REPORT

OF THE

INDIRECT TAXATION ENQUIRY COMMITTEE

PART II

JANUARY, 1978

GOVERNMENT OF INDIA
MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)

MINISTRY OF FINANCE
DEPARTMENT OF REVENUE
INDIRECT TAXATION ENQUIRY COMMITTEE

. . . .

To

Shri H. M. Patel,
Finance Minister of India,
NEW DELHI.

Sir,

We, the members of the Indirect Taxation Enquiry Committee, submit herewith Part II of our Report.

As you may recall, we had submitted Part I of our Report in October, 1977, outlining in a condensed form our main conclusions and recommendations and the reasons behind them. We have since had time to analyse the results of the various studies which we had initiated and also to examine the impact of indirect taxation on a selected number of important industries as well as products of consumer interest. During the course of our enquiry, we had received several suggestions from men of eminence and representatives of trade and industry on structural as well as procedural problems. After taking into account the results of the studies as well as the suggestions made, we have, in Part II of our Report, presented our final conclusions and recommendations more fully than we had done in Part I.

The task assigned to us has indeed been a complex one. We have had to take into account several issues. Those involving political judgment, we have left for the Government to consider. What we have given our attention to is the task of restructuring the indirect tax system in the country and finding ways and means of eliminating the distortions that have arisen over the years. While basically our approach has been to cover all the relevant aspects of rationalisation of indirect tax structure, we have avoided going into certain areas for the reason that some Committee or the other had studied them in the recent past.

We hope that our recommendations will help Government in bringing about a reform in the indirect tax structure that would be enduring as well as acceptable to the community at large.

Yours faithfully,

Sd/-
(L.K. Jha)
Chairman

Sd/- (G. B. Newalkar) Member	Sd/- (J. Sen Gupta) Member	Sd/- (K. Narasimhan) Member-Secretary
Sd/- (M. V. Arunachalam) Member	Sd/- (Raja J. Chelliah) (Member	Sd/- (S. S. Marathe) Member

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INTRODUCTION

We have, in Part I of our Report, set out, in a condensed form, our main conclusions and recommendations. In Part II of the Report, we now proceed to make a fuller and more detailed presentation of our findings and proposals for reform, based on the results of the research studies which we had instituted, and the views put to us by Departments of the Central Government as well as State Governments, by non-official bodies representing trade, industry and labour and by economists and other men of eminence who have given us the benefit of their advice. In this Part we also present a more detailed analysis of the impact of indirect taxation on certain key sectors of the industrial economy which could not be included in Part I of our Report. Our attempt has been to make the presentation self-contained and to obviate as far as possible the necessity to refer back to Part I of the Report. Finally, for purposes of future reference, we have in the Appendix, which appears as a separate volume, included certain facts and figures as well as other material, which we have collected and made use of in the course of our study of the issues assigned to us in our following terms of reference:

(i) To review the existing structure of indirect taxes — Central, State and Local, in all its aspects.

(ii) To examine the role of indirect taxation in promoting economic use of scarce resources.

(iii) To examine the structure and levels of excise duties, the impact of excise duties on prices and costs, the cumulative effect of such duties, their incidence on various expenditure groups, the scope for widening the tax base and increasing the elasticity of the system.

(iv) To examine the feasibility of adopting some form of Value Added Tax in the field of indirect taxation where appropriate and, if found feasible, to suggest the appropriate stage to which it should be extended having regard to Indian conditions, i.e., whether the stage of coverage should be manufacturers, wholesalers or retailers.

(v) To examine whether and how far it would be advisable to assist any particular industry or particular sectors of an industry by grant of concessions in indirect taxes; in doing so, the Committee will doubtless take into account all the normal canons of taxation, and the balance of administrative convenience. In those cases where these devices are found to be advisable, to suggest norms for the same.

(vi) To examine the structure and levels of import duties from the point of view of import trade control, protection to indigenous industry and pricing of indigenous products and suggest changes, if necessary.

(vii) To advise the Government on the steps to be taken to implement the recommendations made, including changes in the administrative and organisational set up.

(viii) To suggest changes, if any required, in the Constitution and in the related taxation statutes, for the implementation of the changes suggested in the tax structure and having regard to the revenue needs of both the Centre and the States.

(ix) To make any other recommendations germane to the enquiry.

(x) To consider the interaction and the proper balance between indirect and direct taxes in our tax structure while examining the role of indirect taxation in mobilising resources.

2. The inaugural meeting of the Committee was held on the 24th July, 1976 when the Finance Minister addressed the Chairman and Members of the Committee. A copy of the Finance Minister's inaugural address is reproduced in Appendix 1.

3. Immediately after the inaugural meeting of the Committee held on the 24th July, 1976, we prepared a nine-point questionnaire (as in Appendix 2) which was issued to associations of all-India

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status representing trade, industry, labour and co-operative interests. The questionnaire was kept deliberately brief because we felt that it would be better to let those addressed make their own representations within the broad framework of the issues posed to us than to get their response to specific points of detail. Simultaneously, the fullest publicity was given to the questionnaire through the press and a general invitation issued to individuals, associations, etc., to send their views to the Committee.

4. Separate letters were addressed to Central Ministers, the Deputy Chairman, Planning Commission, and State Chief Ministers (Governors in some States) as well as to eminent economists, public men and academicians, inviting their views and suggestions about the kind of changes that they would like to see in the structure of indirect taxes. The Committee had the benefit of discussions with representatives of Chambers of Commerce, industrial and labour organisations, individual scholars of repute, some senior officials of Central Government (including those of the Department of Central excise and customs) and a number of Chief Ministers and representatives of State Governments. For this purpose, meetings were held with venues at New Delhi, Srinagar, Bombay, Madras, Trivandrum and Calcutta. Apart from these, the Committee held a number of internal meetings. Part II of the Report was finalised in the last week of December, 1977.

5. In response to our invitations, we received a very large volume of evidence and we are confident that we have heard all points of view as to what would constitute a desirable indirect tax system in the country. The names of all those who responded to our questionnaire or the press note and sent their views in writing are given in Appendix 3A. The names of Central Ministries and State Chief Ministers/Governors who sent a written reply to our communications are shown in Appendix 3B. This Appendix also includes the names of the State Governments/Union Territory Administrations who sent replies to the supplementary questionnaire (included in Appendix 2) touching State taxes. A list of all those who tendered evidence before the Committee at various places is given in Appendix 4.

ACKNOWLEDGEMENTS

6. We should like to take this opportunity to acknowledge gratefully the assistance we have received from all those who have favoured us with their views and advice. One of the things which has impressed us throughout our enquiry has been the widespread recognition of the fact that Government's requirements of revenue for general administration as well as resources for development must be met. The recurring theme in the representations made to us by responsible Chambers of Commerce has been not for a reduction in the overall tax burden as such but that the tax system should be geared to the augmentation of Government revenues without the necessity of frequent changes in the rates of taxation and without causing distortions and side effects which impede industrial growth. Even where some industries pleaded for a lowering of the rates, they have often sought to justify it on the ground that it would, in fact, mean higher revenues on account of higher production and sales.

7. The Committee is grateful to the Directorate of Tax Research of the Central Board of Excise and Customs which provided the Committee with necessary secretarial assistance and useful background material during the initial period of the working of the Committee as well as the Directorate of Statistics (Central Excise and Customs) who constantly made available to us statistical and other relevant data which we needed for our work.

8. Our special thanks are due to Shri Asit Chandmal, Director (Finance) of TELCO who, in an honorary capacity, functioned as a Consultant to the Committee and conducted for us certain very useful studies pertaining to the road transport industry and automobile industry.

9. We also gratefully acknowledge the co-operation and assistance we have received from the Central and State Governments at all levels. It was refreshing to find that the officers of the customs and excise departments as well as those concerned with sales tax administration were ready to suggest changes rather than resist them. For reasons of space and to avoid any possible embarrassment we have not been able to refer individually to the suggestions made to us. But we have, in formulating our recommendations, given them the fullest weight and consideration. We should also like to thank the State Governments concerned for the hospitality and courtesies extended to the Committee during our visits to various States. A number of Indian Embassies abroad have also greatly helped us in our study of the working of the VAT in different countries.

10. The Member-Secretary of the Committee, Shri K. Narasimhan, with his wide experience of administration of indirect taxes and deep knowledge of their tariff structure, gave to the Committee the kind of insight into the issues it was considering, which it would have taken a lot of time and research to obtain otherwise. In this task he was assisted by a competent team comprising the Secretariat under him. Shri M.S. Sivaramakrishna's detailed knowledge of State taxes and understanding of the legal and Constitutional issues in the sphere of indirect taxation were of tremendous value to us. S/Shri B.K. Agarwal, P.N. Malhotra, D.K. Acharyya and P.R.V. Ramanan initiated, at our instance, detailed studies to bring out the impact of the taxation of various inputs on different sectors of the economy. The officers of the Secretariat participated in all our deliberations and we greatly benefited from their comments and criticism which we invited them to make freely. As they go back to their respective responsibilites in the department to which they belong, we hope their association with the work of the Committee will be of some help to them. Finally, Shri N. Subramanian who was looking after the administrative arrangements deserves our special thanks because, within a very short period of time, he was able to make what was a wholly new set up function with the smoothness and efficiency of an old established one. Without naming the other members of the Secretariat staff individually, we would only say that the very large volume of typing and tabulation which the Committee's work entailed was handled by them with speed and thoroughness.

11. Finally, we must acknowledge our indebtedness to previous studies pertaining to our field of enquiry. The first and the foremost amongst them is the Report of the Taxation Enquiry Commission (1953-54) headed by Prof. John Mathai. We have made frequent references to the Taxation Enquiry Commission in our Report. Since then there has been two comprehensive reviews of direct taxes by two Committees respectively headed by Shri Mahavir Tyagi and Justice Wanchoo. Different aspects of indirect taxation have been studied by the Chanda Committee in 1963, the one-man Committee of Shri Bhoothalingam in 1965, the Customs Study Team headed by Shri D. N. Tiwari in 1967 and the examination of the Self Removal Procedure by a Committee headed by Shri Venkatappiah. In our discussion of procedural reforms we frequently refer to the recommendations of the Customs Study Team as well as the Venkatappiah Committee. We feel that considering the impact which the structure of indirect taxes inevitably has on the fast changing economic scene, it would be desirable to have a fresh comprehensive look on the structure of indirect taxation, or better still, on our taxation system as a whole, undertaken by a Taxation Enquiry Commission once in every ten years or so.

CHAPTER 1

INDIRECT TAXES AS A SOURCE OF REVENUE

1.1 Our terms of reference relate to the study of indirect taxes. There is no legal definition of indirect taxes in India. The Constitution of India allocates the taxing powers between the Union and the States through precise entries. In doing so, our Constitution closely follows the pattern of division of tax powers between the Centre and the erstwhile provinces established by the Government of India Act, 1935. The extent of the power, in regard to imposition of taxes, enumerated in List I and List II of the Seventh Schedule to the Constitution are detailed in the Table below:

INDIRECT TAXES LEVIED BY THE UNION AND THE STATES

TABLE 1 - POWERS OF TAXATION - UNION AND STATES

S. No.	No. of Entry in the Seventh Schedule.	Description
(1)	(2)	(3)
Union Field		
List I		
1.	82	Taxes on incomes other than agricultural income
2.	83	Duties of customs including export duties
3.	84	Duties of excise on tobacco and other goods manufactured or produced in India except — (a) alcoholic liquors for human consumption; (b) opium, Indian hemp and other narcotic drugs and narcotics, but including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry
4.	85	Corporation tax
5.	86	Taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies
6.	87	Estate duty in respect of property other than agricultural land

(1)	(2)	(3)
7.	88	Duties in respect of succession to property other than agricultural land
8.	89	Terminal taxes on goods or passengers, carried by railway, sea or air; taxes on railway fares and freights
9.	90	Taxes other than stamp duties on transactions in stock exchanges and future markets
10.	91	Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipts
11.	92	Taxes on the sale or purchase of newspapers and on advertisements published therein
12.	92A	Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce
13.	97	Any tax not enumerated in List II or List III of the Seventh Schedule
State Field		
List II		
1.	45	Land revenue, including the assessment and collection of revenue, the maintenance of land records, survey for revenue purposes and records of rights, and alienation of revenues
2.	46	Taxes on agricultural income
3.	47	Duties in respect of succession to agricultural land
4.	48	Estate duty in respect of agricultural land
5.	49	Taxes on lands and buildings
6.	50	Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development

(1)	(2)	(3)
7.	51	Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India: (a) alcoholic liquors for human consumption; (b) opium, Indian hemp and other narcotic drugs and narcotics; but not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry
8.	52	Taxes on the entry of goods into a local area for consumption, use or sale therein
9.	53	Taxes on the consumption or sale of electricity
10.	54	Taxes on the sale or purchase of goods other than newspapers subject to the provisions of entry 92A of List I
11.	55	Taxes on advertisements other than advertisements published in the newspapers (and advertisements broadcast by radio or television)
12.	56	Taxes on goods and passengers carried by road or on inland waterways
13.	57	Taxes on vehicles, whether mechanically propelled or not, suitable for use on roads including tramcars subject to the provisions of entry 35* of List III
14.	58	Taxes on animals and boats
15.	59	Tolls
16.	60	Taxes on professions, trades, callings and employments
17.	61	Capitation taxes
18.	62	Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling

*Entry 35 of List III relates to mechanically propelled vehicles including the principles on which taxes on such vehicles are to be levied.

(1)	(2)	(3)
19.	63	Rates of stamp duty in respect of documents other than those specified in the provisions of List I with regard to rates of stamp duty

1.2 The residual powers of taxation belong to the Union. This means that even if a tax is not specifically included either in List I or List II, it can be imposed by Parliament.* Another point to note is in respect of Union Territories, Parliament has the power to impose a tax included in the State List.

1.3 In the absence of a legal definition of indirect taxes, we have to fall back upon the economic definition of direct and indirect taxes. As a starting point, one may refer to the classic definition of John Stuart Mill in his "Principles of Political Economy":

> "Taxes are either direct or indirect. A Direct tax is one which is demanded from the very persons who, it is intended or desired, should pay it. Indirect taxes are those which are demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another; such as the excise or customs."

This definition has been relied on in judicial findings also. For example, Lord Cave in the City of Halifax V. Fairbanks' Estate (1928) A.C. 117 said:

> "Thus taxes on property or income were everywhere treated as direct taxes; and John Stuart Mill himself, following Adam Smith, Ricardo and James Mill said that a tax on rents falls wholly on the landlord and cannot be transferred to any one else. On the other hand, duties of customs and excise were regarded by every one as typical instances of indirect taxation.
>
> xxx xxx xxx
>
> The imposition of taxes on property and income, of death duties and of municipal and local rates is, according to the common understanding of the term, direct taxation, just as the exaction of a customs or excise duty on commodities.....would ordinarily be regarded as indirect taxation although new forms of taxation may from time to time be added to one category or the other in accordance with Mill's formula as a ground for transferring a tax universally recognized as belonging to one class to a different class of taxation....."

1.4 Several later economists have expressed views which are in the nature of a further evolution of the lines of thought propounded by J.S. Mill, while others have contended that on economic grounds no clear-cut division can be made between direct and indirect taxes. Nor can the

*The one exception to this general rule is the State of Jammu and Kashmir which has a special position with the residual powers vested in the State.

intention of the Government be a dependable criterion because it may not be fulfilled in practice. It is easy enough to say that a tax should be classified as indirect if it can be passed on to someone else, but it is difficult to identify taxes that cannot be passed on under any circumstances. Equally, the burden of taxes which are normally assumed to be passed on may rest with the legal tax-payers themselves under given conditions. Thus, if the supply of a commodity is highly inelastic, while the demand is quite elastic in the range of the tax inclusive price, the tax on that commodity cannot be shifted. On the other hand, part of the taxes on company profits may be shifted under given conditions or in the long run. Several empirical studies have testified to this possibility. For these reasons, while there is still the presumption that by and large taxes on commodities are shifted, modern economists prefer to use the terms "taxes on commodities and services" and "taxes on income and wealth" rather than the terms "indirect" and "direct" taxes. For our purposes, without going into the niceties of the economic debate, we treat the taxes covered by serial numbers 2, 3, 8, 9, 10, 11 and 12 of the Union List and serial numbers 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 18 and 19 under the State List in the table given in para 1.1 above as indirect taxes. We have, however, confined our discussion to the major indirect taxes, namely, duties of customs and excise and taxes on sales, and the entry of goods into a local area, popularly known as octroi.

1.5 Of the Union indirect taxes, receipts from customs duties are exclusively retained by the Union Government. In respect of the other indirect taxes, the Constitution contains provisions under which:

DISTRIBUTION OF INDIRECT TAX REVENUES BETWEEN THE UNION AND THE STATES

(i) certain duties though levied by the Union are collected and appropriated by the States (e.g. stamp duties and excise duties on medicinal and toilet preparations containing alcohol, opium etc., falling under entry 84 of the Union List) (Article 268):

(ii) certain taxes and duties though levied and collected by the Union are assigned to the States (e.g. terminal taxes on goods or passengers carried by railway, sea or air; taxes on railway fares and freights; taxes other than stamp duties on transactions in stock exchanges and future markets; taxes on the sale or purchase of newspapers and advertisements published therein and taxes on sale and purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce) (Article 269):

(iii) Union excise duties (other than duties of excise on medicinal and toilet preparations referred to in (i) above), though levied and collected by the Union, are distributed between the Union and the States.

1.6 In respect of all the duties and taxes levied and collected by the Union whose proceeds are either assigned or may be assigned to the States, the principles of distribution are determined by the Finance Commissions from time to time. Union excises are at present distributed between the Centre and the States in the ratio 80:20. The tax on the sale or purchase of goods in

the course of inter-State trade or commerce is, under the Central Sales Tax Act, levied, collected and retained by the State from which the goods are sold.

1.7 Generally, no taxes (direct or indirect) have been reserved for local bodies in the Constitution. However, the implication of Article 276 is that the taxes on professions, trades and callings or employments are for the benefit of the State as well as local authorities, municipalities, district boards, etc. The States on their own may assign any of the taxes in the State List, either in whole or in part, to local bodies. The two indirect taxes which have been assigned to local bodies by many States are octroi and terminal taxes. In a few States, the proceeds of entertainment taxes have also been assigned to local bodies within whose jurisdiction they are collected.

GROWTH IN TAX REVENUES

1.8 Table 2, included as annexure to this Chapter, gives the combined tax revenues of the Centre, States and Union Territories since 1950-51 as well as their break-up under direct and indirect taxes. As may be observed from the Table, total tax revenues have recorded an almost twenty fold rise during the period 1950-51 to 1976-77, having increased from Rs.526.57 crores in 1950-51 (before the beginning of the First Five Year Plan) to over Rs.12,076 crores in 1976-77. Another noticeable feature is that the average rate of growth in tax revenues, of about 25 per cent, in the period 1960-61 to 1970-71 (which rate has been maintained in the period 1970-71 to 1976-77) was much higher than the average growth of about 11.5 per cent recorded in the period 1950-51 to 1960-61. This sharp step-up in the tempo of taxation came about as a result of the efforts to mobilise greater resources for promoting higher rates of growth in the Third Plan and to provide for strengthening of the country's defences in the wake of repeated aggressions on our territory.

GROWTH OF INDIRECT TAXES

1.9 The above mentioned Table also brings out the fact that in the augmentation of revenues from year to year indirect taxes have been playing an increasingly important role. Their share in total tax revenues has risen steadily from 63.2 per cent in 1950-51 to 70.2 per cent in 1960-61, to 78.8 per cent in 1970-71 and to 79.3 per cent in 1976-77. The relative shares of the major direct and indirect taxes in the total tax revenues of the Centre and States in 1976-77 (Revised Estimates) are set out in the following Table:

TABLE 3 - RELATIVE IMPORTANCE OF DIRECT AND INDIRECT TAXES IN THE INDIAN TAX SYSTEM — 1976-77

Category	Percentage of contribution to total tax revenues
Indirect taxes of which —	79.3
(a) Union excise	34.6
(b) Customs	12.3
(c) Sales tax	19.0
(d) Other indirect taxes	13.4

Category	Percentage of contribution to total tax revenues
Direct taxes of which —	20.7
(a) Income-tax	8.0
(b) Corporation tax	9.2
(c) Other direct taxes	3.5
All taxes	100.0

SOURCE: Adapted from revenue statistics of Economic Division, Ministry of Finance, (Department of Economic Affairs).

It may be seen that Union excises account for more than one-third of total tax revenues, while sales taxes account for nearly one-fifth. Together they contribute more than 50 per cent of the total tax revenues of the Centre and the States. The two major direct taxes - income and corporation taxes - together make a smaller contribution to revenues than sales taxes.

1.10 As in India, in other developing countries too much greater reliance has been placed on indirect taxes than on direct taxes. In a recent study * conducted by International Monetary Fund covering 47 developing countries it was found that the average share of indirect taxes including some border line items, for the three-year period ending 1971, was about 66 per cent of the total tax revenues. Thus, the share of indirect taxes in India (which accounted for about 78.8 per cent in 1970-71) was appreciably higher than the average share of indirect taxes in the revenues of developing countries. In comparison with industrialised countries, the difference is much more as indirect taxes for the latter account for, on an average, only about 45 per cent of their total tax revenues.

1.11 The Table below indicates how the share of major indirect taxes in the total revenues from indirect taxes has changed during 1950-51 to 1975-76.

TABLE 4 — RELATIVE SHARE OF MAJOR INDIRECT TAXES -- 1950-51 TO 1975-76

Category of indirect tax	Percentage contribution to total indirect tax revenues						
	1950-51	55-56	60-61	65-66	70-71	72-73	75-76
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1. Union excise duties	17.1	28.6	43.9	41.0	47.0	45.7	44.3

(Contd)

* R.J. Chelliah, H.J. Bass and Margaret R. Kelly, "Tax Ratios and Tax Effort in Developing countries," 1969-71, IMF Staff Papers, Volume XXII, No. 1, March, 1975, pages 187-205.

Category of indirect tax	Percentage contribution to total indirect tax revenues						
	1950-51	55-56	60-61	65-66	70-71	72-73	75-76
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
2. Customs duties	39.7	32.8	17.9	24.6	14.0	16.8	16.3
3. Sales taxes	14.7	16.0	17.3	17.4	21.0	19.4	22.8
4. Taxes on vehicles	2.0	3.0	3.6	2.8	3.0	2.7	2.4
5. Taxes on passengers and goods carried by road	-	0.7	0.6	1.5	1.6	1.9	2.1
6. All others	26.5	18.9	16.7	12.7	13.4	13.5	12.1

SOURCE: Adapted from revenue statistics of Economic Division, Ministry of Finance, (Department of Economic Affairs).

The share of excise duties in the revenues derived from indirect taxes as a whole has been rising steadily, although there seems to have been a marginal fall in the seventies. The share of customs duties which has shown wide variations reflecting changes in import policies as well as in the level of duties, has latterly shown a pronounced downward trend. These trends reflect the changes in the economy as industrialisation and import substitution have progressed from plan to plan. With rising levels of domestic production and prices(together with increases in the tax rates), the share of State revenues derived from sales taxes and taxes on passenger and goods carried by road have displayed a definite upward trend.

ELASTICITY OF INDIRECT TAX REVENUES

1.12 It is usual to measure the degree of response of a tax system to changes in national income by what is known as income elasticity of the tax system. Income elasticity, also called built-in elasticity, of a tax is generally defined as the percentage of automatic change in the tax yield during a given period divided by the percentage change in the national income in the same period. The term 'built-in elasticity' is used to emphasise the fact that it is the automatic change in the tax yield in response to changes in national income which is being taken into account and not the actual growth in revenue between two points of time which is attributable also to changes in the rates of tax or in the base of taxation. Since the actual revenue collections from a tax between two points of time may have been influenced by discretionary tax (rate or base) changes introduced by the Government during the period, for calculating the build-in elasticity of the tax the effect of the latter has to be eliminated. If the income elasticity derived as indicated above, is unity or more than unity, the rise in the tax yield will be proportionate or more than proportionate to the rise in national income. On the other hand, an income elasticity of less than unity would mean that the tax ratio would go down from year to year as the national income goes up unless new taxes are imposed or existing tax rates are enhanced.

1.13 The studies relating to the elasticity of some of the major indirect taxes, which are available, are for periods prior to 1965. We requested the National Institute of Public Finance and Policy (NIPFP) to undertake a study of the elasticity of the major indirect taxes, namely, Central excises, customs duties, general sales taxes, entertainment tax and taxes on motor vehicles and on passengers and goods for a more recent period. The methodology and the various assumptions underlying the computation are explained in the study included in Appendix 5. The major conclusions are:-

(i) Excise duties showed an income elasticity of less than unity in the period 1963-64 to 1974-75 - the elasticity co-efficient being 0.75;

(ii) Customs duties were found to have no close relationship with income - during the period 1963-64 to 1974-75. But they were income elastic during the period 1969-70 to 1975-76 and the elasticity co-efficient for that period works out to 1.72; and

(iii) General sales taxes had a fairly high degree of elasticity, the elasticity co-efficient for all States for the period 1963-64 to 1974-75 being 1.15;

(iv) The taxes on motor vehicles and on passengers and goods and the entertainment tax also had elasticities greater than unity for the period under reference.

