difference in the Indian context is the fact that the government provides no social security for the unemployed, the retired, the uneducated or those who are terminally ill. While education and medical facilities are available in the urban areas, the quality of both falls much below desired standards. Our implementation of various social schemes are so hollow, opaque and non-visible that the public at large does not want to feel cheated or look foolish by paying the actual taxes when they know that there is no monitoring mechanism that ensures proper utilization of public money. We pay road tax but how good are our roads!

The scheme for the unemployed announced from time to time have only scratched the surface of the problem with substantial amounts not reaching the intended target population. Indians have, therefore to provide for their old age, their medical needs, education of their children, and marriage expenses of daughters. In this environment, far from there being a stigma on tax evaders, such practice is socially accepted and approved in every strata of Indian society. Therefore it is imperative that the policies of the budget should be in sync. with the social requirements of the citizens.

Deductions, exemptions and benefits:

The Finance Minister's has reduced the deductions available u/s 88.

It is only in the case of the dwindling class of honest tax payers who declare their income truthfully, that the question of claiming deductions, exemptions and benefits arises.

A perusal of the provisions of the permissible deductions would bring forth two important facts.

First, a very small quantum of deduction is available to each tax payer considering the level of investment he has to make. It is obvious that the lower the rate of tax, the less is the impact on the tax revenues of the government.

Second, all the aforesaid benefits pertain to personal needs, like medical, education, old age pensions, etc. By removing or reducing these tax benefits there would be a little impact on revenue collection, but it would leave a bitter taste in the mouth of honest taxpayers.

The Finance Minister's desire to raise more revenue has to be in sync with the need of millions of tax payers who wish to perform their duties as law abiding citizens. Savings are not only for the benefit of the individual but form the bedrock of a nation's long-term investment policy.

What to tax?

The social approach of the government has to ensure equity and it is true that income tax is an important tool. Higher income tax on higher income group and vice-versa. Whereas the author differs in the philosophy altogether. For a change, think of equity in consumption

The Finance Minister should tax luxury consumption, instead of incomes and this can be done by lowering income tax and raising excise and customs duties. That will be both equitable as well as pro-growth

The choice of tax should be made on the three criteria of equity, investment and simplicity.

Inequity in incomes is undesirable and non-cohesive socially only if used for consumption. It is good if it is used for investment. It does not matter to the poor if the rich have huge bank balances with which they put up factories, as it leads to more jobs.

The problem with FM's approach is that though equitable, income tax is consumption-friendly and complicated. A complicated tax collection system leads to the generation of more black money and more consumption. The country has to increase investment while maintaining equity.

It is possible to impose high duties on cars and chocolates while maintaining them at low levels on match boxes and inexpensive paper used for copy books. Such excise would be equitable. The difference is that this equity would be at the point of consumption, not income.

The rich who earn and consume will pay more taxes, those who earn and invest will pay less. Would it not be a nation building exercise?