

Tax Determinant Studies and Socio-Political Variables : A Suggested Methodology

P. Mishra

The "displacement effect" hypothesis may be one of the relevant aspects to consider while dealing with the tax revenues or public expenditure over a long period of time. This will give proper weightage to the 'Shift' and 'Changes in elasticity' if any, in the revenue and/or expenditure functions.

In this paper, therefore, an attempt has been made to examine whether (or not) the inclusion of the "displacement effect" hypothesis in the determinant studies would provide better explanation to the growth of tax revenue (or expenditure) and would suggest a better alternative forecasting model. Data used in the study pertain to Union Tax Revenue in India for a period of thirty years. Our findings suggest that revenue expenditure functions give a "better fit" when socio-political variables of global and non-global nature are taken into account.

Section I

Studies relating to public revenues and expenditures have emphasised mostly the normative theories of Public Economics. Discussions about an ideal tax structure, taxable units, definition of income and other similar topics have attracted much attention of the researchers in the field of public revenues. There has been a relative neglect of positive analysis as compared to the normative approach particularly in the field of tax revenues. So far as the positive analysis in the field of tax revenue is concerned much emphasis has been put on the studies relating to effect of various kinds of taxes on distribution, incentives relating to work effort, savings, investments etc. However, a few studies have investigated how in fact the tax structure of a country has behaved over time and what relationship the growth of tax revenues has with (a) different indicators of economic development and (b) the socio-political development in and outside the country.

Amongst the behaviouristic approaches to public expenditures and revenues, the determinant studies and other similar studies are worth mentioning. However, most of the determinant studies have been in the areas of government expenditures based on cross-section data 1/. These studies have tried to explain the inter-state/inter-country variations in the level of government expenditure in different countries by incorporating different economic variables e.g., per capita income, density of population, urbanisation, money supply etc.2/. A very few determinant studies have taken socio-political factors into account while incorporating different economic variables. In other words, in a multivariate determinant study inclusion of socio-political factors e.g., "Social Upheavals" as factors responsible for the growth of tax revenues (or expenditure) is not customary. Strictly speaking, a social upheaval (a world war, a bilateral war, changes in political ideologies etc.) is as relevant as other explanatory variables like different indicators of economic development which are usually included in a traditional determinant analysis. It may be argued that determinant studies are basically used for forecasting purposes and since social