1.14 Thus, in the case of excises, which are the largest contributor to revenues among the indirect taxes, for every single-point increase in national income, the automatic increase in revenue, according to the study, was only about three-quarter of a percentage point. The limitations of data and methodology indicated in the study would suggest that some margin of error is to be allowed for. However, the conclusion can be drawn that excises were clearly inelastic to changes in national income at current prices. Therefore, the need to raise the tax rates in order that the same percentage of the national income comes to the exchequer, led to an upward revision of rates in almost every Budget. Predominance of specific duties in the period under reference has been one of the major factors responsible for the overall low elasticity of the excises.

1.15 As regards import duties, the major imports have been of goods in the nature of raw materials, intermediates and capital goods required by industry. As the industrial output went up, particularly in the seventies, the demand for them showed bouyancy. This and the ad valorem nature of import duties, in general, were the main factors responsible for high elasticity of import duties. The high elasticity of sales taxation is mainly accounted for by its almost universal coverage and the ad valorem nature of the levies in general.

INCREASE IN TAX RATIO

1.16 It would also be of interest to study the trend of total tax revenues in relation to national income, especially the ratio of taxation to national income - the so-called 'tax ratio' - which is generally taken as an index of the tax burden on the community. The following Table indicates the variation in tax ratio during the period 1950-51 to 1975-76:

TABLE 5 - VARIATION IN TAX RATIO - 1950-51 TO 1975-76

Year	Total Tax revenues (Rs. crores)	Net national income (Rs. crores)	Tax ratio (i.e. ratio of taxation to national income) (Percentage)
1950-51	626.7	9530	6.6
1955-56	767.6	9980	7.7
1960-61	1350.4	13263	10.2
1965-66	2921.6	20637	14.2
1970-71	4752.4	34462*	13.8
1971-72	5575.2	36332*	15.3
1972-73	6435.8	39643*	16.2
1973-74	7388.6	49396*	15.0
1974-75	9223.1	58137*	15.9
1975-76	11181.7	60293+	18.5

* Estimates

+ Quick Estimates

SOURCE: 1. Tax revenue figures - Economic Division, Ministry of Finance, Department of Economic Affairs.

2. National income - Economic Survey, 1976-77, Government of India, for statistics from 1960-61 onwards. For previous years, Pocket Book of Economic Information, 1966, Department of Economic Affairs.

The increase in the tax ratio from about 6.6 per cent during 1950-51 to more than 18 per cent during the year 1975-76, i.e. more than $2\frac{1}{2}$ times the tax ratio before the beginning of the First Five Year Plan is mainly due to substantial measures to mobilise additional resources for development on an increasing scale as well as to finance the steadily rising non-plan expenditure of Government

1.17 Comparing the tax ratio for India with that for other countries, we find that as against a tax ratio of about 16 per cent for India in 1974-75, it ranged from about 25 per cent to 45 per cent * for advanced countries like U.S.A., U.K. and Denmark in the year 1974. This may suggest that our tax effort is low in comparison with that in advanced countries. One cannot, however, ignore the fact that even a lower tax ratio of 18 to 19 per cent can mean a much higher burden in a country like ours where the per capita income is below Rs. 1,000 a year, than even a high tax ratio of 25 to 30 per cent in countries having per capita incomes reckoned in tens of thousands of rupees.

1.18 On account of paucity of data, it is less easy to compare India's tax effort with that of other developing countries. The International Monetary Fund study quoted earlier showed that the average tax ratio for 47 developing countries in the period 1969-1971 was 15.1 per cent while the figure for India for the same period was 13.4 per cent. The tax ratio in India has since gone up to more than 18 per cent. Though we have no data about changes in the tax ratio in other developing countries, considering that the per capita income in India is one of the lowest even among developing countries, India's tax effort cannot be said to be too low by international standards.

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* The average ratio of taxes (including social security contributions) to GNP in the OECD countries amounted to 33.9 per cent in 1974 (of Revenue Statistics of OECD Countries 1965-1974. Table 1, page 72.)

TABLE 2 - COMBINED TAX REVENUE RECEIPTS OF THE CENTRE, STATES AND UNION TERRITORIES

Revenue Receipts - 1950-51 to 1976-77 (Rs. lakhs)

Description	1950-51	1955-56	1960-61	1965-66	1970-71	1975-76	1976-77 (RE)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
TAX REVENUE	62667 (100.00)	76756 (100.00)	135041 (100.00)	292159 (100.00)	475241 (100.00)	1118173 (100.00)	1207677 (100.00)
I. Direct taxes	23056 (36.79)	25907 (33.75)	40207 (29.77)	73414 (25.13)	100907 (21.23)	249255 (22.29)	249679 (20.67)
II. Indirect taxes	39611 (63.21)	50849 (66.25)	94834 (70.23)	218745 (74.87)	374334 (78.77)	868918 (77.71)	957998 (79.33)
(i) Customs	15716	16670	17003	53897	52402	141940	149045
(ii) Union excise duties	6754	14525	41635	89792	175855	384478	417660
(iii) State excise duties	4985	4516	5491	10017	20143	45748	51740
(iv) Stamp duties	2392	2679	4037	7372	11413	23444	26703
(v) Registration fees	387	401	685	1183	2076		
(vi) General sales tax	5820	8159	16392	38154	78640	198247	228857
(vii) Taxes on vehicles	778	1508	3415	6122	11218	20875	24031
(viii) Entertainment tax	@	@	@	@	@	13997	15334

Cont'd....

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
(ix)	Taxes on goods and passengers carried by road	11	351	556	3370	5844	18583	20398
(x)	Taxes and duties on electricity	312	582	1251	3536	6711	11186	12989
(xi)	Tax on purchases of sugarcane (including Cess on sugarcane)@@	216	371	500	1196	1152	3587	4288
(xii)	Others £	2240	1087	3869 YY	4106	8380	6833	6953

Note:- Figures in brackets indicate percentage to total tax revenue.

@ Included in "Others"

@@ For the years 1950-51 to 1970-71 represents Cess only.

£ These include entertainment tax, terminal tax and betting tax in Delhi, tobacco duties, newspaper and advertisement tax, education cess, taxes on raw jute etc. The figures for the years 1975-76 and 1976-77 also include foreign travel tax.

YY Includes Rs. 1589 lakhs from tax on Railway fares.

(Source: Economic Division, Ministry of Finance, Department of Economic Affairs)

CHAPTER 2

CENTRAL TAXATION - 1. CENTRAL EXCISE DUTIES

2.1 Excise duties, or excises as they are sometimes called, are generally defined as inland taxes or duties imposed upon the domestic production of commodities for sale or consumption within the country. Excise as a levy, either in the shape of a tax or a toll, has been collected in India from ancient times. An excise duty on liquor and salt was levied to augment revenues from traditional sources even in the Mauryan period. The early empires, the Moghuls, the Marathas and their successors, the British, levied various forms of taxes on salt treating it as a monopoly article. Products like sugar, cloth, leather and dairy products were also subject to excise duty during Moghul period and even during early British rule. However, by 1894 a beginning may be said to have been made towards the modern excise system, when a duty at the rate of 5 per cent ad valorem was imposed on cotton yarn of counts above twenties - the object undoubtedly being to indirectly tax the indigenous cloth which competed with Lancashire cloth. In the year 1896, this was changed into an excise duty on cloth, the rate being fixed at 3½ per cent. Even coarser cloth which did not compete with those imported from Lancashire, got taxed. This levy came up for strong criticism and there were repeated demands for its withdrawal. Even the Indian Fiscal Commission (1921-22) recommended its abolition. The levy ceased to operate with effect from 1st December, 1925, and was abolished finally in the year of 1926, when the industry was found to be facing a critical situation.

HISTORICAL BACKGROUND

2.2 A levy on motor spirit (at the rate of 6 annas per imperial gallon) was introduced in 1917. Though the primary purpose of this levy was to curb consumption of petrol so as to conserve supplies for meeting was requirements, it was retained permanently as it proved to be a good source of revenue - as has happened time and again with taxes originally introduced to serve an economic purpose. The next item to be placed under excise was kerosene on which a duty (at the rate of one anna per imperial gallon) was levied in 1922. No new commodities were taxed thereafter for a number of years till 1930 - when silver was also brought under the excise purview. But with the separation in 1937 of Burma - the main producer of silver - the duty ceased to be of any revenue significance.

2.3 The year 1934 mark the first step in the rationalisation of excise levies and extension of their coverage. This was in the context of the Great Depression when the revenues of the Government of India were on the decline. It is interesting to reflect that while post-Keynesian economic thought favours a lowering of tax rates to combat recessionary conditions, the view at that time was to cut down Government expenditure and increase taxes. To augment revenues, sugar, matches and steel ingots were brought under the tax net. Sugar and matches were selected as their indigenous production had expanded greatly under the heavy protection provided in the years following the First World War and the yield from Customs duties on them had gone down. The imposition of excise on steel ingots (with a countervailing customs duty) was to cover the loss in customs revenue due to the considerable reduction affected in the import duty as a result of Tariff Boards' recommendations regarding protection to the steel industry. Mechanical lighters were also brought under the excise net the same year, though there was no indigenous production, lest the high excise on matches should encourage investment in the manufacture of lighters - which showed considerable sophistication in fiscal policy. Exigencies of the Second World War necessitated further extension of excises besides the increase in duties on the existing items. Pneumatic tyres and tubes were taxed in the year 1941 and even vegetable product was subjected to excise duty in the year 1943.

2.4 While considering the extension of excises to more commodities, the general policy approach appears to have been to follow the guiding principles laid down by the Indian Fiscal Commission (1921-22) which were mostly endorsed by the Indian Taxation Enquiry Committee of 1924-25. The Indian Fiscal Commission (1921-22) had briefly summarised the principles of excise duties as follows:

"(i) Excise duties should ordinarily be confined to industries which are concentrated in large factories or small areas;

(ii) They may properly be imposed for the purposes of checking the consumption of injurious articles and especially on luxuries coming under this category;

(iii) Otherwise they should be imposed for revenue purposes only;

(iv) While permissible on commodities of general consumption, they should not press too heavily on the poorer classes;

(v) When an industry requires protection, any further necessary taxation on its products may, if the other conditions are fulfilled, take the form of an excise duty plus an additional import duty. The latter should fully countervail the former and may be pitched at a higher rate". *

2.5 The Indian Taxation Enquiry Committee (1924-25) had suggested a slight modification, only to the last recommendation, namely—

"When an industry requires protection and a consumption tax is also required from the produce of that industry in the interest of the revenues, the necessary amount of excise is unobjectionable provided that it is accompanied by an import duty equal to the excise duty, together with the necessary protective duty, plus a small extra duty to compensate for the administrative inconveniences to the manufacturers caused by the excise duty. **

2.6 The Indian Taxation Enquiry Committee (1924-25) had also made recommendations for taxing different forms of tobacco and suggested various possible methods by which they could be taxed. It had recommended a system of licensing for the taxation of unmanufactured tobacco. The imposition of a tax on unmanufactured tobacco was, however, deferred mainly because of the administrative difficulties involved in controlling a large number of tobacco producers, dealers etc. It was only when the need for additional resources became very compelling during the War, that a tax on unmanufactured tobacco (with an elaborate scheme of tax administration) was introduced in the year 1943, thus marking a departure from the past pattern of taxation which had been confined to products of organised industries alone. As further sources of revenue, duties were levied on coffee, tea and betel nuts in 1944. (Duty on betel nuts was abolished in 1948 because of administrative difficulties and the fact that after partition major production areas had been lost to India. The duty on salt was remitted on the eve of Independence in 1947.

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* Report of the Indian Fiscal Commission (1921-22) Para 151, p. 87.

** Report of the Indian Taxation Enquiry Committee (1924-25) Vol. I, Para 163, p. 133.

2.7 Between 1944 and 1954, only two new excise levies were introduced. Cigarettes were subject to a duty, in addition to the existing duty on unmanufactured tobacco, in 1948. Mill-made cotton cloth was subject to duty again in the following year, mainly to make up for the heavy loss in revenue resulting from the abolition of the salt duty, and also to help the handloom industry without affecting the mill industry. Cement, footwear, rayon and art silk fabrics and soap (manufactured with the aid of power) had also been added to the Central excise tariff in the year 1954, by the time the Taxation Enquiry Commission (1953-54) submitted its report to the Government.

2.8 The Taxation Enquiry Commission (TEC) set forth various considerations which should govern the future taxation policy with particular reference to the resources that would be needed for the development of the country. The following extracts from its report are of special interest:

> "The tax system must have an adequacy of both depth and range. If it is to promote an accelerated pace of development, additional taxation of a wide range of luxury or semi-luxury products at fairly substantial rates, accompanied by broad based taxation of articles of mass consumption at comparatively lower rates, is, therefore, indicated....."*
>
> "It is necessary to emphasise that higher taxation of luxury articles will, by itself, not produce sufficient revenue. For any substantial receipts from commodity taxation and appreciable restraint on consumption in the economy as a whole, it will be necessary to extend excises and sales taxation to the consumption of lower income groups and of goods which are commonly classed as necessaries, including several goods which are included in the Essential Goods Act under Article 286 of the Constitution.....
> An extension of the taxation of necessaries appears unavoidable, if significant results by way of diversion of resources for financing public investment are to be secured....."*

2.9 The TEC had also examined the excise tax structure on the existing items and recommended certain changes in regard to some of them. Besides, it also suggested extension of excises to certain specified commodities which covered both consumer items as well as products which are also used as inputs. The items recommended were paints and varnishes, dry and storage batteries, paper, biscuits, electric fans, aerated waters, electric lamps, glass and glassware, ceramics, vegetable oils, woollen textiles and sewing machines. One of the criteria by which the TEC had judged the suitability of commodities for levy of excises was the extent to which the indigenous production had developed under the umbrella of protection, so that the revenue loss due to decline in imports could be recouped. The TEC did not, however, deal with the likely interaction of extended excises with sales taxes or with the problems that would be caused by taxation of inputs.

2.10 The year 1955 thus marked the beginning of a new phase in the growth of excises. Although the TEC had specifically mentioned only a limited number of commodities to be brought under excise, the broad principles that they had adumbrated indicated lines of further expansion. The number of items subject to excise was steadily expanded as the need for additional revenues kept on rising. Largely on considerations of ease of collection and partly also because levies on articles of mass consumption met with opposition from the public, heavier reliance was placed on the taxation of

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* Report of the TEC (1953-54) - Vol. I,
Chapter 8, Paras 14 and 15. pp. 148-49.

inputs, whose producers were few, than on consumer goods. Metals, chemicals, dyes, plastics and yarns and a number of other inputs were subjected to excise by the beginning of the sixties. Side by side the rates on consumer goods subject to excise were also raised.

2.11 While these ad hoc changes were being made, the need to have a fresh look at the possibilities of additional revenue mobilisation began to be felt. Customs revenues could not grow sufficiently with the emphasis on import substituion and the paucity of foreign exchange. Income and wealth taxation could only reach a small fraction of the population. In 1968, Government appointed a one man (Shri S. Bhoothalingam) Committee to examine and report on the rationalisation and simplification of the structure of direct as well as indirect taxes. In regard to excise taxation, Shri Bhoothalingam had recommended that instead of having levies at different rates on selected products there should be a uniform duty (described by him as general excise duty) at the rate of 10 per cent ad valorem on all manufactured products (with some exceptions) with a tax base which excluded the value of all materials bought out for the purpose of production but not the value of equipments and services. * The view taken by Government on this recommendation, we understand, was that the recommendation as a whole could not be accepted at that stage. But the need to enlarge the tax base by levying a low ad valorem duty on a large number of finished goods which did not bear any excise duty then, even if it meant relatively low revenue yield for each new commodity, was accepted in principle. This policy thinking was summed up by the Prime Minister, who was then holding the Finance portfolio, in her Budget speech of 1970, the relevant extract from which is given

> "It has often been suggested that the scope for excise taxation should be widened to include taxation at a low rate of about 10 per cent on practically the whole range of manufactured products. Without going that far it is proposed to levy a 10 per cent ad valorem excise duty on a number of new items including office machines, metal containers, sparking plugs, stainless steel blades, slotted angles, iron safes and safe deposit vaults..... The additional revenue from these new duties will amount to Rs. 10.40 crores."

2.12 As of 1974-75, around 128 commodities (or to be more precise, commodity groups under different tariff items) were subject to excise, of which a few were in effect totally exempted. In the Budget for 1975-76, a general one per cent tax was introduced on all goods "not elsewhere specified" manufactured in factories as defined in the Factories Act, 1948, though a number of goods were specifically exempted from the same. In effect, what we are having today is an extended excise system which is tending towards universal coverage of industrial goods.

2.13 Till 1943, different commodities were subject to excise levies under different enactments.

THE CENTRAL EXCISE LAW

By 1944, no less than 16 separate enactments regulated the levy and collection of excise duties of which 7 related to salt, 2 to silver and mechanical lighters and the remaining 7 to motor spirit, sugar, matches, steel ingots, tyres, tobacco and vegetable product. In 1944, the various laws were consolidated in the Central Excises and Salt Act.

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* - Final report on rationalisation and simplification of the tax structure. December, 1967, paras 3.3 to 3.11. pp.6-11.

(1 of 1944) and the Central Excise Rules (1944) and the common provisions made applicable to all goods. Section 3 of the Act empowers the levy of duties of excise, while the Schedule to the Act, commonly known as "Excise Tariff" enumerates the articles on which duty is leviable and the rates applicable to them. The other provisions deal with procedural matters. The original Act has been amended from time to time and various new rules have also been framed resulting in complexities in the matter of administration. The Central Excise Reorganisation Committee, 1963 (Chanda Committee) recommended a comprehensive review of the Act and the Rules, and suggested incorporation of all the substantive provisions of the law in the Act itself and also the removal of the various anomalies. Accordingly, a new Central Excise Bill was introduced in Parliament. But the Bill lapsed due to the dissolution of Lok Sabha in December, 1970 and no new bill has yet been introduced.

2.14 Apart from the excise duties levied on various products under the Central Excises and Salt Act, 1944, some other types of Union excises are also currently in operation. In the early fifties, there were repeated demands from the trade for the Central Government to levy and administer the sales taxes on all excisable goods, collecting them along with the Central excise duties. In 1957, following the agreement between the Centre and the States at the meeting of the National Development Council held in December, 1956, it was decided that the Centre would levy additional duties of excise on mill-made textiles, sugar and tobacco (including manufactured tobacco), in lieu of the sales taxes then being levied by the State Governments. The net proceeds of revenue so collected were to be distributed among the States subject to the condition that income then derived would be assured to each State. Accordingly, the Additional Duties of Excise (Goods of Special Importance) Act, 1957 was enacted in December, 1957. We discuss this levy more fully along with sales tax and other State levies.

TYPES OF UNION EXCISE LEVIES

2.15 Tea, mill-made-textile fabrics (cotton, artsilk, woollen), oil extracted from oil seeds, cotton, jute and tobacco are subject to cesses under separate enactments which are collected by the Central excise department. Their net proceeds are earmarked for specified purposes, for example, promoting the growth of the particular industry or sectors of the industry from which they are collected.

2.16 Another type of duties of excise to which we would briefly refer here are the levies, under the Mineral Products (Additional Duties of Excise and Customs) Act, 1958, on certain petroleum products. Because the cost of imported crude oil keeps on fluctuating and occasions arise when, with the prevailing price structure of petroleum products, the refineries/marketing companies make windfall profits, the Act gives the necessary powers to Government to divert these fortuitous profits to the Exchequer by way of an additional tax which cannot be passed on to the consumers. The levies have in fact enabled the Government to mop up the windfall benefits accruing to the refineries and marketing companies. *

* Since the above passage was written, we understand that on most petroleum products these additional duties have been withdrawn and merged - partially or wholly - with the basic duty leviable under Central Excises and Salt Act, 1944.

DIFFERENT SCHEMES OF EXCISE DUTY COLLECTIONS

2.17 Central excise duties are, at present, collected from various producers/manufacturers under the following different procedures:

(i) Physical Control;

(ii) Self Removal Procedure;

(iii) Compounded Levy Scheme;

(iv) Simplified Procedure;

(v) Special Procedure for commodities taxes under the residuary item 68.

2.18 Prior to 1968, the administration of excises was based mainly on physical control - its basic features being prior assessment of goods, pre-payment of duty and physical supervision over clearance by the excise officers. However, with effect from 1st June, 1968, the procedure of collection of excise duties was radically changed when all except 14 commodities (this exception was reduced to only unmanufactured tobacco in August, 1969) were brought under a self assessment procedure called 'Self Removal Procedure' or 'SRP'. Under this procedure, the assessee is allowed to take clearance on his own assessment of the duty liability without prior permission of physical checks by excise officers. To ensure correct assessment and payment of duty due to the Government, certain obligations have been placed on the manufacturers. An important requirement of this procedure is prior approval of documents called 'classification list' and 'price list' (the latter being necessary when the goods are assessed on an ad valorem basis) before any clearances can be effected from the factory. In the classification list the manufacturer makes a declaration giving a detailed description of each and every item of goods produced so that they can be classified in terms of the tariff and the rate of duty applicable to them determined accordingly. The price list has to give the prices charged to different classes of buyers, along with discounts and deductions, etc. The penal provisions for unauthorised removal or other contraventions of rules and regulations are more stringent under the SRP than those under the procedure of physical control.

2.19 Two schemes relating to collection of duty have been specially introduced for the benefit of small units for whom it is difficult to comply with the rigours of normal excise formalities. The first, generally known as the "Compounded Levy Scheme", was introduced in the year 1954 to take care of excise collection from a large number of small decentralised powerloom units. * Instead of paying duty on the basis of assessment on individual clearances, the units were given the option to compound and discharge their duty liability by paying a lumpsum amount determined with respect to certain factors (like the number of powerlooms installed, etc.). The duty is payable on quarterly or yearly basis. This scheme has been extended to some more commodities which include Khandsari sugar, battery plate and coarse grain plywood manufactured by small units. Once the compounded levy is paid, the manufacturer is exempted from almost all the other formalities of accounting, etc.

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* With the grant of total exemption to weaving stage duty on powerloom fabrics the scheme is no longer applicable to powerloom units.

2.20 The other scheme, commonly called "Simplified Procedure" of duty collection from small producers, was introduced with effect from 1st March, 1976, on the recommendations of the Self Removal Procedure (Review) Committee (Venkatappiah Committee). The scheme which is applicable to small producers in 46 notified industries provides for a reduced compounded duty liability - the extent of concession is generally 10 per cent of the duty payable by the organised sector - which is payable before the start of each month. The eligibility criterion for this scheme is that the annual value of production (determined in accordance with a prescribed procedure) should not be higher than Rs. 5 lakhs. We discuss more about this scheme in Chapter 12.

2.21 Apart from the above mentioned procedures of assessment and duty collection, there is a special procedure which is applicable in respect of goods classified under the residuary tariff Item No. 68 of the Central Excise tariff. The procedure is similar to the SRP with a large number of relaxations from the normal formalities having regard to the very low rate of duty and the enormous administrative burden that would otherwise have devolved on the departmental heirarchy. Thus as against the requirements of prior submission and approval of price lists for other goods assessed on an ad valorem basis, the manufacturers of goods classified under Item No. 68 are allowed to assess their goods on the basis of the invoice price itself.

GROWTH OF EXCISE REVENUES

2.22 From a revenue yield of about Rs. 2.85 crores from only two items which were subject to excise in 1920-21, (leaving salt revenue which contributed another Rs. 6.76 crores) the yield during the year 1950-51 had gone upto Rs. 6.75 crores from 13 items; it rose further to Rs. 1758.85 crores in 1970-71 from 88 items and is estimated at Rs. 4176.60 crores in 1976-77 from 124 items. * Side by side, the share of excise in in the total tax revenues of the Centre increased from about 4.7 per cent in 1920-21 to around 16.7 per cent in 1950-51. 45.8 per cent in 1960-61 and is estimated to be as high as 52 per cent during the year 1976-77. The ratio of excise to national income too has grown significantly, from about 0.7 per cent in 1950-51 to about 5.1 per cent in 1970-71 and is estimated to have been about 6.4 per cent in 1975-76.

2.23 The growth in revenue, which has been particularly sharp in the last 10 years, has been due to various factors, namely, increased coverage, changes in tax rates and increased consumption. The NIPFD study on elasticity of excise revenues, referred to earlier, has estimated that the gross increase of Rs. 2925.7 crores in revenue in 1975-76 over 1965-66 is attributable in the following proportion to the three factors mentioned above.

		Rs. crores	Percentage of total revenues
(i)	Due to increased coverage (new goods)	343.19	11.73
(ii)	Due to rate changes in relation to goods taxed in 1965-66.	1532.68	52.39
(iii)	Due to growth of base of goods already taxed in 1965-66.	1049.83	35.88
		2925.70	100.00

* The term 'item' here refers to tariff items which in several cases cover more than one commercially known commodity, Even residing tariff No. 68 has been taken one item.

Increase in tax rates stand out as the biggest factor in the growth in revenue, contributing more than half of the increase in revenue in 1975-76 over 1965-66.

2.24 In Table 1, appended to this Chapter, we give a break-up of the excise revenue derived from different commodities based on the Revised Budget Estimates for the year 1976-77. The table enables us to analyse the way in which the excise burden falls on different product groups, except for the commodities covered by the residuary tariff item No. 68 because a commodity-wise break-up of the miscellany of products covered by this item is not available. From a study of the figures in this table, the following broad conclusions can be drawn:

(i) Roughly, half of the excise revenue, is derived from direct levies on what could be deemed to be consumer products while the other half of the revenue comes mainly from the taxation of inputs as well as capital goods - most of the latter being covered by tariff item No. 68.

(ii) The nominal levies on the final products which may be deemed to be goods of mass consumption make a very substantial contribution as shown in the following table:

TABLE 2 - REVENUE FROM MASS CONSUMPTION GOODS

Sl. No.	Description	Revenue realised in 1976-77 (RE) (Rs. crores)
(1)	(2)	(3)
1.	Manufactured tobacco (cigarettes, biris, smoking mixtures, snuff, chewing tobacco and cigars and cheroots)	404.60
2.	Sugar (including khandsari)	242.40
3.	Kerosene	167.88
4.	Textile fabrics (excluding jute fabrics)	185.62
5.	Tea	62.00
6.	Coffee	6.25
7.	Medicines (patent or proprietary)	53.80
8.	Printing & writing paper	27.50*
9.	Matches	38.00
10.	Vanaspati and refined vegetable oil.	20.45

* Estimated share is RE of Rs. 84.00 crores from paper and paper boards.

(1)	(2)	(3)
11.	Soap	15.00
12.	Footwear	5.40
	Total :	1228.82

i.e. 29.4 per cent of total net excise revenues.

(Source : Explanatory Memorandum on the Budget of the Central Government for 1977-78 and Directorate of Statistics and Intelligence, Central Excise & Customs, New Delhi).

However, if the duties on unmanufactured tobacco and fibres and yarn are also taken into account, the revenue realisations from manufactured tobacco and textile fabrics would go up to Rs. 506.60 crores and Rs. 600.02 crores respectively, which would raise the excise revenue from goods of mass consumption as a percentage of total revenue to 41.8. Further, some items of mass consumption such as aluminium utensils, which do not appear in the above table, because no excise is directly levied on them, would account for a non-too-small figure because of the tax on aluminium.

REVENUE FROM WAGE GOODS

2.25 The articles consumed by the working class have a special importance of their own. Of the various articles which are taken up for working out the index of consumer prices for industrial workers, there are many important items like cereals and pulses, vegetables, fruits milk and soft coke which are either not excisable or exempt. The other major essential wage goods consumed by the industrial workers which pay excise duty are sugar, kerosene, matches, vegetable product, tea, coffee, soap, footwear and cotton fabrics. The table below indicates the trend of revenue realisation on these identified wage goods in the last two decades:

TABLE 3 - REVENUE FROM WAGE GOODS SINCE 1956-57

Year	Revenue realised from wage goods (Rs. crores)	Total revenue from all excises (Rs. crores)	Col. (2) as percentage of col. (4)
(1)	(2)	(3)	(4)
1956-57	97.66	192.7	50.9
1961-62	181.67	489.1	37.1
1966-67	289.47	1033.77	28.0
1971-72	469.32	2061.10	22.8
1976-77 (RE)	677.15	4176.60	16.2

The above table brings out that even though in absolute terms the excise realisations from the identified wage goods have gone up considerably over the last 20 years, their share in the total excise collections has shown a steady fall. However, here again, a note of caution has to be added because the taxation of inputs has not been reflected in the above figures and also because tobacco family has been left out. Similarly, the burden on the working classes through the levies on buses, trucks and the fuel used for running them has not been reflected in the above figures. These are points we discuss in a later chapter dealing with the incidence of indirect taxation on different expenditure groups.

SHIFT TO AD VALOREM DUTIES

2.26 Though in the past specific duties predominated in the excise tariff, in recent years there has been a growing emphasis on ad valorem levies. The duties on most of the new commodities brought under the excise net since 1970-71 have been levied on an ad valorem basis. In recent years, there has also been a trend to convert specific duties to ad valorem duties. Thus, in respect of two important revenue items - paper and cotton fabrics - duties were converted to ad valorem basis in the 1976 Budget. Duties on a number of items (like paints and varnishes, radios, tape recorders etc.), which were hitherto charged at specific rates, have been converted to ad valorem basis in the 1977-78 Budget. The table below shows tha the relative importance of specific and ad valorem duties in terms of yield (in 1976-77).

TABLE 4 - RELATIVE SHARE OF EXCISE REVENUE FROM SPECIFIC AND AD VALOREM DUTIES

Sl. No.	Commodity Group	Estimated revenue realisation (1976-77) (Rs. crores)	Percentage of total excise revenue
(1)	(2)	(3)	(4)
1.	Subject to specific duty	2127.87	58.7
2.	Subject to ad valorem duty	1900.84	45.3
3.	Others —		
	(a) Ad valorem component	97.69	2.3
	(b) Specific component	70.31	1.7
4.	Total	4196.71*	100.0

* Gross revenue excluding cesses and miscellaneous receipts.

Note : (i) The Item 'Others' mentioned above includes commodities which are subject to ad-valorem-cum-specific rates such as aluminium.

(ii) Revenue from commodities in which some sub-headings are subject to specific rates while the rest are subject to ad valorem rates, (such as, copper and copper alloys) has been apportioned and shown against S. Nos. 1 & 2.

From the above table, it may be seen that despite the shift to ad valorem levies in recent years specific duties even now continue to account for a substantial proportion of the excise revenues. The major revenue yielding items which are still subject to specific duties are most petroleum products, ferrous metals, copper, unmanufactured tobacco, biris, synthetic fibres and yarn and most varieties of cement.

CONSIDERATIONS INFLUENCING EXCISE TAXATION AND PRESENT RATE STRUCTURE

2.27 The present structure of excise rates on various commodities is the result of attempts made from year to year, in successive Budgets, towards mobilisation of additional resources as well as to achieve various socio-economic objectives through fiscal means. Revenue considerations often led to ad hoc increases in rates of excise duty. Reductions in rates of duties were also effected, though less frequently, in response to representations seeking relief on various grounds. The following are some of the considerations which have influenced the rates of excise taxation on different products:

(a) On the administrative ground of ease of collection, inputs rather than the finished products made from them were often preferred for the purposes of levying excise duties;

(b) The most important factor has undoubtedly been the consideration of progression. Differential rates of duties were levied from time to time on different commodities or even on different varieties of the same product with the object of placing the minimum burden on the poorer sections and having a higher tax incidence on the upper income groups;

(c) The rates were often raised to mop up surplus profits of industries whose products enjoyed a premium in the market because of scarcity. While proposing increase in the 1965-66 Budget, on certain items like copper, steel and tin plates, the then Finance Minister had stated in his Budget speech:

"In a growing economy with shortage at various levels, there is also a tendency for the price structure to be distorted. It is common knowledge that excessive profits are being made in the sale of products based on scarce materials..... and I propose to make selective increase in both import and excise duties to mop up these surplus profits";

We are constrained to add that when the shortage disappeared the duty was not always reduced,

(d) The rates were raised at times to curb consumption or to stop the diversion of low-taxed items for use as a substitute for other items taxed at higher rates. Thus, in

November, 1973, a sharp duty increase on petrol and significant increase in the duty on kerosene were proposed to arrest the consumption of petrol and prevent the diversion of kerosene for use in admixture with diesel oil;

(e) The need to improve our export earnings of foreign exchange have, at times, influenced levies on particular products. Thus, one of the reasons behind the enhancement of excise duties on tea in 1970 was to curb domestic consumption so as to make available larger quantities for export;

(f) Taxes were also levied on some commodities to raise revenue from those who could not be reached by direct taxation. Thus, the levies on fertilizers and power driven pumps were imposed in the year 1969 mainly because agricultural incomes were not, it was felt, being adequately taxed;

(g) In some cases, taxes were imposed or raised on the organised sector to promote the growth of decentralised production; and

(h) Sometimes tax relief was given to individual industries facing difficulties.

2.28 Attention to all these diverse factors inevitably meant that a multitude of rates came into being and similar products, whether consumer goods or inputs, were often subject to very different rates. This trend was further accentuated by certain other factors. At times, the need for additional revenue was met by differential surcharges levied on a select range of goods. One of the reasons for doing so, apparently, was that while the basic excise duty had to be shared with the States in a fixed proportion, it was intended that the so-called special or auxiliary duties would not be so shared. In course of time, these duties got merged into the basic excise duties bringing new rates into being. Something similar happened whenever specific duties were converted into ad valorem duties. The attempt to keep the new ad valorem rates as close to the then existing ad valorem incidence of specific duties led to some odd rates coming into existence. In the event, a multitude of rates ranging from 2 per cent to 370 per cent came into being in respect of consumer products. There is a similar multiplicity and diversity in the rate structure of raw materials and other inputs. In addition, there are specific rates on a fairly wide range of products and in fact, as shown above, more than half the excise revenue still comes from specific duties. If these also are reckoned in ad valorem terms the estimated range and number of rates in existence will go up greatly.

EXEMPTIONS

2.29 Though the Central Government have no powers to enhance the rate of excise duty levied on any product above the level approved by Parliament (commonly called the statutory or tariff rate), they have been vested with powers to exempt, by issue of notifications, any excisable product either wholly or partially from the duty of excise leviable on it. The exemption may be either general and unconditional or specific and subject to certain conditions. The Government have made extensive use of the powers to grant exemptions and more than 600 notifications are currently effective which have been issued from time to time on various considerations. Some concessions are meant to give relief to consumers, like the recent reduction in the excise on sugar. A range of exemptions in favour of small producers have also been introduced to enable them to develop and withstand competition from larger producers - which we shall be discussing in Chapter 12

of the Report. The rest of the exemptions have been issued for various miscellaneous purposes such as promotion of exports (e.g., the partial exemption for certain processed vegetable non-essential oils produced by the solvent extraction method), providing incentive to higher production (e.g., the scheme applicable to a number of industries with effect from 1st July, 1976), conservation of scarce resources and encouragement of the use of unconventional raw materials or wastes (e.g., the partial exemption to paper using bagasse, cereal straw or jute stalks partial exemption to copper or zinc products using scrap, complete exemption to particle boards, etc.) and to support programmes of public health and family planning (e.g., the exemption to contraceptives). A number of exemptions have been provided for particular end-uses of certain products and are available subject to elaborate conditions being satisfied. The verification of their fulfilment has often led to complexities of administration. For example, there is a complete exemption for refined diesel oil, if it is supplied for use in a fishing vessel designed for deep sea fishing which is not less than 13.7 metres in length and has a motive power not less than 150 BHP, provided a number of other conditions are also satisfied. These include elaborate documentation, production of proof of export of shrimp (within 3 months of the date of export or in any extended period that may be allowed) at the rate of one tonne of shrimp for each quantity of 1.08 KL of refined diesel oil desired to be obtained free of duty) and submission of monthly returns of actual quantities of shrimp exported. Often exemptions have been issued to meet specific situations faced by particular units or small segments of an industry at a particular point of time. Some of the exemptions have continued even when the circumstances for the grant of exemption have changed. Finally, there are exemptions which have been given on the consideration that the cumulative incidence on particular commodities, due to the taxation of inputs as well as final products, is too high. To deal with this problem some other procedures are also available which we discuss below.

RULE 56-A PROCEDURE

2.30 Under the provisions of rule 56-A of the Central Excise Rules, 1944, manufacturers of certain notified finished excisable goods are allowed to bring excise/countervailing duty paid raw materials or components and take credit for the said duty in an account (called Proforma Credit Accounts) which can be utilised for payment of duty on the finished excisable goods. For example, compressors and condensors for refrigerators are liable to excise but when they are used in the assembly of refrigerators, proforma credit is given if the refrigerator manufacturer buys such compressors and condensors on payment of duty. The list of products which are at present notified under rule 56-A is given in Table 5 amended to this Chapter. Though the rule itself provides for the application of this procedure to all cases, whether the input and the finished product fall under the same tariff item or sub-item or otherwise, in practice, there are very few instances of proforma credit being available for inputs which fall under a tariff item different for the final product in which it is used. Thus, when refined vegetable non-essential oils are used in the manufacture of vanaspati, the vanaspati manufacturers can claim proforma credit of duty paid on such oils. This has been made permissible by grant of a special notification. Another restrictive feature of the rule is the limitations on the type of inputs for which the relief is permissible. Thus, the scheme is not applicable for giving relief in respect of duty paid on packaging materials or consumable stores. It is also not permissible to claim relief under the scher if the finished product is wholly exempt. Finally, no relief of customs duty paid on inputs is available under rule 56-A, though, as observed above, the amount of countervailing duty paid is eligible for relief.

2.31 Then there is the set-off procedure under which relief in respect of input taxation is provided by a notification exempting the final product to the extent of the excise or countervailing customs duty paid on the specified inputs used in its manufacture. For example, steel ingots, if made out of duty paid iron in any crude form, are exempt to the extent of duty paid on such crude iron. Like proforma credit, the set-off provisions have been applied to a limited extent and do not have large coverage.

SET-OFF PROCEDURE

2.32 The procedure laid down in Chapter X of the Central Excise Rules envisages removal of dutiable raw material or intermediate products under bond for use in specified industrial processes and provides for full or partial exemption from excise duty on such raw materials or intermediates when actually used for the specified purposes. A distinction between the previous provisions and this provision is that whereas the duties are paid in the first instance in the former cases and later adjusted against the duty liability on final products, under Chapter X procedure the goods move either without or only on partial payment of duty. This procedure has at times been extended to cases where the final products are exempt from duty and has also been applied to consumable inputs such as fuel.

CHAPTER X PROCEDURE

2.33 Finally, there are certain other exemptions which have been issued to lower the cumulative duty burden on account of taxation of inputs as well as the final product. There are cases where the input is completely exempt for certain uses keeping in view the fact that duty is leviable on the final product also. For example, starch is exempt from the duty leviable on it, if it is used in the factory of production for further manufacture of glucose and dextrose - on which separate duty is leviable. There are also exemptions in respect of finished or semi-finished products, if dutiable raw materials or intermediates are used in their manufacture e.g., articles of plastics (with some exceptions) are exempt from duty, if they are manufactured out of duty paid plastic resins.

OTHER CASES

2.34 Another provision in the Central Excise Rules for mitigating the burden of cumulative taxation is to be found in Rule 56-B. It provides for movement of semi-finished goods, which though excisable but are not in a state of marketability. This enables the completion of certain manufacturing processes for which the facilities may not be available with the producer and their return thereafter to the factory of the original manufacturer. The rule also provides for the removal of goods on payment of duty from the premises of an assessee who receives such goods for completion of the manufacturing process. The movements under this rule are allowed at the discretion of the Collectors of Central excise.

MOVEMENTS UNDER RULE 56-B

2.35 The preceding review brings out the following salient features of the Indian excise tax system:

(a) To start with relatively few products - mostly in the nature of mass consumption goods - were taxed. With the growing needs of revenue emphasis shifted to major inputs. The tax base was then widened on a selective basis, year after year, till almost the entire range of manufactured products were covered under excises in the year 1975;

(b) The consideration of progression has played an important role while fixing the rates on final products, and there has been an attempt to tax the goods consumed by the lower income groups at lower rates and charge higher duties on products consumed by the upper income groups. Various other considerations have also influenced the rate structure, which include use of excises to correct imbalances between demand and supply and promotion of export;

(c) The power to grant exemptions has been extensively used by Government for achieving various objectives. A good number of exemptions have been given with a view to assisting and encouraging the growth of cottage and small scale producers and protecting them from competition from larger manufacturers. There are others which have been granted for various end-uses subject to elaborate conditions being satisfied - often leading to complications in the matter of tax administration;

(d) A heavy reliance has been placed on the taxation of inputs (particularly some basic raw materials) which has persisted even when the excises have become almost universal in character. Though some procedures have been evolved to mitigate the distortions caused by taxation of inputs as well as final products, their use is limited and not extensive;

(e) There has been a shift from specific to ad valorem duties with a view to making revenues more elastic with reference to prices and national income, but still a substantial proportion of excise collections accrue from specific duties.

(f) The major proportion of revenue from consumer products is contributed by a select range of mass consumption goods. However, the share of revenue, realised from certain important wage goods in the total excise realisations has been on the decline, in the last few years;

(g) The variety of considerations influencing the taxation of various goods together with the large number of exemptions have resulted in a complex tax structure. There is a multitude of rates on consumer products, raw materials, intermediates and other inputs which differ widely not only between commodity groups but even within the same commodity group;

(h) Different schemes of excise duty collections have been evolved over time and emphasis has shifted from physical control to self-assessment. Separate schemes have been introduced for duty collections from small scale producers.

(i) Despite all the changes in tax policies and producers, the tax administration is still basically governed by the law enacted in 1944 - with certain amendments and rules made under it. The need for a comprehensive new law has been voiced and even accepted in principle, but the original enactment is still in force.

We have dealt with these aspects and have made some recommendations in Part I of our Report. In this Part, we discuss them more fully later.

TABLE 1 - COMMODITY-WISE REVENUE FROM UNION EXCISE DUTIES (1976 - 77)

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S. No.	Description of goods	Revenue for 1976-77 (Revised Estimates)
(1)	(2)	(3)
	A FOOD AND BEVERAGES	
1.	Sugar (including khandsari)	242.40
2.	Tea	62.00
3.	Aerated waters	14.20
4.	Food products	8.80
5.	Prepared or preserved foods	7.50
6.	Coffee	6.25
7.	Confectionery and chocolates	2.35
8.	Glucose and dextrose	1.90
	Total A - Food and beverages	345.40
	B VEGETABLE OILS	
9.	Vegetable product	18.50
10.	Refined vegetable oils	1.95
	Total B - Vegetable oils	20.45
	C TEXTILES	
11.	Rayon and synthetic fibres and yarn	276.00
12.	Cotton fabrics	121.80
13.	Cotton twist yarn and thread	72.40
14.	Rayon or artificial silk fabrics	52.00

(1)	(2)	(3)
15.	Yarn, not elsewhere specified	51.00
16.	Woollen fabrics	11.70
17.	Wool tops	8.20
18.	Woollen yarn	6.80
19.	Coated textiles	0.10
20.	Textile fabrics, not elsewhere specified.	0.02
	Total C - Textiles	600.02
	D DRUGS AND MEDICINES	
21.	Patent or proprietary medicines	53.80
	Total D - Drugs and Medicines	53.80
	E TOBACCO	
22.	Cigarettes	366.00
23.	Tobacco (un-manufactured)	102.00
24.	Biris, snuff and chewing tobacco	34.50
24A.	Cigars and cheroots	3.00
25.	Smoking mixtures	1.10
	Total E - Tobacco	506.60
	F PETROLEUM PRODUCTS	
26.	Motor spirit	415.00
27.	Refined diesel oils and vaporising oil	315.00
28.	Kerosene	167.00

(1)	(2)	(3)
29.	Petroleum products, not otherwise specified.	55.00
30.	Blended or compounded lubricating oils and greases	47.00
31.	Furnace oil	45.50
32.	Diesel oil, not otherwise specified	23.00
33.	Asphalt and bitumen	14.00
34.	Calcined petroleum coke	3.50
	Total F - Petroleum Products	1085.00
	G METALS	
	(a) Iron and steel	
35.	Iron or steel products	254.00
36.	Iron in any crude form	9.00
37.	Steel ingots	9.00
38.	Tin plate and tinned sheets	3.50
	Total G(a) - Iron and steel	275.50
	(b) Non-ferrous metals	
39.	Aluminium	113.00
40.	Copper and copper alloys	19.60
41.	Zinc	7.80
42.	Lead unwrought	0.33
	Total G(b) - Non-ferrous metals	140.73

(1)	(2)	(3)
	H CHEMICALS	
43.	Fertilisers	95.00
44.	Artificial or synthetic resins, plastic materials and articles thereof.	67.00
45.	Synthetic organic dyestuffs	35.00
46.	Paints and varnishes	20.00
47.	Chemicals like calcium carbide bleaching powder etc.	11.00
48.	Caustic soda	9.60
49.	Organic surface active agents	8.80
50.	Gases	7.45
51..	Soda ash	4.20
52.	Acids	3.75
53.	Optical bleaching agents	3.00
54.	Carbon black	2.90
55.	Sodium silicate	2.70
56.	Glycerine	2.25
57.	Starch	2.00
58.	Rubber processing chemicals	1.60
59.	Menthol	0.45
60.	Camphor	0.35
	Total H - Chemicals	277.05

(1)	(2)	(3)
	I OTHER SPECIFIED MANUFACTURED GOODS	
61.	Cement	138.30
62.	Tyres and tubes	130.00
63.	Paper	84.00
64.	Motor vehicles	75.00
65.	Jute manufactures	42.00
66.	Matches	38.00
67.	Refrigerating and air conditioning appliances and machinery	24.50
68.	Electric batteries and parts thereof	23.80
69.	Electric wires and cables	23.50
70.	Glass and glassware	23.50
71.	Rubber products	21.20
72.	Metal containers	21.00
73.	Electric motors	18.00
74.	Cosmetics and toilet preparations	16.20
75.	Soap	15.00
76.	Motor vehicle parts	12.50
77.	Chinaware and Porcelainware	12.00
78.	Electric bulbs and tubes	10.60
79.	Plywood	10.00
80.	Asbestos cement products	8.50
81.	Rolling bearings	8.50

(1)	(2)	(3)
82.	Electric fans	8.20
83.	Wireless receiving sets	8.00
84.	Welding electrodes	6.50
85.	Electrical stampings and laminations	5.65
86.	Footwear	5.40
87.	Office machines	4.95
88.	Steel furniture	4.40
89.	Internal combustion engines	4.15
90.	Bolts, nuts and screws	4.05
91.	Power driven pumps	3.75
92.	Cinematograph films	3.70
93.	Coated abrassives and grinding wheels	3.50
94.	Mineral fibres and yarn	3.15
95.	Jute twist, yarn and thread	3.00
96.	Tooth paste	2.90
97.	Specified cutting tools	2.50
98.	Cellophane	2.20
99.	Pilfer proof caps	2.10
100.	Gramophones and parts thereoı	2.00
101.	Tool tips	2.00
102.	Crown corks	1.90
103.	Graphite electrodes and anodes	1.85
104.	* Domestic electrical appliances	1.85

(1)	(2)	(3)
105.	Wire ropes	1.80
106.	Motor starters	1.65
107.	Safes, strong boxes etc.	1.30
108.	Electricity supply meters	1.25
109.	Photographic apparatus and goods	1.10
110.	Pressure cookers	0.85
111.	Playing cards	0.80
112.	Adhesive tapes	0.65
113.	Vacuum flasks	0.60
114.	Permanent magnets	0.60
115.	Synthetic rubber	0.50
116.	Zip or slide fasteners	0.45
117.	Tape recorders	0.40
118.	Work trucks	0.40
119.	Certain parts of wireless receiving sets	0.38
120.	Cinematograph projectors	0.35
121.	Electric insulating tapes	0.30
122.	Computers	0.30
123.	Linoleum	0.30
124.	Typewriter ribbons	0.24
125.	Slotted angles and channels	0.12

(1)	(2)	(3)
126.	Mechanical lighters	0.02
	Total I - Other Specified Manufactured Goods	858.16
	J MANUFACTURED GOODS, NOT OTHERWISE SPECIFIED	
127.	Goods falling under Item No. 68	34.00
	Total J - Manufactured Goods, not otherwise specified	34.00
	Grand total	4196.71
	(a) Cesses on oil and oil seeds, copra, cotton, coal and coke, rubber, salt, iron ore, crude oil, limestone, dolomite and tobacco	88.14
	(b) Miscellaneous	6.60
	Grand total of all Union excise duties (gross)	4291.45
	Deduct-refunds etc.	114.85
	Grand total - Union excise duties (net)	4176.60

Note:— Revenue figures indicated under Col. 3 include estimated realisations from additional duties of excise in lieu of Sales tax, auxiliary duties of excise and cesses - wherever applicable.

Source : Explanatory memorandum on the budget of the Central Government for 1977-78.

TABLE 5 - EXCISABLE GOODS NOTIFIED UNDER RULE 56-A OF THE CENTRAL EXCISE RULES, 1944.

S. No.	Description of goods
1.	Vegetable product
2.	Pigments, colours, paints, enamels, varnishes, blacks and cellulose lacquers
3.	Synthetic organic dyestuffs
4.	Synthetic organic products of a kind used as organic luminophores: Products of the kind known as optical bleaching agents, substantive to the fibre
5.	Patent on proprietary medicines
6.	Nitric, Hydrochloric and Sulphuric acids
7.	Refined Diesel oil
8.	Gases
9.	Soap
10.	Organic surface active agents (other than soap) surface active preparations and washing preparations, whether or not containing soap, manufactured or packed with the aid of power or of steam for heating
11.	Artificial or synthetic resins and plastic materials and cellulose esters and ethers, and articles thereof including polvurethane foam and articles made of polyurethane foam falling under item No. 15A of the First Schedule to the Central Excises and Salt Act, 1944 (1 of 1944)
12.	Plywood
13.	Paper and paper boards
14.	Cotton twist, yarn and thread, all sorts
15.	Woollen yarn
16.	Cotton fabrics
17.	Man-made fabrics falling under item No. 22 of the First Schedule to the Central Excises and Salt Act, 1944 (1 of 1944)

S. No.	Description of goods
18.	Asbestos cement products
19.	Steel ingots
20.	Copper and copper alloys
21.	Iron or steel products excluding pipes and tubes other than seamless pipes and tubes
22.	Zinc
23.	Aluminium
24.	Lead
25.	Tin plates and tinned sheets, including tin taggers, and cuttings of such plates, sheets, or taggers
26.	Internal combustion engines
27.	Refrigerating and air-conditioning appliances and machinery, all sorts, and parts thereof
28.	Electric motors, all sorts and parts thereof
29.	Electric batteries and parts thereof
30.	Electric fans
31.	Wireless receiving sets
32.	Electric wires and cables
33.	Motor vehicles and tractors (including agricultural tractors)
34.	Footwear
35.	Gramophones and parts thereof
36.	Jute manufactures
37.	Jute twist, yarn, thread, ropes and twine, all sorts
38.	Confectionery and chocolates

S. No.	Description of goods
39.	Prepared or preserved foods
40.	Glucose and dextrose and preparations thereof
41.	Fertilizers
42.	Steel furniture and parts of such furniture
43.	Lubricating oil falling under item No. 11A of the First Schedule to the Central Excises and Salt Act, 1944 (1 of 1944)
44.	Zip or slide fasteners and parts thereof
45.	Blended or compounded lubricating oils & greases
46.	Calcined petroleum coke
47.	Vacuum flasks and other vacuum vessels and parts thereof
48.	Cinematograph projectors and parts thereof
49.	Wire ropes of iron or steel
50.	Rubber processing chemicals, namely:
	(1) accelerators
	(2) antioxidants
51.	Starch; including dextrine and forms of modified starch
52.	Mineral fibres and yarn and manufactures therefrom

CHAPTER 3

CENTRAL TAXATION — 2. CUSTOMS DUTIES

HISTORICAL BACKGROUND

3.1. A duty on imports is among the oldest forms of taxation. Even in the 4th Century B.C., Kautilya in his Arthashastra laid down certain principles for the collection of tolls on merchandise which was imported or exported. The rationale behind this approach seems to have lain in the fact that most communities were and had to be self-sufficient, in respect of their basic needs and what was imported was mainly in the nature of luxury or fancy products. However, as countries developed and progressed, the character of international trade began to undergo a change. Not only silks and spices but cotton and grain began to move across the seas. By the time Adam Smith published his classic 'Wealth of Nations', which in a sense laid the foundations of modern economic thought, he was able to make out a convincing case for free trade. Although his work and that of his successors had a profound influence, particularly in his own country, Great Britain, a number of factors led policy makers to depart from his doctrine. Considerations of revenue, though they were there, were not the most important of these. The desire to foster domestic industries by protecting them from foreign competition, the stimulation of employment opportunities and the need to achieve a balance in the country's external payments by restricting, through tariffs, the domestic consumption of imported goods have, at least in developed countries, become the major elements which were taken into account in framing the import tariff. Developing countries have, in recent years, been relying on import control as an additional and sometimes the main, instrument for the purpose.

3.2. In tracing the evolution of import duties in India, we find that in the time of the Moghuls the duty did not exceed 5 per cent ad valorem. There was also an elaborate system of internal transit dues, which was a concomitant of the break-up of the Moghul Empire and the coming into being of a number of independent authorities. These internal transit dues had become such a serious impediment to trade that the East India Company, in their early days, had sought and later demanded an exemption from payment of these dues. The inland duties were abolished in 1844. The various duties on sea-borne trade were placed on a legal footing in 1803. Different customs regulations seem to have been introduced and repealed, or revised, rather frequently, in the first half of the 19th century.

3.3. In the early period of British rule, the three Presidencies, namely, Bengal, Bombay and Madras, had each their own independent Customs regulations and the rates of duties varied from presidency to presidency. The separate provincial rates of duties were replaced by a uniform all India tariff in the year 1859 when the tariff structure was first rationalised under the Customs Duties Act, 1859. The rationalisation of tariff structure by this statute was, it seems, only incidental, the primary purpose being one of tapping newer sources of revenue. Schedule A to this Act listed 23 items on which import duty was leviable. In this Schedule, the free list convering 9 duty-free items was given first and the dutiable articles followed. There was also a residuary item which convered all items not specifically enumerated, which were chargeable to duty at 10 per cent. The duties on all the articles excepting certain wines, liquors and spirits, were ad valorem.

3.4. The tariff structure has since then undergone numerous changes from time to time under various enactments. In 1860, the differential duties on British and foreign goods, which had been

introduced in 1848, were withdrawn and nearly everything imported into India was charged to duty at 10 per cent ad valorem and the duty on cotton yarn was raised from 3.5 per cent to 5 per cent. In 1862, the duty on cotton piece goods was reduced to 5 per cent and that on yarn to 3.5 per cent. The general duty of 10 per cent ad valorem was reduced to 7.5 per cent in 1864 and still further to 5 per cent in 1875. With a view to achieving a better classification of the goods, the tariff was revised through the Indian Customs Duties Act, 1867, the revised Import Schedule enumerated all articles liable to customs duty in alphabetical order. There was no import duty on articles not enumerated in the Schedule. The same pattern of alphabetical enumeration was followed in the Import Schedule to the Indian Customs Duties Act, 1870, Indian Tariff Act, 1871 and Indian Tariff Act, 1875.

3.5 The Indian Tariff Act, 1882 removed all import duties except on (i) arms, ammunition and military stores, (ii) liquors; (iii) oil; and (iv) salt. In the year 1888, a duty of ½ anna per gallon was imposed on petroleum. In 1894, following a change in the sterling-rupee exchange rate, customs duties were reimposed. Simultaneously, an attempt to categorise dutiable items in different schedules, and the grouping of the items in broad categories in each schedule was made in the Indian Tariff Act, 1894. There was a general residuary item (Item 78) in the schedule covering all other non-specified articles, with a rate of duty of 5 per cent. Thus, in 1894, the previous trend towards free trade culminating in the 1882 Act was reversed and general import duties were reimposed and even extended to some previously exempted articles like cotton piece goods.

3.6 The tariff structure introduced in 1894 remained in its main essentials unaltered till World War I. In general, it consisted of a low uniform rate of duty imposed on nearly all imports, while liquor and tobacco were taxed at comparatively high rates. In 1916, the financial burden imposed by the war necessitated an enhancement of the duties.

3.7 At the end of World War I, the general rate of import duty was 7.5 per cent with machinery and iron and steel paying duty at 2.5 per cent sugar at 10 per cent and motor spirit at 6 annas a gallon. The general rate was raised successively to 11 per cent and 15 per cent respectively in the years 1921 and 1922. Other changes made in these two years included enhancement of the duties on liquors, tobacco and sugar and the levy of a high specific duty on matches. The duty on certain articles in the nature of luxuries, such as, motor cars, silk piece-goods and watches, was raised to 30 per cent. Cotton yarn which, since 1896, had been free, was taxed at 5 per cent. On several other items also, duties were raised.

3.8 Prior to 1923, the policy pursued by the Government was based on the philosophy of free trade and the changes effected in the import duties were on revenue, rather than protective, considerations. In that year, following the recommendations (excerpte below) of the Indian Fiscal Commission (1921-22), Government accepted the policy of discriminating protection.

PRINCIPLE OF PROTECTION

"(a) That the Government of India adopt a policy of protection to be applied with discrimination along the lines indicated in the Report.

(b) That discrimination be exercised in the selection of industies for protection, and in the degree of protection afforded, so as to make the inevitable burden on the community as light as is consistent with the due development of industries.

(c) That the Tariff Board in dealing with claims for protection should satisfy itself —

(i) that the industry possesses natural advantages ;

(ii) that without the help of protection it is not likely to develop at all, or not so rapidly as is desirable ; and

(iii) that it will eventually be able to face world competition without protection.

(d) That raw materials and machinery be ordinarily admitted free of duty and that semi-manufactured goods used in Indian industries be taxed as lightly as possible.

(e) The industries essential for purposes of National Defence and for the develpment of which conditions in India are not unfavourable, be adequately protected, if necessary.

(f) That no export duties be ordinarily imposed except for purely revenue purposes, and then only at very low rates; but that when it is considered necessary to restrict the export of foodgrains, the restriction be effected by temporary export duties and not by prohibition." *

The Commission had also recommended —

(a) that a permanent Tariff Board should be set up ;

(b) that the tariff should consist partly of revenue and partly of protective duties, these two elements should be clearly distinguished,

(c) that the tariff should be elaborate with a view to removing ambiguities, and

(d) that while adopting a policy of preferential duties, guidelines stated in the report should be followed.

3.9 While accepting the policy of discriminating protection, Government did not go so far as to set up a permanent Board but appointed ad hoc Boards for investigating the claims of protection made by different industries. A regular Tariff Board could be appointed only in 1945, which was later succeeded by the Tariff Commission after Independence. On the basis of the recommendations of these bodies, the Government prescribed protective duties in respect of various industries from time to time.

3.10 In 1931, with the world economy in the grip of the Great Depression, the general rate of import duties which had remained at 15 per cent since 1922 was raised to 25 per cent. In the following year, with the conclusion of the Ottawa Trade Agreement, the principle of Imperial Preference came into play. The tariff was amended by the Indian Tariff (Ottawa Agreement) Amendment Act, 1932 to introduce a general rate of preference of 10 per cent. In 1934, a major rationalisation of the tariff classification by introducing 570 items arranged in 22 sections in the First Schedule to the Indian Tariff Act, 1934, was made but without any changes in the rates of duty. In 1939, several major changes were made in the tariff, to implement the scheme of preferences agreed to under the Indo-U.K. Trade Agreement.

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*Report of the Indian Fiscal Commission 1921-22, pp. XV and XVI.

3.11 During World War II, the rates of duty on several individual items were raised. Through the Finance Act, 1942, an overall surcharge of 20 per cent on almost all duties, was imposed. In 1944, the rate of surcharge on potable spirits and cigars, cigarettes and tobacco, was increased from 20 per cent to 50 per cent. In 1946, certain important adjustments were made in the duties on a number of items.

3.12 In the early years after Independence, while revenue considerations were not ignored, there was greater emphasis on making the import tariff help the country's industrial develpment.

POST-INDEPENDENCE DEVELOPMENTS

Accordingly, important reductions were made in the import tariff in 1948 and 1949. The duty on industrial plant and machinery was reduced from 10 per cent to 5 per cent and it was either removed or reduced on a number of raw materials for industries. Only the rates on a number of luxury articles were increased substantially.

3.13 Another series of changes became necessary as a result of India becoming a signatory to the General Agreement on Tariffs and Trade (The GATT) under which India agreed not to raise its* import duties on a wide range of items above a certain level or to allow them duty free entry on the understanding that the principal suppliers of those products would reciprocate by allowing duty free or low duty entry to some of India's principal exports to those countries. When the initial bindings under the GATT were negotiated, some consumer goods like razor blades were included in them because at that time it could not be conceived that these would be produced in the country itself and would be needing protection. At later stages, as the domestic production capacity was enlarged, the need to withdraw these bindings and offer others instead led to many changes as a result of re-negotiations. Similarly, some raw materials, such as copper, lead and zinc, which had also been subject to GATT bindings were re-negotiated at later stages because it was felt that they should not remain duty free. Under the Tariff (Amendment) Act, 1949, a number of new tariff headings and also changes in the duty on various items were made to give effect to the commitments made by India under the GATT. At the same time, in order to give shape to the fiscal policy of free India, a Fiscal Commission was set up in 1949.

3.14 The Fiscal Commission, which examined the tariff policy pursued during the period following 1923, observed that the policy of discriminating protection had achieved a fairly large measure of success and that on balance the direct and indirect advantages to the community resulting from the protection granted to the major industries which received it had offset the burden on the consumers.* The Commission recommended continuance of the protection, but on the principles enunciated in its report. The protection of industries should, it stated, be related to an overall planning of economic development — otherwise, there might be unequal distribution of burden and uncoordinated growth of industries.** In relation to the General Agreement on Tariffs and Trade, the Commission was of the view that "it will not be to India's benefit to keep out of the GATT." In the matter of granting tariff concessions, India should concentrate on (a) capital goods, (b) other machinery and equipment, and (c) essential raw materials.

3.15 In 1950, the general rate of duty was 30 per cent and applied to all articles not otherwise specified in the Schedule (Item No.87). Many specified items were also taxed at 30 per cent. Luxury items, e.g. cigarettes, cigars and tobacco; wines and spirits; fireworks, art silk goods, plated

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* Report of the Fiscal Commission, 1949-50, Vol. I p. 331

** Ibid, op.339 and 340

were; motor cars; games and sports requisites; clocks and watches, smokers' requisites exposed cinema films; electric lighting bulbs, wireless apparatus; etc. were selected for specially high duties. 69 items were subjected to protective duties while 62 items which included grains, pulses, wheat, rice, dried skimmed milkpowder, salt, metallic ores, chemical manures, sulphur, raw hides and skins, raw rubber, books, sugar machinery, and agricultural machinery were entirely free. There were a few items, e.g., fuel oils, lubricants, raw film, coal-tar dyes, printer's ink, raw cotton, industrial machinery and plants, railway materials, etc., which carried low duties.

3.16 In the fifties, India's sterling balances began to decline and before the end of the decade concern over foreign exchange led to a major tightening of restrictions on imports through import licensing. This had a number of consequences. Imports of the high tariff items - usually luxuries or semi-luxuries - were drastically curtailed, if not totally banned. Their revenue potential was eroded. As a compensatory measure, the duties leviable on other products, even those deemed to be necessities, began to be raised from year to year resulting in a proliferation of rates. Secondly, the policy of not allowing anything to be imported which was being produced in sufficient quantities in the country, was adopted. Where domestic production was inadequate or limited, imports were allowed, but the volume of such imports was rarely enough to meet the entire domestic demand. Further the duties on them, on revenue considerations, were pretty high. In this altered climate, industries not only did not need to go to the Tariff Commission to seek protection but they preferred to avoid doing so, because the protection already available to them through import restrictions and revenue duties was usually more than what the Tariff Commission could be expected to recommend on a careful consideration of costs and the interests of consumers. While protective duties continued to be in force for those industries which had gone to the Tariff Commission, the occasion to impose new protective duties became less and less as the years went by and, in 1976, the Tariff Commission was wound up.

3.17 Referring to the multiplicity of rates, the Customs Re-organisation Committee, in its report submitted in 1958, had observed as follows:

> "Almost all multiples of 5 upto 100 are to be found in these rates. We appreciate that a Customs Tariff should normally make a distinction between various categories of goods, as for example, (1) essential and non-essential consumer articles; (2) raw materials for essential and non-essential industries; (3) protected and non-protected items, but the reason for prescribing different ad valorem rates of duty for articles falling within the same category is not clear."

The Tariff Revision Committee also referred to this in their Report when they observed :

> "We appreciate that this multiplicity of rates is in many cases due to the rates on individual items having been altered separately, at different times, for revenue purposes. It is, however, obviously necessary when a comprehensive review of the Tariff is being undertaken, to harmonise the rates of duty on different articles and avoid unnecessary distinctions."

3.18 Around the middle of the year 1965, India's foreign exchange reserves had come down to a critically low level of less than Rs. 100 crores which was hardly sufficient for meeting the seasonal swings in the country's international trade and payments, leave alone unforeseen contingencies.

It was felt that the attempt to deal with the situation through a tightening of import control alone was not the right answer, because the delays in the issue of import licences could do considerable damage to the economy. Various malpractices also were seen to be developing. Import licences were sold at a premium because with restricted supplies, the difference between domestic price and import price was far greater than the import duties levied on them. The scarcity of essential imports also meant that often an industrial unit which had got an actual-user licence for a raw material or component found it more profitable to sell the product than to undertake its processing. The desirability of liberalising import control and using high tariff as a means of keeping the volume of imports down and checking abnormal profits of importers was emphasized from many quarters.

3.19 It is against this background that a wide ranging rationalisation of the import tariff was undertaken in August, 1965. As a result, broadly three rates came into effect namely, 40 per cent, 60 per cent and 100 per cent ad valorem. The general statutory rate of import duties for machinery was fixed at 40 per cent but the effective rate was limited to 35 per cent for some time. The rate of import duty on basic industrial raw materials, such as prime steel and non-ferrous metals, was also fixed at 40 per cent. For most of the processed industrial materials, the duty was 60 per cent. For fully manufactured goods, by and large, the rate was 100 per cent. This rate structure was changed following the devaluation of the rupee in June, 1966. The rates of import duty were scaled down in order to prevent the landed cost of all imported goods going up to the full extent of the devaluation of the rupee. In the process, various rates of import duties emerged. The most important changes were in respect of those articles which were chargeable to duty at 40 per cent. and 60 per cent. The rates in these articles were brought down to 27.5 per cent and 50 per cent respectively. The rates of import duties which were scaled down after devaluation were, however, gradually restored over the years to the pre-devaluation levels mainly on revenue considerations Though there were only three standard ad valorem rates, the effective rates of duty in fact were seven — 15 per cent, 27.5 per cent, 35 per cent, 40 per cent, 50 per cent, 60 per cent, and 100 per cent.

3.20 Another attempt to rationalise the import tariff was made in May, 1971, when the above seven ad avalorem rates of duty in force were replaced by four rates of import duty, namely, 30 per cent, 40 per cent, 60 per cent and 100 per cent on the pattern introduced in 1965. This is the structure of what are known as basic import duties that exists at present. Import duty at 30 per cent is applied to iron and steel. Capital goods, such as plant and machinery, and basic raw materials, are chargeable to duty at the rate of 40 per cent. The raw materials subject to this rate of duty include, among other things, raw rubber, wood pulp, asbestos raw, lubricating oils and greases, dyeing and tanning substances, non-ferrous metals and metallic ores and concentrates. The 60 per cent rate is applied to processed industrial raw materials, semi-finished goods and intermediate products (including chemicals and bulk drugs and medicines). All goods that could be described as consumer items, as well as a number of other fully processed products (e.g., smaller ball bearings) attract a basic import duty at the rate of 100 per cent.

BASIC IMPORT DUTY

3.21 The general rate structure of import duties given above was not without a number of exceptions. Thus, while the basic duty on mild steel was 30 per cent, the duty on stainless steel sheets prior to the 1977-78 budget was 300 per cent. - since reduced to 200 per cent - on the consideration that they were used mainly for making utensils and the use of precious foreign exchange for this purpose had to be discouraged to the maximum possible extent. However, the duty on stainless

steel plates, sheets and strips, required for the manufacture of specified capital goods, equipments and components, is 40 per cent. Certain products are exempt from import duty either on the consideration that their consumption should not be taxed, e.g., food grains, skimmed milk-powder and books, or because they are important raw materials for domestic industries for which indigenous supplies are non-existant or inadequate, e.g., sulphur, or because they are primarily meant for manufacture of export products, e.g., raw cashew, raw jute and rough diamonds.

3.22 A significant development since 1971 in regard to basic import duties is the change made in the preferences under Indo-United Kingdom Trade Agreement and the bindings under GATT. These were in existence from 1939 and 1949 respectively. As a result of re-negotiations in 1971 and 1973, many of the items whose tariffs ware bound under the GATT were released on consideration of protection to indigenous industry and revenue. More important of the items thus released are raw wool, staple fibre, copper unwrought, agricultural tractors, tallow, certain coal-tar dyes, wood pulp, high speed and alloy steel, and certain raw materials for the plastic industry. Subsequently, in 1975, a general waiver from GATT bindings was secured in anticipation of the switch-over to the new Customs Tariff based on Customs Co-operation Council's Nomenclature, so that the rates of duties on GATT-bound items could be suitably recast. Following the waiver, some modifications were made in the budget for 1976-77, but a number of items continue to be bound under because, in return, the countries which are the main suppliers of these items have bound their tariff either at the low level or on a duty free basis for some of India's important exports to them. Pursuant to the termination of the Indo-United Kingdom Trade Agreement on 31st December, 1975, the preferential rates applicable were withdrawn in two phases. On Ist July, 1976, the quantum of preferences was reduced by 75 per cent and from Ist July, 1977, the remaining 25 per cent has also been withdrawn.

AUXILIARY DUTY

3.23 Under the Finance Act, 1963, Government took powers to impose a regulatory duty of Customs on all imports. The intention was to regulate the quantity of goods imported by changing the level of duties. The rates of regulatory duty were changed from time to time. Finally, the regulatory duty was abolished and in its place came an auxiliary duty effective from March, 1973. The auxiliary duty is levied on a sliding scale, as follows :

(a)	Where the basic duty is 'nil' or above but less than 60 per cent	5 per cent ad valorem
(b)	Where the basic duty is 60 per cent or more but less than 100 per cent	15 per cent ad valorem
(c)	Where the basic duty is 100 percent or above	20 per cent ad valorem

The auxiliary duty on crude petroleum is specific. A few products are exempt from it. The auxiliary duties are, in effect, an addition to the basic duties. Thus the effective rates of duty on iron and steel add up to 35 per cent; on basic raw materials to 45 per cent; on processed industrial materials and semi-processed goods to 75 per cent; and on consumer goods to 120 per cent.

3.24 ADDITIONAL IMPORT DUTY

In addition to the basic and auxiliary duties, there is an additional duty levied under the Customs Tariff Act, 1975 which is also known as a countervailing duty. The principle underlying a countervailing duty is that when an indigenous product is subjected to an excise levy, an equivalent addition should be made to the import duty to ensure that the protection provided by the import duty to domestic industry is not eroded. In the past, the countervailing duty was not levied in cases but only on a few identifiable products where it was felt that the margin of protection to the domestic producer was being unduly reduced on account of the excise. Initially this was done by adding, after the basic rate of duty in the Schedule itself, words to the effect "plus the excise duty for the time being leviable on like articles if produced or manufactured in India, and where such duty is leviable at different rates, the highest duty". As the number of excisable items increased, this system was found to be complicated and cumbersome. Accordingly, in February, 1963, a provision was made by amending the Indian Tariff Act, 1934 to insert a new Section 2A to provide for the levy of countervailing duty in all cases where excise duty was leviable on a like indigenous article. This section was further amended under the Finance Act, 1963 to revise the basis for the levy of countervailing duty in cases where excise duty is ad valorem so as to include in the value of imported articles all import duties chargeable on them. In theory, the justification for the levy of countervailing duty is to ensure that the level of protection to domestic industry is not undermined by the levy of excises. However, since the import duties themselves have been imposed on revenue considerations and in most cases would appear to be much higher than what is needed for protection to indigenous industry, the countervailing duty becomes an additional source of revenue, rather than a measure to ensure adequacy of protection to domestic industry. Further, the rationale behind the inclusion of import duty in the price of the imported product (for calculating the countervailing duty is the assumption that the import duty equalises the landed cost of the product with the domestic cost of its indigenous equivalent. Therefore, to ensure that the countervailing duty is equal to the excise duty paid by the domestic producer, the import duty has necessarily to be taken into account in calculating the countervailing duty. However, since the import duty is often much higher than what is needed to equalise the import price with domestic price, the inclusion of the import duty in the calculation of countervailing duty further raises the level of import duties without any conscious application of the mind of Government and Parliament as to whether what in essence is an increase in the import duty should be quite as high as it turns out to be.

3.25 EXPORT DUTIES

Export duties have been levied on different commodities from time to time. These indeed were an integral feature of the early tariff policy. During the early part of the British rule, these were levied at small ad valorem rates on many articles of export.* In 1860, all exports paid a 3 per cent duty. Though the rates were low and the duties were levied solely for purposes of revenue, the principle was regarded as unsound from the point of view of economics, and a consistent policy of abolition was pursued.** In 1867, the export duty schedule was reduced from 97 items to 9. In 1873, the duty on wheat was taken off. In 1875, the only commodities still paying export duties were rice, indigo and lac. The former two items were freed in 1880. In 1916, an export duty was imposed on jute - raw and manufactured. In 1917, the export duty on jute was doubled. Hitherto all export duties had been levied solely for the sake of revenue. But the export duty on raw hides and skins imposed in 1919 was put forward as a measure of assistance to the Indian tanning industry. It also contained another noval principle by providing for a rebate of two-thirds of the duty on hides and skins exported to the Empire and tanned there.*** The Indian Fiscal Commission (1921-22) felt that export duties

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*Report of the Taxation Enquiry Commission, 1953-54, Vol.II, p. 271

** Report of the Indian Fiscal Commission, 1921-22, pp.11-12

*** Ibid, p.14

should only be levied on articles of which India had a monopoly or semi-monopoly. The Indian Taxation Enquiry Committee, 1924-25, also endorsed this view.* The duty on raw hides and skins was abolished in 1935 only to be reimposed afterwards. During World War II, cotton cloth and yarn were subject to an export duty at 3 per cent ad valorem, but this was converted into an export cess in 1945. From 1946 and for a period of about 10 years thereafter, which covers the early post-independence period, export duties acquired a new importance. When in 1949 along with sterling the Indian Rupee was devalued against the doller, a considerable margin develped between the doller prices for hessian or burlap in the U.S.A. and the prevailing rupee prices in Calcutta. Rather than allow the jute industry to get more profits or let the American importer get it at a cheaper price than what was prevailing in the U.S. market, Government decided to step up the export duty on hessian substantially. A number of other export duties were imposed or enhanced in the context of the devaluation of the rupee as well as the spurt in external demand and prices following the Korean War. However, with the passage of time and with the desirability of giving a stimulus to Indian exports, which were facing increased competition from other countries as well as from substitutes, it became necessary to progressively scale down the export duties on many commidities, such as jute goods, tea, textiles and mineral ores, and by the end of the III Plan, these duties had virtually disappeared. In the wake of the 1966 devaluation, export duties were re-imposed on a number of items, but in course of time, they had to be brought down to ensure the competitiveness of Indian exports in overseas markets. However, even now when world prices are higher than Indian prices, or when it is considered desirable to put a damper on exports in the interests of domestic consumption, export duties are reimposed or enhanced. The latest instance of this kind is the export duty on tea which came into effect from 9th April, 1977. It is worth pointing out that Government have powers to impose and enhance export duties without prior approval of Parliament on the consideration that the tax does not fall on the Indian consumer. Presently, the export tariff schedule consists of 23 items (vide Table I appended to this Chapter).

3.26 While it is true that in conditions of a temporary spurt in world prices relative to Indian prices, export duties have from time to time been deployed and continue to be so used to prevent abnormal profits to exporters or an abnormal price rise in the domestic market, such fortuitous opportunities are becoming increasingly rare.

TRENDS AND COMPOSITION OF CUSTOMS REVENUES

3.27 Table 2 appended to this Chapter gives the trend of total customs revenues from the year 1950-51 onwards. The main component of customs revenues is the revenue from import duties, as may be seen from Table 3 appended to this Chapter. The revenue yield has, however been fluctuating, depending upon the changes in the Import Licensing Policy from time to time which, in turn, has been determined by the trend in the foreign exchange situation and also domestic production. The general trend in the contribution of export duties to revenues is downward. With the growing emphasis on expanding India's export trade, export duties have in the long run lost their potential as sources of revenue.

3.28 Table 4, appended to this Chapter, gives the break-up of imports during 1975-76 and 1976-77. It will be seen that out of the total imports of Rs.5015.15 crores in 1976-77, as much as Rs.3525.27 crores (70.29 per cent) were accounted for by maintenance imports consisting of raw

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* Report of the Indian Taxation Enquiry Committee, 1924-25 Volume I, p.127

materials and intermediates, components and spare parts, and metals. Food, cereals and edible products accounted for 19.49 per cent of the value of imports in that year. Thus, these two categories between them formed 89.78 per cent of total imports. Since foodgrains are exempt from import duty, the bulk of the revenues from import duty has been derived from duties on raw materials and intermediate products.

ELASTICITY OF IMPORT DUTIES

3.29 It was not possible to work out a reliable estimate of the income elasticity of import duties for a sufficiently long period of time, because of various abnormal events and developments in the import and foreign exchange fronts during the last 15 years or so, such as the devaluation of 1966 and sudden changes in import control policies. We could only make a crude estimate of elasticity for the relatively short period from 1969-70 to 1975-76. The income elasticity estimate for this period turned out to be as high as 1.72. This high figure is to be attributed partly to the liberalisation of import restrictions. Besides, there were steep increases in international prices and the duties being ad valorem, there was a sizeable increase in revenues. We cannot expect import duties to be equally income-elastic in the future. However, even under normal circumstances, they would be fairly responsive to growth in income and prices.

PROBLEM OF CLASSIFICATION

3.30 If all imports had been subject to the same rate of duty, the problem of classification would not arise. However, since duties are imposed after considering various relevant factors applicable to each class of goods and as the variety of products which are traded internationally has been growing in complexity and number, more often than not disputes arise regarding classification of goods. These can be minimised by having each tariff defined in sufficiently precise terms so as to leave as little room for doubt as possible about the correct classification of any product. It is also desirable that the nomenclature used by any one country should be easily intelligible and clearly understood in the countries from which the imports are coming. Attempts have been made from time to time to evolve international standards which are then adapted by different countries to suit their own needs.

CUSTOMS CO-OPERATION COUNCIL NOMENCLATURE — HISTORY OF THE NEW LEGISLATION

3.31 The present nomenclature of the customs tariff in India is set out in the Customs Tariff Act, 1975, the First Schedule of which contains the import tariff and the Second Schedule the export tariff. The Act of 1975 replaced the Indian Tariff Act, 1934. While the First Schedule of the latter Act was based on the 'Draft League of Nations' Nomenclature of 1931, known as the Geneva Nomenclature, the present First Schedule to the Customs Tariff Act, 1975 is based on the Customs Cooperation Council's Nomenclature (originally known as Brussels Tariff Nomenclature and hereinafter referred to as CCCN). The changes made in the nomenclature, specially of the First Schedule, are based mostly on the following recommendations of the Tariff Revision Committee set up in 1964.

"(1) The Committee has proceeded on the basis (indicated in its Interim Report and approved in general terms by Government) that the revised Tariff Schedule should adopt the broad structure of the Brussels Tariff Nomenclature (B.T.N.) with such contractions and expansions as might be necessary in the light of the country's

trade pattern, development needs and other factors and that in opening sub-headings, reference should be freely made to the Revised Indian Trade Classification (R.I.T.C.)

(2) It would be desirable to align the I.T.C. Schedule with the revised Tariff Schedule. If possible, the R.I.T.C. may also be modified and aligned with the B.T.N. and the revised Tariff Schedule."

Though the Government accepted the recommendations of the Committee, for various reasons the Bill to give effect to the revised nomenclature could only be enacted much later and came into effect from 2nd August, 1976.

3.32 The new tariff follows the numbering system of the CCCN, namely, 4-digit code with the first two digits representing chapters and the third and the fourth giving indications of the nomenclature heading numbers in each chapter. However, because of the merger of a very large number of nomenclature headings in different chapters, a modified numbering system has been adopted, such as, 01.01/06 signifying that six headings of the CCCN from 01.01 to 01.06 have been merged into one heading. Sub-headings have been identified by showing them in the respective order of serial numbers under each nomenclature heading, whether it be a merged heading or an unmerged heading of the CCCN. The section and chapter notes of the CCCN have by and large been maintained except where, as a consequence of the merger, editing changes have had to be resorted to. When the legislative changes were introduced, it was made clear that the intention of Government was to adopt and revise only the nomenclature part of the First Schedule and to base it on CCCN and to the extent possible, the rate structure of duties leviable would remain the same as in the First Schedule to the Indian Tariff Act of 1934. But it has been brought to our notice that due to the large scale merger of a number of items, the effective rates of duty on a number of products have become higher, particularly in the case of Dodecyl/Alkyl-Benzene, Stereoflongs, and cocoa beans.

3.33 As in the case of excise duties, there are a large number of exemptions from import duties which have been given on various considerations. The more important consideration has been to have no tax on certain types of products which are of interest to the lower income groups, such as, foodgrains and milk-powder. Also, when the need arose to import vegetable oils, on the same consideration it was made duty-free. Some industrial raw materials, like sulphur and others, are also likewise exempt from duty. The rest of the concessions arise out of an obligation that diplomatic personnel, etc., are entitled to import their personal and official requirements without paying duty. Similarly, for the development of Free Trade Zones, duty free treatment is provided to goods going into the specified areas. While the majority of exemptions from import duty are governed by international commitments or socio-economic considerations which arise on a continuing basis, exceptions are those which have been granted for specific end-uses.

EXEMPTIONS

3.34 The preceding factual review of the structure of customs duties in India as it stands today brings out the following salient features.

(a) Import duties have been used primarily for revenue purposes but they have also been used for giving protection to domestic industries and conserving foreign

exchange. In regard to the latter two functions, import control has been playing the major role.

(b) Attempts have been made from time to time to rationalise import duty structure by prescribing basic rates of duty which are more or less uniform for particular classes of goods, such as, capital goods, raw materials and consumer goods.

(c) However, with the imposition of countervailing duties, which are calculated on the basis of the CIF price plus the basic and the auxiliary duty applicable to the product, the final levies on different products present a bewildering variety of rates.

(d) The rates of duty applicable to consumer goods are the highest and the duties on raw materials and capital goods are the lowest, with semi-processed materials being taxed at intermediate rates. In actual fact, the contribution of consumer goods to the revenue on account of import duties is very small. This is because foodgrains which have accounted for the bulk of consumer goods imports have been duty free while the import of other consumer goods bearing high import duties has been severaly restricted and often banned through import control.

(e) Export duties have begun to perform more of a regulatory than a revenue earning function.

(f) A limited attempt has been made to bring Indian import tariff nomenclature in line with international practice.

We have discussed the above aspects and indicated the broad lines of reform in Part I of our Report. We present a fuller discussion of these later.

TABLE 1 — LIST OF GOODS SUBJECT TO EXPORT DUTY

S.No.	Description
1	Coffee
2.	Black pepper
3.	De-oiled groundnut oilcakes
4.	De-oiled groundnut meal (solvent extracted variety)
5.	Tobacco, unmanufactured
6.	Silimanite

Table -Contd.

S.No.	Description
7.	Kyanite
8.	Mica, including fabricated mica
9.	Seatite (Talc)
10.	Manganese ore
11.	Iron ore —
	(i) Lumpy iron ore
	(ii) Iron ore fines (including blue dust)
12.	The following Chromite ore and concentrates, namely:–
	(i) High grade fines and concentrates with Cr_2O_3 content 47 per cent and above
	(ii) Medium grade fines and concentrates with Cr_2O_3 content 35 per cent and above but below 47 per cent.
	(iii) Lumpy ore with Cr_2O_3 content 35 per cent and above but below 42 per cent.
	(iv) Low grade lumpy ore or fines or concentrates with Cr_2O_3 content below 35 per cent. and F O content above 23 per cent.
13.	Manganese dioxide
14.	Hides, skins and leathers, tanned and untanned, all sorts but not including manufacture of leathers
15.	Raw wool
16.	Raw cotton
17.	Cotton waste, all sorts
*18.	Jute manufactures (including manufactures of Bimlipatam jute or mesta fibre) when not in actual use as covering receptacles or binding, for other goods

*Presently, these two items are fully exempt.

Table - Concld.

S.No.	Description
*19.	Coir yarn
20.	Groundnut
21.	Animal feed
22.	Cardamom
23.	Tea.

*Presently, these two items are fully exempt.

TABLE 2 — TREND OF CUSTOMS REVENUES

(Rs. In Crores)

Year	Total Customs Revenue	Total Tax Revenue of Central Government	Col.(2) as percentage of Col.(3)	Net national product at current prices	Col.(2) as percentage of Col.(5)
(1)	(2)	(3)	(4)	(5)	(6)
	Rs.	Rs.		Rs.	
1950-51	157.16	404.53	38.84	9530	1.64
1955-56	166.70	485.07	34.36	9980	1.67
1956-57	173.23	573.13	30.22	11310	1.53
1957-58	179.99	695.77	25.86	11390	1.58
1958-59	138.29	715.12	19.33	12600	1.09
1959-60	156.11	812.28	19.21	12950	1.20
1960-61	170.03	908.92	18.70	13263	1.28
1961-62	212.25	1053.75	20.14	13987	1.51
1962-63	245.96	1285.04	19.14	14795	1.66
1963-64	334.75	1633.84	20.48	16977	1.97
1964-65	397.50	1820.69	21.83	20001	1.98
1965-66	538.97	2060.67	26.15	20637	2.61
1966-67	585.37	2306.50	25.37	23848	2.45
1967-68	513.35	2352.68	21.81	28054	1.83
1968-69	446.50	2509.84	17.78	28507	1.56
1969-70	423.31	2823.07	14.99	31606	1.34
1970-71	524.02	3206.80	16.34	34462*	1.52
1971-72	695.67	3872.44	17.96	36332*	1.91
1972-73	856.64	4509.70	18.99	39643*	2.16
1973-74	996.43	5073.38	19.64	49396*	2.01
1974-75	1332.90	6321.75	21.08	58137*	2.29
1975-76	1419.40	7608.78	18.70	60293**	2.35
1976-77	1490.45	8080.93	18.40	N.A.	

*Provisional

**Quick estimates

Sorce.- 1. Net National product - Pocket Book of Economic Information, 1966 Ministry of Finance (Deppt. of Economic Affairs) for the years prior to 1960-61. For subsequent years, Economic Survey of the Government of India, 1976-77.

2. Revenue figures - Directorate of Statistics & Intelligence (Central Excise & Customs) N. Delhi.

TABLE 3 - CONTRIBUTION OF IMPORT AND EXPORT DUTIES TO TOTAL CUSTOMS REVENUES

(Rs. Crores)

Year	Import duties	Export duties	Total Customs Revenue
1950-51	109.80	47.36	157.16
1955-56	128.94	37.76	166.70
1960-61	156.91	13.12	170.03
1965-66	536.83	2.14	538.97
1969-70	355.05	68.26	423.31
1970-71	461.40	62.62	524.02
1971-72	623.67	72.00	695.67
1972-73	766.77	89.87	856.64
1973-74	911.38	85.05	996.43
1974-75	1242.33	90.57	1332.90
1975-76	1336.12	83.28	1419.40
1976-77 (R.E.)	1370.29	120.16	1490.45

Source, — Report of the Taxation Enquiry Commission (1953-54);
Economic Division, Ministry of Finance (Department of Economic Affairs), and
Directorate of Statistics and Intelligence (Central Excise and Customs), New Delhi.

TABLE 4 — BREAK-UP OF IMPORTS BY MAJOR HEADS DURING THE YEARS 1975-76 AND 1976-77

S.No.	Major heads	1975-76		1976-77	
		Value	Percentage to total imports	Value	Percentage to total imports
(1)	(2)	(3)	(4)	(5)	(6)
1.	Maintenance Imports	3317.54	64.32	3525.27	70.29
	(a) Raw materials and Intermediate goods (excluding metals)	2363.03	45,82	2572.14	51.28
	(b) Components and spares	551.10	10.68	573.56	11.44
	(c) Metals				
	(i) Iron and steel	305.56	5.92	219.73	4.38
	(ii) Non-ferrous metals	97.85	1.90	159.84	3.19
2.	Food, Cereals and Edible products	1398.91	27.12	977.34	19.49
3.	Complete machinery and equipment	357.84	6.94	435.60	8.68
4.	Essential finished goods	63.81	1.24	65.99	1.32
5.	Others including unclassified items	19.72	0.38	10.95	0.22
	Total	5157.82	100.00	5015.15	100.00

Source.— Office of the Chief Controller of Imports and Exports, New Delhi.

CHAPTER 4

INDIRECT TAXES AT THE STATE AND MUNICIPAL LEVELS

4.1 In this Chapter, we discuss the evolution and structure of indirect taxes levied by State Governments, of octroi duties levied by local authorities in many parts of the country as well as some taxes which although imposed by the Centre do not contribute to the Central exchequer but are exclusively for the benefit of the States.

4.2 TRENDS AND COMPOSITION OF STATE TAX REVENUES

As with the taxes levied by the Centre, the yield of taxes levied by the States has grown very rapidly during the last 25 years. From only Rs. 221.70 crores in 1950-51, States' own tax revenues rose to 3748.45 crores in 1976-77 (Table 1 below). The bulk of State tax revenues is now accounted for by indirect taxes. Their share rose from 63.3 per cent in 1950-51 to 86.94 per cent of the total tax revenues in 1976-77. Of these, sales taxation* is the most important and accounts for nearly 56.70 per cent of States* own tax resources; its share increased from about 26 per cent in 1950-51.

TABLE 1 — RELATIVE IMPORTANCE OF VARIOUS STATE TAXES

Source of revenue	1950-51	1960-61	1975-76	1976-77
	(Rs. in crores)		R E	
(1)	(2)	(3)	(4)	(5)
	(Rs.)	(Rs.)	(Rs.)	(Rs.)
DIRECT TAXES:				
1. Land revenue	49.56	91.19	196.12	199.33
	(22.36)	(21.36)	(5.73)	(5.32)
2. Agricultural Income -tax	3.59	9.71	15.99	16.75
	(1.61)	(2.13)	(0.46)	(0.44)
3. Stamps & Registration fees	25.98	43.54	228.89	243.64
	(11.73)	(9.58)	(6.70)	(6.50)
4. Other direct taxes	2.18	3.11	21.21	30.40
	(1.00)	(0.67)	(0.62)	(0.80)
TOTAL:	81.31	153.55	462.21	490.12
	(36.70)	(33.74)	(13.51)	(13.06)

*Sales taxation here includes general sales tax, motor spirit sales tax, Central sales tax and purchase tax on sugar-cane, and other agricultural products.

TABLE - Concld.

Source of revenue	1950-51	1960-61	1975-76	1976-77
	(Rs. in crores)		R E	
(1)	(2)	(3)	(4)	(5)
	(Rs.)	(Rs.)	(Rs).	(Rs.)
INDIRECT TAXES :				
5. Sales tax	58.02	158.74	1892.41	2125.50
	(26.18)	(34.90)	(55.32)	(56.71)
6. Excise duties	47.79	53.08	419.46	447.72
	(21.56)	(11.67)	(12.27)	(11.95)
7. Taxes on Vehicles	7.54	33.62	202.65	220.94
	(3.40)	(7.39)	(5.92)	(5.90)
8. Taxes on goods and passengers	0.11	5.56	160.10	170.66*
	(0.04)	(1.22)	(4.69)	(4.55)
9. Electricity duties	3.12	12.51	109.42	112.09
	(1.40)	(2.76)	(3.19)	(2.99)
10. Entertainment tax	8.06	15.60	142.09	154.30
	(3.64)	(3.42)	(4.15)	(4.11)
11. Other Indirect taxes and duties	15.73	22.24	32.40	27.12
	(7.08)	(4.90)	(0.95)	(0.73)
TOTAL :	130.37	301.35	2958.53	3 258.33
	(63.30)	(66.25)	(86.49)	86.94)
GRAND TOTAL :	221.68	454.90	3420.74	3748.45
	(100.00)	(100.00)	(100.00)	(100.00)

SOURCE: Finances of State Governments — Ministry of Finance, (Department of Economic Affairs)

Figures in brackets show the corresponding percentages to the total tax revenues of the States.

*This does not include Tamil Nadu figures, as the taxes on passengers, goods and vehicles are merged there.)

The share of land revenue, which was once the mainstay of tax revenues, now accounts for about 5.3 per cent of total of the revenues from State taxes. The steep decline in the relative importance of land revenue is due in no small measure to the anxiety of the State Governments to keep the direct tax burden on the agricultural sector at a relatively low level. State excise on liquor ceased to be a buoyant source of revenue as a result of the policy of prohibition adopted in varying degrees by different States. In consequence, sales taxation became the one source of revenue which State Governments developed to meet the increasing need for resources.

4.3 SALES TAXATION

Entry 48 of List II in the Seventh Schedule to the Government of India Act, 1935, vested the power to levy "taxes on the sale of goods and advertisements" in the Provincial Legislature to the exclusion of the Central Legislature. Acting under these powers, the Province of Bombay was the first to levy a tax on sales of tobacco in a limited way in 1938. In the same year, the Central Province also levied a retail tax on motor spirit and lubricants. This was followed by the levy of a general sales tax in Madras in 1939 at a low rate of half per cent to make good the loss of revenue due to prohibition. By 1950, almost all the States had introduced sales tax levies in their respective areas.

4.4 CONSTITUTIONAL PROVISIONS IN-TERPRETATION OF

A disconcerting feature of the growth of State sales tax systems prior to the enactment of the Constitution in 1950 was that each State also sought to tax an inter-State sale of goods as an internal sale, with the result that a single inter-State transaction was taxed by more than one State imposing a heavy and unregulated burden both on the consumer and the trade. Article 286 and Part XII of the Constitution relating to trade, commerce and intercourse within the territory of India were designed to rectify this position. The effect of the Constitutional provisions was:

(i) the power to levy "taxes on the sale or purchase of goods other than newspapers" vested in the State Legislature - (Entry 54 of the State List);

(ii) the power to levy "taxes on the sale or purchase of newspapers and on advertisements published therein" vested in Parliament (Entry 92/Union List);

(iii) by article 286, the State Legislature was prohibited from imposing a tax on the sale or purchase of goods outside the State or which took place in the course of import of goods into or export of goods out of the territory of India. The Article forbade the State from imposing a tax on sale or purchase taking place in the course of inter-State trade or commerce but made the ban subject to Parliamentary legislation to the contrary.

(iv) Article 286 also provided that the Legislature of a State was not competent to impose or authorise the imposition of a tax on the sale or purchase of any goods declared by Parliament by law to be essential for the life of the community unless the legislation was reserved for consideration of the President and has received his assent.

4.5 However, the interpretation of Article 286 became the subject matter of considerable litigation. The wording of the Articles of the Constitution and their interpretation by the Judiciary gave

ample scope for States to try to tax inter-State transactions in one way or another. The Madras High Court described the situation in the following words:— (22 Sales Tax cases 443)

> "It became a common phenomenon for the Tax Officers of one State to pitch their tents in another State and enforce the provisions of their sales tax laws over the exporting non-residents. It has naturally led to a great deal of confusion, inconvenience, unreasonable tax burden and harassment by the Tax Officers of the consuming State demanding and collecting taxes from non-resident dealers belonging to the exporting States."

4.6 TEC'S VIEWS ON SALES TAX

At this stage, the TEC, in the course of its comprehensive enquiry, went into the problems arising out of the then existing systems of sales taxation and the economic, administrative and legal complications that they gave rise to. Its recommendations covered :—

a) principles which should guide State governments in regard to Sales taxation

b) considerations on which Parliament should regulate the rate of Sales taxation of certain products and

c) the way in which the taxation of inter-State sales should be regulated.

4.7 AMENDMENTS TO CONSTITUTION

The Constitution (Sixth Amendment) Act, 1956 was a direct consequence of the TEC's recommendations. Parliament acquired the power to levy taxes on the inter-State sale or purchase of goods. Through an amendment to Article 269, the revenue arising out of taxation of inter-State sales were assigned to the States. Article 286 was also concurrently amended to enable Parliament to formulate by law the principles for determining when a sale or purchase of goods took place in the course of import of goods into or export of goods out of the territory of India. A further clause gave Parliament the power to declare goods, which are of special importance in inter-State trade and or commerce and subject the State's power to levy sales tax to such restrictions and conditions as Parliament might impose. The Central Sales Tax Act was a culmination of these several developments.

4.8 In the field of local sales tax laws, the TEC, after studying the then existing nascent systems of sales taxation in different States, recommended that these laws should generally have the following two elements, namely,—

(a) a general turnover tax, with few exemptions, to be levied at a low rate of half per cent, and

(b) a single-point tax on a list of special goods that could bear higher rates.

The general character of the turnover tax would ensure a broad-based coverage leading to a fairly high income elasticity of revenue, while the low rates would minimise any distorting effects arising from the multi-point character of the tax. The single-point tax would enable the States to impose a larger burden on the better-off sections of the population who might be expected to consume goods in the nature of comforts and luxuries. Apparently, because the TEC had recommended that the general tax should be levied only at a low rate, they did not devote any special attention to the problem of cascading.

4.9 In the development of the sales tax systems, subsequent to the submission of the TEC report early in 1955, the States did not adhere to the pattern recommended by the Commission. The imperative need to increase tax revenues at an accelerated pace in successive plan periods, the desire to attract industries and to encourage them to go to backward areas, considerations of administrative convenience and efforts to remove certain genuine difficulties of trade and industry led each State to make changes in their sales tax laws with the result that the sales tax systems display considerable differences from State to State.

EVOLUTION OF DIFFERENT SALES TAX SYSTEMS

4.10 Conceptually, three types of sales tax are levied; the single-point, the double-point and the multipoint, the last having the character of a general turnover tax. In practice, there are mixtures of these types in individual States. The majority of States impose in the main a single-point tax. They are Assam, Haryana, Himachal Pradesh, Jammu & Kashmir, Madhya Pradesh, Meghalaya, Nagaland, Orissa, Punjab, Rajasthan, Uttar Pradesh and West Bengal. In some of these States, certain goods, however, are taxed at more than one stage. Maharashtra and Gujarat have adopted the double-point system, Andhra Pradesh, Bihar, Karnataka, Kerala and Tamil Nadu formally impose a multi-point tax. Even in States having a multi-point levy, the major part of the revenue is now derived from items subject to a single-point tax. A large number of commodities were placed under a single point levy in Tamil Nadu with effect from 4.3.74. In all these States, a number of commodities, especially those classified as luxury goods, are taxed only at a single point. Except for Jammu & Kashmir and Rajasthan, other States having a single-point system formally impose the tax at the last point in the chain of transactions, but over the years the tax on a number of commodities has been shifted to the first point to minimise the scope for evasion. Variations in the system of sales taxation found in different States reflect adaptations to varying conditions and perhaps also historical factors. It is possible however, to discern a common trend towards the imposition of a single-point tax on several commodities. Attempts have also been made through the meetings of the Regional Councils for Sales Tax, set up by the Government of India under Article 263 of the Constitution, to bring about a measure of uniformity in the rates of taxation on particular categories of goods.

PATTERN OF RATE STRUCTURE OF SALES TAXATION

4.11 The rate of sales tax in the multi-point States is generally 4 per cent. This is the rate currently in force in Andhra Pradesh, Kerala, Karnataka and Tamil Nadu, though Bihar has a lower rate. Assuming that a commodity ordinarily passes through two or three stages before reaching the final consumer, a 4 per cent multi-point sales tax usually entails an incidence of 8 to 12 per cent tax on the price paid by the final buyer. In addition, the cascading effect accounts for a further increase in prices. Though there is no uniformity in the matter of selection of goods for single-point taxation in these States, by and large, luxury goods are taxed at only one point (mostly first sale in the State) and at rates varying from 12 to 15 per cent. Products which commonly come under this category are motor vehicles, arms, refrigerators and air-conditioning plants, radios, gramophones, cameras and films, watches, iron and steel safes cigarette cases and lighters. Another group of commodities taxed mostly at only one point is made up of goods of common use, such as cycles and cycle parts, edible oils, kerosene, coffee, tea, certain foodgrains, drugs and medicines as well as products like cement and fertilisers. The rates of tax for this latter category vary from 1 to 10 per cent. For facility of collection, the single-point tax is sometimes levied on the first purchase, as for example, on turmeric; paddy, coriander, green gram and black-gram, cashew nuts, chillies, etc. in Andhra Pradesh and rubber, cardamom and cashew-nuts in Tamil Nadu. Cardamom, shrimps and lobsters etc. are taxed in Kerala at the last point of purchase within the State of Kerala. Rates for these items vary from 2 to 5 per cent.

4.12 In the States following the single-point system, the rate of tax varies generally from 4 to 7 per cent. However, as in the multi-point tax States, a number of luxury articles are subject to a higher rate up to 15%. Commodities of common consumption like paper, powdered milk, edible oils, washing soaps, plastics, matches and kerosene are generally taxed at lower rates.

4.13 In all the States, some commodities are exempt from sales tax, though the list of exemptions is not uniform. Articles that are generally exempt are salt, fruits, vegetables, certain handicraft products and family planning appliances. Foodgrains are exempt in some States, while in others they are taxed at a concessional rate. In addition, those commodities which are taxed under separate enactments like electricity and in some States liquor are also exempt from general sales taxation. A brief account of the sales tax rates in some States on selected products is given in Appendix 6.

TREATMENT OF RAW MATERIALS AND INTERMEDIATE PRODUCTS UNDER SALES TAXATION

4.14 In principle, sales taxes make no distinction between consumer goods and inputs, or rather between sales to final users and those to producers. The sales tax on inputs, therefore, has an impact on the prices of final products similar to that of excise levies. The impact gets compounded by the interaction of sales taxes and excises, which we discuss in Chapter 5. However, like the provisions under rule 56-A etc. in respect of excises, most State laws provide for a limited measure of relief, through partial or full exemptions or concessional treatment, in regard to sales tax when intermediate products are sold to manufacturers. The practice in different States is briefly summarised below.

4.15 While some States grant total exemption from sales tax to raw materials sold to manufacturers, others extend only a concessional treatment. Gujarat, Haryana and Punjab are examples of States granting exemptions but the exemptions are generally subject to certain conditions. Thus, Gujarat limits the exemption to materials used in manufacturing taxable goods while in Pubjab the exemption is granted only if the taxable goods are sold within the State and the goods manufactured are not otherwise exempt from sales tax.

4.16 Most States, however, extend concessional treatment to raw materials rather than grant total exemption. Here again, there are variations in the manner and extent of concessions granted. Rajasthan taxes raw materials used for manufacture in the State, of goods for sale either within the State or in the course of inter-State trade at one per cent. In Kerala, the treatment accorded to component parts and raw materials is not uniform. On raw materials, the concession is conditional, if the final product bears sales tax within the State on sale. On the other hand, component parts get the concessional treatment even if the products manufactured out of them within the State do not bear any sales tax when transported outside the State on consignment basis or sold in the course of export.

4.17 In Uttar Pradesh the concessions seem to be designed particularly to help new industrial units. From 1974 onwards new industrial units enjoy complete exemption from tax - subject to a time limit of five years for backward districts and three years for other districts - on the purchase of raw materials and intermediate goods required in connection with the manufacture of 35 notified goods like bicycles, radios, television sets, transformers, electrical equipments and so on. After the expiry of the time limit, the manufacturers of notified goods can purchase the raw materials and intermediate goods at a concessional rate of 2½%. Other new units, not manufacturing

any ofthe 35 notified goods, can purchase raw materials at a concessional rate of 2½% for the same periods as prescribed for the notified goods in respect of backward and other districts, but on expiry of the prescribed period, they are required to pay full tax on their purchase of raw materials and component parts.

4.18 In Maharashtra, tax is levied at concessional rates on inputs sold to manufacturers without any condition about sales of the manufactured product being effected within the State. By a notification issued under the Bombay Sales Tax Act, a registered dealer who is a manufacturer, can purchase certain specified goods paying sales tax at the concessional rate of 3%. The specified goods cover inputs which are to be used for the purpose of manufacture of taxable goods in Maharashtra. In respect of goods exported out of the country, the tax paid on inputs is refunded by the State Government.

4.19 In West Bengal, a registered dealer is taxed at a concessional rate of one per cent only on sales to another registered dealer of goods required by the latter for use in the manufacture in West Bengal of certain notified commodities and 2 per cent in respect of similar sales to those manufacturing goods other than the notified ones.

4.20 In Andhra Pradesh, a registered dealer selling goods to another for use by the latter as a component part of certain products specified by the State Government which he intends to manufacture-inside the State for sale in the State or in the course of inter-State trade or commerce has to pay sales tax at a concessional rate not exceeding 3 per cent.

4.21 The concessions given in different States, it will be seen, are invariably limited to sales of inputs to manufacturers within the State. They are generally granted only in respect of materials, such as components, etc. which are physically embodied in the final products. Sometimes, they are confined to inputs of products which are meant for sale or consumption within the State. The basic concern underlying these concessions seems to be to attract industries into the State, to encourage their location in backward areas or to mitigate the adverse effects of taxation of intermediate products primarily to consumers within the State.

4.22 We have so far discussed the structure of States' sales taxation primarily with reference to its impact on the internal economy of the State. However, a noteworthy feature of sales taxation in the country is that it is based both on origin and destination principles. In other words, the same product gets taxed by the State in which it is produced and also by the State in which it is consumed. A number of consequences follow from this. Goods produced in one State but consumed or used in other States have to bear the burden of sales taxation by both States though not in equal magnitude. As a result, sales taxes levied by one State fall on the residents of other States. As indicated earlier, the TEC had made certain recommendations in regard to inter-State taxation.

THE CENTRAL SALES TAX ACT

4.23 The TEC's report also helped to clarify the thinking and to promote better understanding in the country as a whole as well as between the Centre and the States about the scope for Central regulation of sales taxation by States. In 1952, Parliament had enacted the Essential Goods (Declaration and Regulation of Tax on Sale or Purchase) Act, which declared a large number of goods as "essential goods" and thereby extinguished the right of States to tax them. This Act had evoked a considerable amount of criticism from the State Governments because they felt that it unduly restricted their powers of taxation. The TEC pointed out that the list of goods covered by the 1952 Act included those "which cannot except by a wide

interpretation be regarded as essential to the life of the community .....". The Commission also expressed the view that the purpose of the legislation could not be to restrict the power of a State to tax its own citizens but ito achieve some degree of uniformity in the tax burden on goods which were important in inter-State trade.

4.24 The Law Commission suggested the lines on which legal shape could be given to implement the TEC's recommendations. The Constitution (6th Amendment) Act and the Central Sales Tax Act (CST Act) were enacted in 1956 in pursuance thereof. The latter Act continues to be the instrument through which the Centre can regulate the taxation of goods of special importance in inter-State trade and also determine the manner and extent of taxation of inter-State sales of goods. For goods of special importance in inter-State trade, the Act provided that sales tax on them should be levied only once and at the maximum rate of one per cent. This rate was subsequently raised in response to pleas from State Governments to enable them to mobilise additional resources. The revisions raising the ceiling from the original level of 1% to 2%, 3% and 4% were effected in 1958, 1966 and 1975 respectively. The list of declared goods originally covered by the CST Act was expanded twice. Following the replacement of sales tax by the Additional Excise duty on textiles, tobacco and sugar in 1957, the list was expanded to include these items so that no State could find it worthwhile to opt out of the voluntary agreement not to levy sales tax on these items. The list was further expanded with effect from 7.9.1976 to include cereals (like paddy, rice, wheat etc.), crude mineral oil and pulses (like gram, dhalls, etc.). At present, the following commodities are included in the list of declared goods:—

(i) Coal including coke in all its forms but not including charcoal,

(ii) Cereals,

(iii) Cotton,

(iv) Cotton yarn,

(v) Cotton fabrics,

(vi) Crude oil,

(vii) Hides and skins,

(viii) Iron and steel,

(xi) Jute,

(x) Oilseeds,

(xi) Pulses,

(xii) Rayon and artificial silk fabrics,

(xiii) Sugar,

(xiv) Tobacco, and

(xv) Woollen fabrics.

4.25 The provisions of the CST Act relating to inter-State sales apply to :—

(a) movements of goods taking place from one State to another; or

(b) sales effected by transfer of documents or title to goods during the movement from one State to another.

The Central Sales Tax (CST) alone is leviable on the first inter-State sale of all goods other than newspapers, actionable claims, stocks, shares and securities and electrical energy. Subject to certain exceptions, the tax is collected in the State where the movement of goods originates and the tax so collected is retained by that State. As the revenue is assigned to the States, the administration of the CST Act is also entrusted to the State Governments. For the purpose of the assessment, collection and enforcement of the tax, the sales tax authorities can exercise the powers available to them under their respective local sales tax laws. The provisions of the laws of the State concerned regarding returns, assessments, appeals, reviews, revisions, etc. apply in their entirety to like matters under the CST Act. The rates of CST have also undergone three revisions, from the original rate of 1% recommended by the TEC. These rate revisions, which were justified on the ground of mobilising additional resources for the States, took place in 1963, 1966 and 1975, raising the rates respectively to 2%, 3% and 4%.

4.26 The current ceiling rates of 4% or the rate applicable to internal sales of the concerned goods, whichever is lower, on inter-State sale of goods apply only to goods sold to Governments (Central and State) and to registered dealers of goods in the importing State. If inter-State sales are made to parties other than a Government or a registered dealer, than a higher rate of tax is applicable. In respect of such sales of "declared goods" the CST is chargeable at twice the rate applicable to the same goods inside the exporting State (that is, the rate can go up to 8%). Inter-State sales of all other goods to parties other than a Government or a registered dealer are taxed at the rate of 10 per cent or the rate applicable to the sale or purchase of such goods inside the exporting States, whichever is higher. These provisions are subject to the exception that inter-State sales from a State of goods which are generally and unconditionally exempt from the sales tax within the State will be exempt from the CST also.

4.27 While States have full freedom to tax all internal sales and purchases within their territories and also collect taxes on inter-State sales under the conditions imposed by the CST Act, they are barred by the Constitution* from taxing sales in the course of exports out of the country. For quite some time, there was a controversy as to what should be taken to constitute an export sale. The controversy was set at rest by a recent Supreme Court judgment** under which it was ruled, inter alia, that the export transaction that would qualify for exemption from sales tax would be the transaction between the actual exporter (by contract) and the importer abroad, and not any other person who carries out the necessary process on behalf of the actual exporter. This judgment had far-reaching consequences especially in respect of canalised exports through public sector corporations, for which Indian exporters are not allowed to deal with any foreign party directly. To correct this anomalous situation, an amendment has since been made providing that the transaction immediately preceding the export of goods which is inextricably connected with that export and is effected in pursuance of an existing "back-to-back" contract, would be deemed as a sale in the course of export and would qualify for exemption from sales tax.

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*Article 286(1) of the Constitution read with Section 5 of the Central Sales Tax Act.

**Supreme Court judgment in the case of Md. Serajuddin vs State of Orissa.

4.28 Another measure of Central regulation of sales taxation which deserves mention is the scheme of Additional Excise duty in lieu of sales tax covering tobacco, sugar and textiles which, as rightly pointed out by the Fourth Finance Commission, is a kind of tax rental agreement between the Union and the States. Following the recommendations of the National Development Council (NDC) made in December, 1956, and after considering the Second Finance Commission's views, the Additional Duties of Excise (Goods of Special Importance) Act, 1957 was enacted to replace the sales tax on these commodities by an additional duty of excise. The levy, however, does not cover inputs used in the manufacture of these commodities, with the result that the States levy a sales or purchase tax on inputs like cotton yarn and sugar cane though they cannot tax textiles or sugar.

ADDITIONAL EXCISE DUTY IN LIEU OF SALES TAX

4.29 As agreed upon between the Central Government and the States, the proceeds of the Additional Excise duties are distributed to the States to compensate for the loss of corresponding sales tax revenue. The formulae applied for distribution of the proceeds among the States have been varied from time to time on the basis of the recommendations of the Finance Commissions. As recommended by the Sixth Finance Commission, the proceeds of the Additional Excise duties are distributed to various States taking into account population, State domestic product at current prices and production of the commodities subject to Additional Excise duties within the State, the weights allotted for the three criteria being in the ratio of 70:20:10 respectively.

4.30 The question of extension of this levy to more commodities was considered at length by the Fifth Finance Commission which felt that the full utility of such a scheme could not be realised unless the arrangements could be extended to other important commodities also. But the extension of Additional Excise duty to more commodities has met with opposition from the States who look upon the levy as causing erosion of their own taxing powers. Besides, the States have complained that Additional Excise duties have not been increased in keeping with the increase effected from time to time in basic excise duties. Further, until a few years ago, most of these commodities were taxed on a specific basis which, according to the States, resulted in lack of buoyancy in the revenues that they desired from Additional Excise; they, therefore, argued that their own sales tax revenues had been showing a higher rate of growth than the yield from the Additional Excise.* In view of the known opposition from the States, the Finance Commission had urged dialogue between the Central and State Governments on the issue. Subsequently, these issues were discussed at the meetings of the NDC in December, 1970, and it was decided to continue the existing scheme subject to the rates of Addtitonal Excise duty being stepped up to 10.8% of the value of clearances. As for as practicable, a ratio of 2 : 1 between the basic and Additional Excise duties was also to be kept. Further, it was decided that on as many of the items as possible, the Additional Excise duty would be levied on an ad valorem basis. In pursuance of these decisions, the Additional Excise duties were raised substantially in three successive Central Budgets of the years 1971 to 1973. The Sixth Finance Commission, in its report, observed** that -

> "it is clear from the memoranda submitted to us by the State Governments that they are, by and large, now satisfied with the manner in which Government of India have implemented the recommendations of the National Development Council and that they do not seek any material changes in the present scheme of levy of additional excise duties."

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*In actual fact since 1960-61 the increase in sales tax revenues is 13 times while the increase in revenues from Additional Excise duties is 7 times. But the increase in the former is largely due to extension of coverage and upward increase in the rates of some commodities. Therefore, the two ratios are not quite comparable.

**Report of the Finance Commission, 1973 - Chapter V, Para 4, Page 18.

4.31 SALES TAX ON MOTOR SPIRIT

Sales tax on motor spirit is generally levied under a separate enactment. The tax falls on motor spirit, diesel oil and also on certain other derivatives such as, aviation turbine fuel. Some States have, in recent years, merged it with the general sales tax. In some States, it is a single point levy on the first sale of motor spirit within the State. The rate structure adopted in some States is specific (i.e., in terms of paise per litre) and in others ad valorem based on either sale price or turnover. In general, specific rates vary from 7 paise per litre to 21 paise per litre, while the other rates vary from 9 per cent to 30 per cent of sale price or turnover as the case may be. The yield of sales tax on motor spirit has increased fairly rapidly during the last 15 years. From about Rs.16 crores in 1960-61, it is expected to exceed Rs.100 crores in 1976-77.

4.32 OTHER STATE TAXES

Apart from sales taxation (including the tax on motor spirit and purchase tax on sugar-cane) which, as mentioned earlier, accounts for more than 56 per cent of the revenues from State taxes, the other important indirect taxes levied by the States are :-

(i) State excise on liquor,

(ii) Tax on motor vehicles,

(iii) Tax on passengers and goods,

(iv) Entertainment tax, and

(v) Electricity duty.

The relative importance of these taxes in the scheme of finance of the State Governments is brought out in Table 1 of this Chapter.

4.33 Next in importance to sales taxation comes the State excise on liquor*, though its share in the totality of State's own tax revenues is much smaller - only about 12 per cent as of 1976-77. This share has, for reasons already stated, declined to this percentage from 21.6 per cent in 1950-51. The yield of State excise duties for all the States is estimated to be Rs.447.72 crores for the year 1976-77. The States which derive substantial revenue from this source are Andhra Pradesh, Bihar, Kerala, Madhya Pradesh, Maharashtra, Punjab, Rajasthan, Uttar Pradesh and West Bengal.

4.34 MEDICINAL AND TOILET PREPARATIONS (EXCISE DUTIES) ACT

Apart from State excise duties on liquor, there are also duties on medicinal and toilet preparations containing alcohol, narcotic drugs and narcotics, whose proceeds accrue to the States. These duties are imposed by virtue of Article 268 of the Constitution under a Central enactment, namely, the Medicinal and Toilet Preparations (Excise Duties) Act, 1955 and are administered by the States. The Act and the Rules follow the pattern of the Central Excise Act and Rules.

4.35 The rates of duty on the medicinal and toilet preparations containing alcohol, narcotic drug or narcotics had remained unchanged for a long period from 1964 to 1976. Under the Finance Act, 1976,

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*State excise is levied on intoxicants, rectified spirit, Indian-made foreign liquor, and country liquor like toddy, etc.

these rates were revised upwards by about 100% or more. At present, the rates broadly applicable to the most important medicinal and toilet preparations are as under:—

	Description	Rate of duty
(i)	Allopathic Medicinal preparations	
	(a) Patent or proprietary	20% ad valorem or Rs.3.75 per litre of the strength of London proof spirit, whichever is higher.
	(b) Unrestricted preparations which can be consumed as alcohol	Rs. 30.00 per litre.
	(c) Preparations containing narcotics or narcotic drugs	20% ad valorem
(ii)	Ayurvedic, Unani and other indigenous systems	
	(a) unrestricted preparations which can be used as alcohol	Rs.30.00 per litre
	(b) preparations which can be used as medicine	
(iii)	Homeopathic preparations	Rs.7.50 paise per litre
(iv)	Toilet preparations	60% ad valorem or Rs.7.50 per litre whichever is higher.

We understand that the occasion for raising the rates was the reported large scale misuse of certain medicinal preparations as alcoholic drinks.

4.36 Other indirect taxes levied by the States together account for about 18 per cent of the revenues from State taxes, each individual tax making a modest contribution, with the tax on motor vehicles yielding the highest at 5.90 per cent of the total. Taxes on motor vehicles are annual charges and are generally based on the type of vehicles and on the horse-power of the engine and, in the case of passenger vehicles, on the seating capacity and the class of route. In recent years, the growth in revenue from this source has been substantial in many States. Table 2 below shows that the aggregate of the revenues of 15 States was more than 6 times for 1976-77 compared to the corresponding figures for 1960-61:—

TABLE 2 — REVENUE FROM MOTOR VEHICLES TAX FOR SOME STATES

State		Revenue (in Rs. lakhs) 1960-61	1976-77(BE)
Andhra Pradesh	...	253	2794
Assam	...	64	272
Bihar	...	12	676
Gujarat	...	179	1265
Jammu & Kashmir	...	10	95
Karnataka	...	358	1600
Kerala	...	239	1737
Maharashtra	...	714	2375
Madhya Pradesh	...	188	780
Orissa	...	82	640
Punjab & Haryana	...	93	1521
Rajasthan	...	101	740
Tamil Nadu	...	533	4600
Uttar Pradesh	...	322	1801
West Bengal	...	219	1050
		3367	21946

SOURCE: Report of the U.P. Taxation Enquiry Committee (pp.287) and Finances of State Governments, Ministry of Finance (Department of Economic Affairs).

4.37 In addition to the tax on motor vehicles, most States also impose a tax on passengers and goods carried by road. The assessment is based on the amount of passenger fares or weight of goods or freight, as the case may be. Table 3 below shows that the revenues in respect of 12 States have increased five times from 1965-66 to 1976-77 :—

TABLE 3 — REVENUE FROM GOODS AND PASSENGERS TAXES FOR SOME STATES

State		Revenues (in Rs. lakhs) 1965-66	1976-77 (BE)
Assam	...	38	83
Bihar	...	78	582
Gujarat	...	340	2231
Jammu & Kashmir	...	11	86
Kerala	...	143	100
Karnataka	...	1 56	940
Madhya Pradesh	...	320	1480
Maharashtra	...	553	2733
Orissa	...	12	224
Punjab & Haryana	...	5 11	3416
Uttar Pradesh	...	4 26	1725
Rajasthan	...	1 95	1055
West Bengal	...	..	2200
		2783	14855

SOURCE : Report of the U.P. Taxation Enquiry Committee (pp.287 and Finances of State Governments, Ministry of Finance (Department of Economic Affairs).

The total yield from this tax is Rs. 171 crores excluding that of Tamil Nadu for which separate figures are not available. The taxes on vehicles and goods and passengers have been merged into one tax in

this State. The States which get a substantial amount of revenue from this source are Gujarat, Punjab, Haryana, Madhya Pradesh, Maharashtra, Rajasthan, Uttar Pradesh and West Bengal. Appendix 7 shows the rates of motor vehicles tax and goods and passengers tax in some States.

4.38 The last mentioned tax is really in the nature of a tax on transport services. The other taxes on services imposed by the State Governments are the entertainment tax and the electricity duty. The entertainment tax is an elastic source of revenue; its share in the total of the State taxes has increased considerably over the years. Entertainment tax forms about 4.11% of the States' Budgets for 1976-77 financial year, the total revenue being placed at about Rs.154.30 crores. Andhra Pradesh, Gujarat, Karnataka, Maharashtra, Tamil Nadu, Uttar Pradesh and West Bengal collect more than Rs.10 crores under this head, the highest being in Maharashtra (Rs.31.88 crores) followed by Tamil Nadu (Rs.21.31 crores) and Uttar Pradesh (Rs.17.40 crores). The tax is generally levied on the value of cinema tickets or as a show-tax at certain rates payable by the proprietor of a cinema show. In States where there are races, there is also a betting tax on the value of admissions, stakes and bets in race courses.

ELECTRICITY DUTY

4.39 State Governments are empowered to levy electricity duty on the energy consumed or sold in in the State (Vide Entry 53 of the State List Seventh Schedule of the Constitution). However, the levy is exempted in respect of certain activities. Article 287 of the Constitution inter alia provides for exemption from taxes on electricity consumed by the Government of India or consumed in the construction, maintenance or operation of Railways belonging to the Government of India. Article 288 provides for exemption from taxation by States in respect of electricity stored, generated, consumed, distributed or sold to any authority established by law for regulating or developing any inter-State river or river valley.

4.40 In Commissioner of Sales Tax vs. M.P. Electricity Board (25 STC page 188 SC) it was held that anything tangible or transferable from hand to hand or capable of delivery is "goods" and electric energy therefore falls within the definition of "goods". Following this judgment, the Central Sales Tax Act was amended in 1972, whereby inter-State sales of electric energy are not taxable. Consequently, there will not be any export of taxation from one State to another on electricity generated in one State and sold to another.

4.41 The electricity duty is partly a tax on consumption and partly a tax on an input. The revenue significance of the duty from electricity is not considerable in most States except in Bihar, Gujarat, Maharashtra and West Bengal. For 15 States (Table 4 below), the receipts from the duty rose from 3532 lakhs in 1965-66 to Rs.11145 lakhs in 1976-77 (i.e. slightly more than three times).

TABLE 4 - REVENUES FROM ELECTRICITY DUTIES - FOR SOME STATES

State		Revenues (in Rs. lakhs) 1965-66	1976-77 (BE)
Andhra Pradesh	...	2	6
Assam	...	7	44
Bihar	....	322	1008

State		Revenues (in Rs. lakhs) 1965-66	1976-77 (BE)
Gujarat	...	307	1425
Kerala	...	1	425
Madhya Pradesh	...	168	750
Tamil Nadu	...	433	145
Maharashtra	...	889	2921
Karnataka	...	217	600
Orissa	...	87	705
Punjab & Haryana	...	273	960
Rajasthan	...	38	206
Uttar Pradesh	...	89	425
West Bengal	...	699	1525
		3532	11145

SOURCE: Report of the U.P. Taxation Enquiry Committee (pp. 287) and Finances of State Governments, Ministry of Finance (Department of Economic Affairs).

4.42 Divergent approaches have been followed in the matter of levy. Some State laws provide for concessional rates for consumption in industries with total exemption for specified periods in respect of certain select industries, cooperative factories etc. A separate treatment for consumption for agricultural purposes is also a common feature of many of the Acts. Kerala levies the duty at a percentage on the price of the energy indicated in the invoice. Tamil Nadu levies an electricity duty at the rate of 3 paise per unit in respect of sale of energy to licensees. In addition, it also levies a tax, at a percentage of the price of energy, both on consumers supplied by the Electricity Board as well as on self generated consumption of energy. In States like West Bengal, Punjab, Gujarat, Maharashtra, the duties are levied on a slab system. In Maharashtra, the rates are higher for highly industrialised areas like Greater Bombay, Poona and Kirkee. A lower rate for rural areas than urban areas is found in Gujarat.

4.43. A table showing overall average rates of tariff in certain States in respect of certain key areas, namely domestic light and fans (50 Kwh/month) commercial lights and fans (50 Kwh/month), agricultural 10 HP 15% LF (817 Kwh/month), small industry 10 KW 20% LF (1460 Kwh/month) and large industry 1000 KW 50% LF(365000 Kwh/month) is given in Appendix 8.

LEVY ON INDUSTRIAL ALCOHOL

4.44 The term "industrial alcohol" is usually referred to mean 95% ethyl alcohol which is made unfit for beverage use by the addition of certain chemicals called denaturants as well as rendered incapable of effecting any recovery of alcohol from the mixture. Industrial alcohol goes in for various purposes in industries like synthetic rubber, plastics, organic chemicals, insecticides, paints, varnishes, etc.

4.45 We gather that the question as to who has got the legislative power for levying excise duty on industrial alcohol is still a subject matter of controversy. The latter is believed to centre round the exact import of the term "intended for human consumption". This may call for an amendment of the law, stipulating the correct jurisdiction, so that the overlapping is avoided. A fact to be noted is some States get revenue from this source through licence or vending fees.

INDIRECT TAXATION BY LOCAL BODIES - OCTROI

4.46 We now come to the field of local taxes. Local Government is a State subject under Entry 5 of the Seventh Schedule of the Constitution and the responsibility for providing adequate finances for local bodies is that of State Governments. While distribution of sources of revenue between the Centre and the States is provided for in the Constitution, there is no Constitutional reservation of sources of revenue for local bodies.

4.47 The question of resources for local bodies was examined in detail by the TEC who observed that it was both desirable and necessary that certain taxes should be reserved for being utilised exclusively by or for local bodies. The Commission was, however, not in favour of a Constitutional amendment with a view to providing Constitutional reservation of sources of revenue for local bodies, and, therefore, recommended that the following taxes should be reserved for exclusive utilisation by or for local bodies :—

(i) Tax on lands and buildings, popularly known as property tax ;

(ii) Taxes on the Entry of goods into the areas of local authority for consumption, use or sale therein popularly known as Octroi ;

(iii) Taxes on professions, trades and callings ;

(iv) Taxes on vehicles other than mechanically propelled ;

(v) Taxes on animals and boats ;

(vi) Taxes on advertisements other than newspaper advertisements.

4.48 In addition, the Commission recommended that the following taxes should also be permitted to be levied by local bodies :—

(i) Theatre tax or Show tax ;

(ii) Duty on transfer of property ;

(iii) Taxes on goods and passengers carried by road or waterway; and

(iv) Tolls.

4.49 While different State Governments have made different provisions in this respect, the three most important taxes assigned to local authorities are the octroi (and similar taxes), the urban property tax and the tax on professions, trades and callings. The latter two taxes are in the nature of a direct tax.

4.50 The term "Octroi", one of the important sources of revenue for local bodies, has not been used in the Constitution. However, the taxes covered by Entries 52 and 59 in the State List and Entry 89 of the Union List of the Seventh Schedule take on the characteristics of octroi as understood traditionally. In particular, Entry 52 which provides for the levy of taxes on the entry of goods into a local area for consumption, forms the principal legal basis for the levy of octroi. At present, octroi is levied only in certain States ; the estimated revenue being as in Table 5 below :—

TABLE —5 REVENUES FROM OCTROI - FOR SOME STATES

S.No.	State	Estimated revenues (1976-77) (Rs. crores)
1.	Gujarat ...	23.12
2.	Haryana ...	4.09
3.	Jammu & Kashmir ...	0.94
4.	Himachal Pradesh ...	0.87
5.	Maharashtra ... (separate figures at S.No. 13 for Bombay only)	34.66
6.	Manipur ...	
7.	Karnataka ...	12.13
8.	Orissa ...	1.81
9.	Punjab ...	5.63
10.	Rajasthan ...	7.13
11.	Uttar Pradesh ...	19.80
12.	West Bengal (Calcutta) ...	22.05
13.	Bombay ...	36.80

S.No.	State		Estimated revenues (1976-77) (Rs. crores)
14.	Delhi*	...	10.63
			179.66

*A Terminal tax is being levied by Delhi Administration and a "Mahimai" tax by Pondicherry Administration, both of which are akin to octroi.)

SOURCE: Planning Commission.

4.51 The reliance of different States on the revenues derived from octroi varies. Many States do without octroi. In West Bengal, it is only the Metropolitan Calcutta which has octroi duties accounting for over Rs. 20 crores a year, Similarly, other metropolitan cities like Bombay and Delhi derive revenues estimated around Rs. 35 crores and Rs. 11 crores a year respectively. Some of the other States where octroi revenues are sizeable are Gujarat, Karnataka, Uttar Pradesh and also Maharashtra.

4.52 In general, under the powers given to local bodies; octroi is leviable on goods and animals imported into a local area, irrespective of the mode of transport and even if the goods are brought into the local areas by individuals carrying these goods themselves. While assessment procedures in the various States are more or less uniform, the rates are either specific (based on weight) or ad valorem. By and large, specific rates usually related to weight predominate, resulting in low ad valorem rates on costly items and higher ad valorem rates on low priced goods. In Uttar Pradesh, for instance, the average rate of octroi on watches, as of 1974, was Rs. 100 per quintal. One quintal of watches would cost anything between Rs. 1 to Rs. 2 lakhs. Hence, the ad valorem rate in this particular case worked out to be 1 paisa per Rs. 100. On the other hand, in the case of a commodity, such as, tea, the rate of octroi was Rs. 6 per quintal which meant an ad valorem rate of 46 paise per Rs. 100. However, because of the ease of collection by the octroi staff, as ad valorem duties would mean assessment of duty after establishing the correct price for each products, specific rates of duty have been in common use even though they are regressive in their impact.

4.53 The octroi rate structures prescribed by local bodies vary and there is lack of uniformity even with regard to local bodies in the same State. In fact, the Uttar Pradesh Taxation Enquiry Committee (Lakdawala Committee) found very wide variations in the rates of octroi levied by different municipal Corporations and municipal boards in Uttar Pradesh, in spite of the fact that the rate schedules were subject to approval by the State Government.

4.54 In some States, the State Government has, through notifications, granted exemptions from octroi, or extended concessional treatment to certain commodities, particularly raw materials meant for use by local industries and agricultural products, such as, wheat, grams; maize and barley. Apparently, the cases for exemption from octroi are examined on merit, keeping in view the local conditions, promotion of industries and the financial position of the local bodies.

4.55 There are two variants of octroi as obtaining in different local bodies, namely, 'octroi without refunds' and 'octroi with refunds'. In the system without refunds which prevails in Punjab and Rajasthan, no appeal for drawback is entertained unless there is an error of calculation. However, in both the States as well as in Uttar Pradesh, no octroi is charged on those goods that simply pass through the jurisdiction of the local bodies under the system known as "Transit Pass System." Under the system of octroi with refunds, which applies to States other than Punjab and Rajasthan, if any portion of the goods brought within the local area is exported, the owners become entitled to a refund of the proportional amount of tax paid.

4.56 We conclude our review of indirect taxation at State and municipal levels by drawing attention to the emergence of sales taxes as the dominant source of revenue to States and the second largest source of tax revenues in the economy. In the matter of rates as well as in other relevant respects, the pattern of taxation by different States shows considerable variations. These become matters of concern on account of the impact of taxation by one State on the residents of other States as well as on the national economy as a whole. The last major effort to achieve a measure of coordination through Central regulation of sales taxation was the enactment of the Central Sales Tax Act twenty years ago. The question whether and what further steps in this direction are necessary will be discussed later in this report. The other levies are quantitatively less important though some of them, like electricity duty and the octroi, will also be discussed further.

CHAPTER 5

INTERACTION OF CENTRAL AND STATE TAXES

INTRODUCTION

5.1 We have had occasion to refer to the fact that indirect taxes in India fall both on final products and on inputs used in their manufacture. Often the term 'inputs' is thought of as raw materials and components which are physically embodied in the final product. We use the expression in a broader sense to cover the entire range of products, which get used for and during the process of, the manufacture of a product, whether they become physical ingredients of a final product (e.g., raw materials and components) or are used in marketing it (e.g., packaging materials and containers) or get consumed in the process of manufacture (e.g., fuel). Since excises and sales taxes fall both on the final products as well as on various inputs which are used in their manufacture, and as there are but limited provisions for relief from input taxation, there is a considerable divergence between the nominal rate of tax, which the consumer is aware of when he buys a product, and what we would call "cumulative levy", which would represent the sum total of the burden of all the indirect taxes levied by different authorities at various stages before the final product reaches the consumer. The cumulative impact of excises alone, which are levied only at manufacturing stage, is itself significant as various inputs get taxed at successive stages of production. Such a structure of excises, taken together with the sales tax system built up by the State Governments, has created an extremely complex structure of internal indirect taxation in the country. The overlapping coexistence of two generalised systems of levy, the excise based on the principle of production or origin and the sales tax based, subject to some limitations, on principles of both production and consumption, i.e., both origin and destination, each compounding the effects of the other through interaction, has given rise to uncontrolled and unintended incidence of taxation on different commodities. Because both sales taxation and excise duties are widely applicable to inputs, subject to the reliefs and limited exemptions indicated earlier, the impact of their interaction becomes much more serious than is generally realised. Octroi duties which are also levied on inputs aggravate the problem.

5.2 In addition to excise duties account must also be taken of import duties. Imported raw materials usually bear a duty of 45 per cent and in addition countervailing duty at varying rates. Various semi-processed intermediates which are also imported in large quantity get taxed at the much higher rate of 75 per cent, apart from the countervailing duty, which is levied on tax inclusive price. Unless the goods go directly to the manufacturers who use them as inputs, there may be sales taxes to be paid on the price inclusive of the import duty when the importer sells them to the manufacturer. If, after further processing, the raw materials/semi-processed intermediates are sold as a component to another manufacturer, both excise duties and sales tax become applicable to them and so the process goes on till it finally reaches the consumer.

DEMERITS OF MULTIPLE TAXATION

5.3 Multiple taxation adversely affects the costs and prices throughout the economy. When taxes fall both on inputs and on the final product, such of these taxes as are levied on an ad valorem basis fall not only on the value of the products but at each stage they fall on the taxes that may have been earlier levied on them. Along side, there is an escalation of costs and profits at each stage. When an input is subjected to excise and/or sales tax, the manufacturer who uses it needs a larger amount of working capital to maintain the necessary stock of the inputs; hence a

greater financial burden is imposed on him. In the process, the cost of his final product gets raised. Besides, he works out his own profit margin as a percentage of his costs which include input taxes, and arrives at a price by adding a higher quantum of profit. On this price, the excise on the finished product is worked out. Then comes the sales tax which is levied on the price inclusive of excise duty. Thereafter, the product goes to the wholesaler and then the retailer, each of whom once again, has to find a larger amount of finance which raises his costs and profits expectations. At each stage, the mark-up by producers and traders gets inflated because the profits which they seek to earn are related to the total capital which they employ, i.e., they would like to earn a certain rate of return on capital employed, and the amount of capital employed, as explained above, inevitably increases if the costs of inputs are raised on account of the indirect taxes levied on them. This snow balling or pyramiding effect which is also referred to as 'cascading' raises the price of the final product to consumers, by more than the sum total of the different taxes levied at intermediate stages. In other words, the increase in consumer prices due to cascading is not limited to what accrues to the Exchequer by way of revenue. The same amount of revenue may be raised with a smaller rise in the price of final product and, therefore, a lower burden on the consumer, if a non-cumulative type of tax was imposed at the final stage of production, that is, on the finished product.

5.4 The extent of cascading naturally differs from product to product but is serious enough in a very large number of cases to bring about a marked divergence between the nominal rates of excise and of sales tax on final products and the cumulative burden of import duty, excise and sales tax which they, in fact, bear on account of levies on inputs. As a result, the nominal rates give a misleading picture of the distribution of the tax burden among products and sections of the community.

5.5 There have been attempts in the past to measure the impact of taxation of inputs on different products. The National Council of Applied Economic Research (NCAER) had conducted two selective studies, one with a data base relating to 1972 and another with that relating to 1975-76. In the former study, impact of input taxation was measured in relation to the actual ex-factory price as well as cost of the final product as it would have been if no levy had been made at any but the final stage. The latter study was confined to excise duties and the impact was measured in relation to the ex-factory price. Both the studies, however, took into account the taxes on inputs as well as on inputs of inputs. The studies which we have undertaken, and the details of which are set out in the Table appended to this Chapter include only the taxes on first-stage inputs and measure incidence as a percentage of ex-factory price of the final product. The actual impact on account of all taxes on inputs and inputs of inputs would be more than what has been shown in our study. Further, if the impact is measured with reference to the tax-exclusive price of the product, the cumulative levy would be higher than the figures shown in our study.

5.6 As would be seen from the Table appended to this Chapter, the levies on even the first-stage inputs bring about a considerable divergence between the cumulative levies and the nominal rates of duty on the finished products, not only in respect of consumer products but also of machinery and inputs which are finished products themselves. Thus, on insulin, an important anti-diabetic drug, and chloroquin phosphate, an important anti-malarial drug, while the nominal rates of excise and sales tax consciously imposed by the Central and State Governments are low (at 2 per cent and 4 per cent), the cumulative levy adds upto 27 per cent and nearly 44 per cent of their ex-factory prices. Likewise, a commonly used analgesic tablet bears a cumulative levy of 31.6 per

cent as against the nominal rates of 12.5 per cent and 3 per cent. In respect of another widely used item, namely, washing soap, while the nominal rates of excise and sales tax are 5 per cent in each case, the cumulative levy is 16 per cent. Similar is the case of a low-priced toilet soap where the divergence resulting from input taxation is around 5.3 per cent. Another item of consumer interest where taxation of inputs has a significant cascading effect is the ceiling fan where input taxation alone amounts to 11.5 per cent of the ex-factory price. Similarly, in the case of a 60 watts bulb, whereas the nominal rates are 15 per cent and 4 per cent, the cumulative levy is as high as 38.7 per cent. Yet another item of consumer interest which bears an effective indirect tax burden far in excess of the nominal rates prescribed for it is the dry cell battery; the input duties in this instance amount to 22 per cent of the ex-factory price.

5.7 In the textile family too, we notice a significant divergence between the nominal rates and the cumulative levy. Thus, we find that on a dyed nylon saree, the duties on inputs alone account for about 23 per cent of the ex-factory price. In the case of a popular blend (67/33) of polyester/cotton shirting the taxes on fibre and yarn alone constitute 34.7 per cent as against the fabric duty of 5.5 per cent. Similarly, hand knitting woollen yarn, which is fully exempt from excise levy bears a cumulative levy of 40 per cent.

5.8 Another class of goods where the impact of input taxation is substantial is capital goods and machinery. We find that a 30HP electric motor, while having nominal rates of 15 per cent and 10 per cent bears a cumulative levy of 34.3 per cent. Again, a power driven pump (of the mono-block type) carries a cumulative levy of 21.3 per cent, the element of input taxation alone being 5.8 per cent as against the nominal rate of excise of 5 per cent on it. Similarly, in the case of commercial vehicles, which are capital goods for the road transport industry, the duties and taxes on inputs amount to 13.2 per cent of the ex-factory price. This is slightly more than even the individual nominal rates of excise and sales tax. Another item belonging to this category, is the water cooler which is widely used in industrial and commercial establishments. Here we find that the taxes on inputs are of the order of 26 per cent as against nominal rates of 20 per cent and 15 per cent under excise and sales taxes.

5.9 Turning to inputs, on an item like printed aluminium foils for packing contraceptives, while the nominal rate of excise is a little over 30 per cent, one finds that the cumulative levy is as high as 63 per cent. In respect of an item like storage battery, which goes as original equipment as well as a replacement, the element of tax on inputs is 14.9 per cent in a total cumulative levy of 51.7 per cent. Truck tyres (nylon) are subject to a cumulative levy of 92 per cent as against the nominal rates of 55 per cent and 10 per cent of excise and sales taxes. Wires and cables which are used widely as inputs as well as for replacement purposes are also among the items which are affected by excessive input taxation. Thus, in the case of PVC armoured aluminium conductor, as against the nominal rates of 5 per cent and 4 per cent, the cumulative levy is 39 per cent. Similarly, enamelled copper winding wires, while being subjected to nominal rates of 10 per cent and 4 per cent bear an effective cumulative levy of 56 per cent.

5.10 One of the facts brought out by our study is that where imported material forms a major component of the inputs, then the effect of import duties tends to be significant. The cascading on account of excise taxation of inputs which are purely indigenous is moderate except in the case of inputs like non-ferrous metals (e.g., aluminium and copper) and textile fibres and yarn (e.g., polyester and nylon). The combined impact of excise and sales tax on inputs even in the case of

indigenous inputs also plays a significant role in bringing about the divergence between nominal rates and cumulative levy.

5.11 The NCAER studies referred to earlier also reveal the extent of input taxation and the effective tax burden borne by various commodities. The first study indicates that tyres, trucks, tractors and yarn (both cotton and rayon), bear a cumulative levy far higher than the nominal rates of excise and sales tax applicable to them. The second study, which measured the impact of excise duties alone shows that cascading of excise on inputs and inputs of inputs is particularly significant (i.e., more than 5 per cent of the ex-factory price of the final product) in the case of aluminium, refrigerators, air-conditioners, tyres and commercial vehicles.

5.12 Further due to widespread taxation of both inputs and final products and that too by different authorities, it is not possible to control tax incidence on final products. It is only after a great deal of research and sometimes not even then, that the total increase in the cost and price of the final product due to levies on various inputs (raw materials, intermediates, etc.) can be determined. The total effective incidence on any given product especially a product at the end of the chain of production, becomes almost fortuitous and largely unknown. This is one of the major consequences of the interaction of the different taxes to which we draw attention at the beginning of this Chapter. It thus happens that the total tax burden on the consumers does not have a determinate degree of progression to which both the Centre and the States individually attach importance in fixing nominal rates on final products. In fact, a heavy tax on an input, for which no relief is given at later stages, generally tends to be intrinsically regressive. It places a greater burden on the varieties of products consumed by the poor than on those consumed by the rich. The way this happens is, that for the range of products in the manufacture of which a particular input is used, the cost of the input would be a higher proportion of the value of the cheaper products than of the more expensive ones in respect of which the value added in the manufacturing stage would be much greater. As a result, the tax levied on the input will constitute a higher proportion of the price of the cheaper product than of the more costly one. Thus, in the case of a textile fabric, while the cost of the fibre or the yarn could be 50 per cent or more of the price of a cheaper variety, in the case of fabrics of fancy designs and colours, specially processed to prevent shrinkage and resist creases, the cost of the fibre or the yarn may well be only 25 per cent of the price of the fabric. This would mean that the percentage incidence of the levy made at the fibre or yarn stage might be twice as much on the cheaper qualities of textiles than on the more expensive ones. Similarly, a tax on aluminium may mean a greater percentage incidence in the case of simple aluminium utensils than in respect of garden furniture made of aluminium.

5.13 Another distortion which taxation of inputs creates is that it generally tends to encourage what is known as vertical integration, that is, bringing under one firm several stages of production. In a vertically integrated firm, the manufacturer himself tries to produce more and more of the inputs needed by him, rather than purchase them from ancilliary industries. By doing so, he clearly saves on sales tax because when he produces rather than buys the necessary inputs for his final product he has no liability to sales tax, since no sales take place in such cases. Thus in the engineering industry, manufacturers of products like bicycles, refrigerators or automobiles would be at an advantage if they manufacture all the components themselves instead of buying out a number of them. Government's policy of developing small scale industries as ancilliaries to larger units, supplying them with components, thus gets hindered. Excise duties too can have a similar effect, but here steps have been taken to mitigate this generally either by levying excise duties on inputs manufactured within the factory, even if used for captive consumption or by giving

relief from excise in respect of bought out components. This device has been used in a large number of cases but the practice is not universal.

5.14 Yet another way in which the taxation of inputs by different authorities can create distortions is by their impact on the allocation of resources. The differential incidence of indirect taxation on different intermediates and inputs has the effect of influencing the producers' choice between factors of production in unintended ways. If the levies are carefully determined to encourage or discourage the use of particular raw materials or intermediates, indirect taxation can be used as a positive instrument of planning. However, when the incidence is purely fortuitous, changes in relative prices of factors of production can give wrong signals to the producers and may in fact encourage them to make greater use of resources which are more scarce. Further, it leads to the misdirection of investments contrary to national priorities.

5.15 It has been an accepted principle in India, as in other countries, to free exports of all internal commodity taxes so that our industries are not handicapped in competing in international markets. Towards this end, a system of drawbacks is operated. But the effectiveness of the drawback system depends on an accurate computation of all taxes paid from the raw material to the manufacturing stage. With the kind of interaction of taxes levied by different authorities at different points, that has been referred to above, it becomes virtually impossible to calculate exactly the total quantum of indirect levies on a product which is to be exported. Although an elaborate system for the grant of drawback of duties has been evolved, the amount of drawback granted seldom equals the actual customs and excise duties paid at successive stages of the manufacture of a given product. Further, sales taxes and octroi duties paid are not taken into account in the drawback calculations. Even if a duty drawback is given for all the levies, the competitiveness of the Indian product would still be adversely affected because, owing to cascading effects, the rise in cost and prices will be higher than the amount of levy and further because, if factor prices have got disturbed, production is not that economical as it would otherwise have been. There arises, therefore, a recurring need for giving various forms of cash assistance and other incentives to Indian exporters which may attract the imposition of anti-dumping duties and other restrictions by importing countries.

ADVERSE EFFECTS ON RAW MATERIALS

5.16 We have referred above to the difficulty in making exports completely free of indirect taxes. In relation to inter-State trade also, there is a tendency for taxes levied in one State being ultimately paid by consumers in other States. Even though there is concessional treatment to inputs in a number of the States' sales tax systems they are often not extended to sales outside the State. This leads to an unplanned distribution of the burden of sales taxation among the citizens of different States with each State trying to export its taxation through the imposition of taxes on inputs and inter-State sales tax. The more developed States which have attained higher levels of agricultural or industrial production or have raw materials needed for industry, get greater benefit and are in effect in a position to export their taxation to other States.

5.17 Some other undesired or undesirable effects of the present system of indirect taxes may also be noted. In order to avoid payment of sales tax at more than one point, manufacturers, instead of operating through whole-salers, prefer to set up their own retail depots. Likewise, to avoid the CST on the inter-State sales manufacturers set up their depots in other States sending the goods on consignment to their own agents thus cutting out the wholesalers. Another type of distortion to which the present system of octroi leads, is in the matter of location of industries.

Because octroi duties can be avoided if all the components and inputs can be manufactured within the limits of the municipality or the local authority concerned, there is a tendency of concentration of industries in larger cities instead of being dispersed over a wider area.

5.18 The possibility of the cumulative impact of excise taxation levied at different stages leading to an unduly heavy burden on a particular product has been recognised by Government and a number of provisions, detailed in Chapter 2, have been introduced to mitigate the rigours of input taxation. The scope of these procedures, as pointed out, is limited in various ways and does not extend to customs duties at all. The sales tax laws of most States also grant limited exemptions and/or concessional treatment for the sale of intermediate products to manufacturers, that go to reduce the cumulative effect of sales taxation in such cases. However, concessions rather than exemptions are the general rule and the concessions are applied in a way that they benefit mostly the producers within the State.

PROVISIONS TO RELIEVE CUMULATIVE IMPACT

5.19 Our review of the interaction of indirect taxes imposed by the Centre and the States brings out that -

(a) as a result of different taxes levied by different authorities both on finished products and on their inputs,

(i) the total burden on the consumer is much higher than the rates of tax imposed on the final product on considerations of desired progression;

(ii) the total increase in the prices of finished products is in excess of the sum total of revenues accruing to the Centre and the States;

(iii) there are distortions in the relative prices of raw materials and other factors of production; and

(iv) there are other economic side effects of an undesirable nature such as discouragement of small scale and ancilliary industries;

(b) both the Central and the State Governments have evolved procedures to mitigate the undesirable effects referred to above but the scope of these procedures is limited in many ways and their application has on the whole been restrictive.

TABLE - DIVERGENCE BETWEEN NOMINAL RATES AND CUMULATIVE LEVIES

Product description	Input duties/taxes as percentage of ex-factory price				Nominal excise duty/ sales tax on finished product		Total cumulative duty as percentage of ex-factory price
	Customs	Excise or countervailing	Sales tax	Total	Excise %	Sales tax %	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Insulin anti-diabetic drug	21.1	-	-	21.1	2.0	4.0	27.2
Chloroquin phosphate anti-malarial drug	37.2	0.5	neg.	37.7	2.0	4.0	43.8
Analgesic Tablets (Strips)	13.6	1.2	0.9	15.7	12.5	3.0	31.6
Washing soap	-	2.7	3.0	5.7	5.0	5.0	16.0
Low-priced toilet soap	0.4	0.9	4.0	5.3	10.0	5.0	20.8
Medium-priced toilet soap	0.6	0.2	3.7	4.5	15.0	5.0	25.3
Ceiling fan 1200 mm. sweep	3.2	4.1	4.2	11.5	15.0	14.0	42.6
Electric bulb 60W	8.5	9.2	1.4	19.1	15.0	4.0	38.7
Flourescent tube-light	2.7	5.9	1.4	10.0	40.0	4.0	55.6
Dry cell battery	13.8	6.3	1.9	22.0	20.0	9.0	52.8
Storage battery	11.9	2.0	1.0	14.9	17.5	16.5	51.7
100%-Nylon dyed saree	-	21.5	1.7	23.2	5.5	-	28.7
100%-Nylon dyed chinon	-	17.5	1.5	19.0	5.5	-	24.5

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
100%-Nylon American Georgette Printed	-	22.1	1.7	23.8	5.5	-	29.3
67:33-Polyester cotton shirting	-	34.0	0.7	34.7	5.5	-	40.2
100%-polyester dyed shirting	-	21.8	1.5	23.3	5.5	-	28.8
74:26-Polyviscose suiting	-	19.6	1.6	21.2	5.5	-	26.7
67:33-Polycotton dyed suiting	-	20.2	0.1	20.3	5.5	-	25.8
All-wool worsted suiting	23.9	-	-	23.9	11.0	-	34.9
80:20 wool-polyester suiting	16.3	9.6	-	25.9	11.0	-	36.9
45:55 wool-polyester suiting	7.5	10.4	-	17.9	11.0	-	28.9
Hand-knitting woollen yarn	28.1	3.9	-	32.0	Nil	8.0	40.0
Asbestos roofing sheets	14.4	10.3	0.8	25.5	15.0	6.6	48.2
Asbestos pipes	14.0	8.8	0.5	23.3	15.0	4.4	43.4
White printing paper	-	1.4	2.0	3.4	5.5	4.0	13.1
Straw board	0.5	3.0	12.9	16.4	30.0	4.0	51.6
Electric motor 30-HP 6 Pole TEFC SCR Motor	0.9	3.1	3.8	7.8	15.0	10.0	34.3

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Monobloc pumpset Type MBN 3	-	2.4	3.4	5.8	5.0	10.0	21.3
Commercial vehicle - (trucks and bus chassis)	3.1	8.0	2.1	13.2	12.5	12.0	39.2
Water cooler	17.5	5.2	3.5	26.2	20.0	15.0	64.2
Refrigerator 165 litres	5.5	9.1	2.9	17.5	40.0	10.0	71.5
Refrigerator 286 Litres	5.5	9.8	2.9	18.2	75.0	15.0	119.5
Air-conditioner	13.5	3.1	4.8	21.4	100.0	15.0	151.4
PVC-armoured cable - aluminium conductor $3\frac{1}{2}$ x 120 mm.	-	21.7	8.0	29.7	5.0	4.0	38.9
Enamelled copper winding wires - 18 SWG	22.5	15.8	3.3	41.6	10.0	4.0	56.0
Super-enamelled copper winding wire 22 SWG	20.5	22.5	4.5	47.5	10.0	8.0	66.3
Printed aluminium foils for contraceptives	4.4	18.1	2.7	25.2	32.5	4.0	63.0
Printed aluminium foils for pharmaceuticals	2.0	23.2	2.4	27.6	34.0	4.0	67.0
Baby-food container (1 Kg. capacity)	21.0	12.6	1.5	35.1	15.0	4.0	54.7
Container (2 Kg capacity)	6.6	12.1	3.2	21.9	15.0	4.0	41.5

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Truck-tyre (nylon)	16.1	1.3	4.1	21.5	55.0	10.0	92.0
Truck-tyre (rayon)	0.5	4.3	9.8	14.6	55.0	10.0	85.1
PVC resins	2.5	3.3	2.2	8.0	40.0	4.0	53.6
Synthetic adhesive	10.6	1.2	2.6	14.4	40.0	4.0	60.0
Ready mixed paint	-	4.6	2.2	6.8	15.0	5.0	27.6
Zinc oxide	-	15.8	2.5	18.3	5.0	12.0	35.9
Aluminium paste	-	22.1	3.0	25.1	10.0	4.0	39.5
Synthetic enamel	7.8	2.5	2.6	12.9	15.0	4.0	32.5
Cement based water paint	-	7.5	3.0	10.5	10.0	7.0	28.2
Vat dye (Blue RSN Powder)	2.5	4.6	2.3	9.4	30.0	5.0	45.9
Tin plate	13.2	9.5	1.6	24.3	17.5	4.0	46.5
Electrical stampings manufactured out of grain oriented steel sheets	21.1	4.3	0.2	25.6	10.0	4.0	40.0

NOTE: 1. The above figures in columns 2 to 5 which are for certain representative product of selected manufacturers, give only the effect of taxes on first stage inputs. If the impact of taxes paid on inputs of inputs is also taken into account, the cumula tive levy will be significantly higher in several cases. Thus, in the case of commercial vehicle, it is estimated that the impact of taxes on inputs of inputs is itself about 6.88% of the ex-factory price. Further, sales tax rates vary from State to State and the rates applied here are those known to be applicable in the State in which the factory manufacturing the product is located. In the case of pure/blended fabrics of nylon/polyester/viscose/cotton it has been presumed that they are manufactured out of indigenous fibre and yarn.

2. The above Table has been prepared on the basis of information obtained from selected manufacturers as well as from excise field formations.

CHAPTER 6

THE INCIDENCE OF INDIRECT TAXES IN INDIA (1973-74)

INTRODUCTION

6.1 The question of the incidence or the distribution of the burden of taxation has been a matter of deep interest to the public at large, because taxes are seen and felt to affect the lives of households and the fortunes of business. It is also a matter in which Governments take a keen interest because they need to try to take the incidence into account while evolving the pattern of taxation. Unfortunately, it is not too easy even to define the concept of incidence, while its measurement presents problems of its own, the paucity of data being not the least important among them.

6.2 The incidence of a tax has been traditionally defined to mean the final resting place of the money burden of the tax. Since those who are liable to pay a given tax may be in a position to shift it to others with whom they have business dealings, the question of determining the final resting place of different taxes arises. The popular notion is that certain taxes, such as those on income, rest permanently on those who pay them to the Government, while others, such as those on commodities, are completely shifted forward to consumers. This has now been recognised to be too simple a view. Some part of the so-called direct taxes could be shifted under certain circumstances, while a tax on a particular commodity may stick for a long time to the producer himself. Moreover, apart from taking away a part of the incomes of different individuals, taxes have other effects on the economy which, in turn, may affect the relative economic positions of those persons. From this point of view, the study of incidence should really cover a broader area than the mere measurement of the direct money burden of taxes. However, there are several difficulties in doing this. In the technical note appended to this Chapter we discuss the various conceptual issues as well as the difficulties involved in empirically measuring the incidence of indirect taxes in India. The sources and nature of data as well as their limitations are also indicated there.

6.3 We entrusted the study of the Incidence of Indirect Taxes in India in the year 1973-74 to the National Institute of Public Finance and Policy, New Delhi. In accordance with our terms of reference, we asked the Institute to determine the distribution of the burden of Indirect taxes levied by the Centre and the States, among the different expenditure groups in rural and urban areas. Following the line of approach of the earlier studies, the Institute has attempted to allocate the burden of taxation on the assumption that all indirect taxes are ultimately shifted forward to the consumers (including Government).

EARLIER STUDIES

6.4 A number of attempts have been made over the last two decades or so to estimate the incidence of taxes in India. Of these, several relate to taxes in particular States or to particular taxes in the country. Examples of the former are the studies by the National Council of Applied Economic Research (NCAER) on the incidence of taxation in the States of Gujarat and Mysore.* Agricultural taxation has claimed particular attention and several scholars have attempted to estimate the burden of taxes on agriculture or on agriculturists.

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*NCAER. Incidence of Taxation in Gujarat, New Delhi, 1970
and Incidence of Taxation in Mysore State, New Delhi, 1972.

Special mention may be made of Hanumantha Rao's study of agricultural taxation in Andhra Pradesh*. Pathak and Patel's study of the same in Gujarat** and Ved Gandhi's study on the burden on Indian Agriculture***.

6.5 The first systematic study of the overall incidence of indirect taxes in India was carried out by the taxation Enquiry Commission, 1953-54 (TEC). This study was based on consumer expenditure data collected by the National Samples Survey (NSS) in the fourth round for the period April/September, 1952 and worked out the burden of indirect taxes in terms of percentages of expenditure in different monthly expenditure classes. More or less the same exercise was repeated for the years 1958-59 and 1963-64 by the Economic Division in the Ministry of Finance, Government of India (MF).@ The present study looks at the incidence of indirect taxes exactly a decade after the last comprehensive study.

6.6 The late Dr. Banamali Dey attempted a study of the shifting and incidence of indirect taxation for the year 1964-65 @@. His study was also based on the NSS consumption expenditure data, but it experimented with a more sophisticated methodology than the earlier studies. Dr. Dey's approach will be explained in the technical note on the definition and measurement of incidence of taxation, annexed to this Chapter.

6.7 We have defined incidence of taxation to mean the distribution of the reduction in real income available for private use. Since incomes are the most important indicators of the relative economic positions (in terms of welfare) of different individuals, we are really interested in knowing how taxes affects the incomes of different individuals, households or social groups. That is why progression and regression are measured with reference to income. If the percentage of taxes increases with income, they are said to be progressive; and conversely, if the percentage falls as income rises, the taxes are said to be regressive. Unfortunately, however, we do not have for India adequate data on income distribution nor expenditure data by income groups. NSS provides details of expenditure only by expenditure groups. Hence, most of the earlier studies of the incidence of commodity taxation have had to be content with working out the burden in terms of percentages of expenditure of households in different total or per capita expenditure classes. Notable exceptions to this general practice are a study of the incidence of taxation undertaken by the Orissa Taxation Enquiry Committee, 1961 $, and an attempt by Lydll and Ahmed (1961) to allocate all taxes among income groups in urban and rural areas £.

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*Rao, C. H. Hanumantha. Taxation of Agricultural Land in Andhra Pradesh, Asia Publishing House, Bombay, 1964

**Pathak Mahesh T. and Patel Arun S. Agricultural Taxation in Gujarat, the Council of Economic Education, Bombay, 1970

***Gandhi, Ved P. The Tax Burden on Indian Agriculture Harvard Law School, Mass, 1966.

@Ministry of Finance, Incidence of Indirect Taxation, 1958-59 and Incidence of Indirect Taxation, 1963-64, New Delhi, 1961 and 1969.

@@Dey, Banamali, "Impact of Indirect Taxes on the Distribution of Consumer Expenditure." Economic and Political Weekly, September 7, 1974.

$Government of Orissa, Orissa Taxation Enquiry Committee Report, Bhubaneshwar, 1961.

£Lydll H. F. and Ahmed M."An exercise in Forecasting Consumer Demand and Taxation Yields in India in 1965-66", Indian Economy Review, August, 1961.

6.8 In the former study, on the basis of certain assumed propensities to save, the expenditure groups were converted into income groups. In the Lydll and Ahmed Study, income tax statistics, unsatisfactory as they were, were combined with NSS data to derive estimates of income distribution for 1955-56. The same distribution was assumed to exist in 1965-66. While such attempts are valuable as experiments in methodology, it is doubtful if the results obtained could really be taken as being reliable for policy formulation. Income tax revenue statistics themselves are subject to several limitations and in their present form cannot be combined with expenditure data for given years. It would seem that much remains to be done before we obtain a satisfactory picture of income distribution for our purpose. In the present exercise, therefore, we are following the example of TEC and the MF in working out the incidence only in terms of percentages of expenditure.

DISTRIBUTION OF TAX BURDEN

6.9 Indirect taxes levied by the Centre and the States rose from 8.9 per cent of national income in 1963-64 - the year of the last MF study of incidence --to 11.2 per cent in 1973-74. Of this 11.2 per cent, 1.65 percentage points could be said to have fallen on the Government sector and on the investors, and the rest to have been shifted to the private consumers. The portion falling on the consumers is estimated to have amounted to 10.54 per cent of household consumption expendiutre. This is an average of the burdens on the rural and the urban households, which differed considerably in percentage terms. While the burden on the rural Households amounted only to 8.0 per cent of their consumption, that on the urban households amounted to 18.0 per cent. The rural sector accounted for 77 per cent. of private consumption, and bore 57 per cent of the indirect taxes allocable to consumers. The share of the rural sector in total population is estimated to have been 80.1 per cent in that year. In the MF study of 1968-69, it has been estimated that, as of 1963-64, the rural sector, accounting 81.5 per cent of the total population then, had paid 60 per cent of the indirect taxes. Thus, the tax share of rural sector is seen to have fallen while its share in population also declined slightly.

6.10 The per capita indirect tax payment per annum for the urban households amounted to Rs. 174.50 in 1973-74, and was about three times the per capita payment of Rs. 57.30 estimated for the rural household. The proportion was nearly the same (2.9) in 1963-64.

AGGREGATE BURDEN

6.11 Table 1 of Appendix 10 presents the details of the indirect taxes paid by the different per capita expenditure groups in rural and urban areas and also indicates the percentage of consumption expenditure paid in taxes in each case. The information on the inter-group distribution of the burden of indirect taxation is abstracted from that table and presented below in Table 1.

TABLE 1 - INDIRECT TAXES AS PER CENT OF TOTAL EXPENDITURE AND TOTAL CASH EXPENDITURE BY PER CAPITA EXPENDITURE GROUPS

(1973-74)

	Rural		Urban		All-India	
Monthly per capita expenditure group (in Rs.)	Tax as per cent of total expenditure	Tax as per cent of total cash expenditure	Tax as per cent of total expenditure	Tax as per cent of total cash expenditure	Tax as per cent of total expenditure	Tax as per cent of total cash expenditure
(1)	(2)	(3)	(4)	(5)	(6)	(7)
			(Percentages)			
0-15	2.91	4.55	3.63	4.44	2.96	4.56
15-28	3.33	5.25	6.31	6.79	3.63	5.46
28-43	4.45	7.27	7.36	7.93	4.89	7.41
43-55	6.18	10.32	9.66	10.31	6.85	10.31
55-75	6.71	11.40	11.86	12.70	7.92	11.82
75-100	10.02	16.43	14.80	15.85	11.40	16.21
100 & above	16.17	22.46	30.19	31.35	21.96	26.77
All households	8.03	12.87	17.96	19.03	10.54	14.96

The most important feature of the estimates presented is that they indicate a progressive distribution of the tax burden in terms of per cent of expenditure. Thus, taking rural and urban households together, we find that the indirect tax burden as a proportion of expenditure increases progressively from about 3 per cent for households with per capita monthly expenditure not exceeding Rs. 15 to nearly 22 per cent for those in the group with expenditure above Rs. 100. Even if the highest expenditure group is left out, the percentage burden is nearly four times on the next highest expenditure group (Rs. 75-100 per capita) as on the lowest expenditure group.

6.12 The progressive pattern of distribution of indirect tax burden is seen to prevail also among rural and urban households taken separately, except that the burden on the urban households is distinctly higher than on the rural households in the corresponding expenditure classes. This difference is partly due to the higher proportion of non-cash expenditures for the rural households and partly due to differences in the pattern of consumption between rural and urban households. The former was the more important factor. This can be seen from the fact that tax burden as a percentage of cash expenditure is only marginally different as between rural and urban households in the same per capita expenditure classes, except for the class having per capita expenditure of Rs. 100 and above. Table 2 of Appendix 10 gives the percentages of cash expenditure to total expenditure for the different per capita expenditure groups in rural and urban areas. In the rural sector, the proportion of cash expenditure remains more or less constant as one moves up the expenditure scale, except at the very top; whereas in the urban sector, the proportion of cash expenditure rises with the level of per capita total expenditure. This is one of the causes of the higher degree of progression in the urban sector.

6.13 It should be remembered that the progression that we have found is only with reference to expenditure. One would like to know if the distribution is progressive also in terms of percentages of incomes of households, i.e., whether the upper income groups pay a higher proportion of their income as indirect taxes. As already indicated, we are unable to provide an answer to this question as satisfactory data on income distribution are not available. It is likely that at the upper end of the income scale, consumption forms a lower proportion of income than it is at the lower end. So indirect taxes may tend towards reduced progression, or even regression, at the top. However, the finding that the top expenditure group in urban areas (which would also be the top income group in the country) pays as much as 30 per cent of its expenditure as indirect taxes, indicates that if the highly progressive direct taxes which the more well-to-do in that group pay (or should be paying) are also taken into account, the tax structure as a whole in India would be progressive with respect to income. Whether that structure is made effective depends of course on the degree of enforcement of the direct tax system. As far as the indirect taxes alone are concerned, it is noteworthy that, in spite of the widespread taxation of inputs, the tax structure turns out to be uniformly progressive over the entire range of expenditure considered.

6.14 While the structure of indirect taxes is progressive with reference to expenditure, it cannot be overlooked that indirect taxes fall even on the poorest sections of society. Thus, urban households with monthly per capita expenditure of Rs. 15 or less at 1973-74 prices (corresponding to Rs. 19.5 or less at current prices) pay 3.6 per cent of their meagre expenditure, which is likely to equal or exceed their income, in taxes, and those in the Rs. 15-28 per capita expenditure group (Rs. 19.5-36.4 at current prices) pay as much as 6.3 per cent of expenditure in indirect taxes. In absolute terms, this means that an urban family of five, spending Rs. 75 per month, pays about Rs. 2.70 per month as indirect taxes, whilst a similar family spending about Rs. 140 per month pays about Rs. 8.85 per month. As far as the first group is concerned, the main contributors to the burden are. Central excise on sugar, fertilisers (through the consumption of agricultural products), tyres and tubes (used by buses and trucks) and jute manufactures (used for moving foodgrains) and sales taxation of foodgrains and atta. As far as the latter group is concerned, the main contributors to the burden. are, Central excise on sugar, tobacco products, iron and steel, diesel oil

(through use of trucks and buses) and jute manufactures (for moving foodgrains);and sales taxes on foodgrains and atta, vegetable oils and fats, and jute manufactures.

6.15 CENTRAL AND STATE INDIRECT TAXES

The incidence of indirect taxation given above represents the combined burden of Central and State taxes. The incidence of the individual taxes included in the study, on the various per capita expenditure classes, is shown separately in Table 2 below:

TABLE 2 - CENTRAL AND STATE INDIRECT TAXES AS PER CENT OF CONSUMER EXPENDITURE BY PER CAPITA EXPENDITURE GROUPS

(1973-74)

	Monthly expenditure groups (in Rs.)- per capita							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All households
	(Percentages)							
Rural								
Central taxes	1.68	1.86	2.58	3.68	4.25	6.32	10.30	4.99
Central excise	1.42	1.50	2.01	2.92	3.27	4.85	7.87	3.85
Import duty	0.26	0.37	0.58	0.76	0.99	1.48	2.43	1.14
State taxes	1.23	1.47	1.86	2.50	2.46	3.70	5.87	3.04
Sales-tax (including sales tax on motor spirit)	0.67	0.85	1.02	1.23	1.31	1.77	2.60	1.49
State excise *	0.22	0.27	0.32	0.63	0.37	0.83	1.82	0.73
Others	0.34	0.35	0.53	0.64	0.78	1.00	1.44	0.83

*On alcoholic drinks

Contd...

	Monthly expenditure groups (in Rs.) - per capita							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
				(Percentages)				
All indirect taxes	2.91	3.33	4.45	6.18	6.71	10.02	16.17	8.03
Urban								
Central taxes	2.42	3.74	4.56	5.97	7.61	9.41	20.99	12.03
Central excise	2.42	3.11	3.75	4.94	6.25	7.77	16.78	9.73
Import duty	0.00	0.63	0.81	1.03	1.36	1.63	4.21	2.30
State taxes	1.21	2.57	2.80	3.69	4.25	5.40	9.20	5.93
Sales-tax (including sales tax on motor spirit)	0.30	1.63	1.86	2.35	2.69	3.01	4.51	3.23
State excise	0.00	0.13	0.02	0.20	0.16	0.79	2.27	1.01
Others	0.91	0.82	0.92	1.14	1.41	1.60	2.41	1.69
All indirect taxes	3.63	6.31	7.36	9.66	11.86	14.80	30.19	17.96
Rural and Urban combined								
Central taxes	1.72	2.05	2.88	4.13	5.04	7.21	14.71	6.77
Central excise	1.47	1.66	2.27	3.31	3.97	5.69	11.55	5.34
Import duty	0.24	0.39	0.61	0.81	1.07	1.52	3.16	1.43
State Taxes	1.24	1.58	2.01	2.73	2.88	4.19	7.24	3.77

	Monthly expenditure groups (in Rs.) per capita							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Rural and Urban combined								
Sales-tax (including sales tax on motor spirit)	0.65	0.93	1.16	1.44	1.63	2.13	3.39	1.93
State excise *	0.21	0.25	0.27	0.54	0.32	0.89	2.01	0.80
Others	0.39	0.41	0.59	0.74	0.92	1.12	1.85	1.04
All indirect taxes	2.96	3.63	4.89	6.85	7.92	11.40	21.96	10.54

*On alcoholic drinks.

6.16 It will be observed that Central taxes account for the larger share of incidence in both rural and urban sectors. But the difference is much more substantial in relation to the urban sector (Central taxes accounting for 12.0 per cent, and State taxes for 5.9 per cent) than in relation to the rural sector (Central taxes 5.0 per cent and State taxes 3.0 per cent).

6.17 Another important conclusion to be drawn from the table is that the Central indirect taxes are more progressive than the State taxes. Central excise, contributing about 50 per cent. to total incidence, is of course the most important single tax and is also seen to be the most progressive. However, the two taxes that fall more lightly on the lowest two expenditure groups are import duties and State excise on liquor, whereas Central excise and Sales taxes account for 72 per cent. of the incidence on them.

INCIDENCE BY TYPE OF GOODS

6.18 One of the novel features of this study is that an attempt has been made for the first time in India to work out the incidence of tax on major types of goods separately. Goods subject to tax have been classified into three main groups according to the nature of use, namely: (i)mostly in the nature of consumption goods (hereafter called 'consumption goods'), (ii) mostly in the nature of intermediate goods including raw materials (hereafter called 'intermediate goods') and (iii) capital goods, partly capital goods and parts thereof. The contribution of the indirect taxes on each group of commodities to the aggregate incidence is brought out in Table 3 below:

TABLE 3 - TAX BURDEN AS PERCENT OF CONSUMER EXPENDITURE ON ALL INDIRECT TAXES ACCORDING TO TYPE OF GOODS

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All households
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
				(Percentages)				
RURAL								
1. Consumption goods	1.28	1.51	2.08	3.20	3.16	5.18	8.53	4.05
2. Intermediate goods	1.47	1.62	2.10	2.63	3.17	4.32	6.78	3.53
3. Capital goods, partly capital goods and parts thereof	0.16	0.21	0.27	0.35	0.39	0.53	0.86	0.45
4. Total (all indirect taxes)	2.91	3.34	4.45	6.18	6.72	10.03	16.17	8.03
URBAN								
1. Consumption goods	1.82	3.06	3.62	5.16	6.36	8.38	14.78	9.17
2. Intermediate goods	1.81	2.90	3.38	4.10	5.00	5.80	12.57	7.48
3. Capital goods, partly capital goods and parts thereof	0.00	0.35	0.36	0.40	0.50	0.62	2.84	1.31
4. Total (all indirect taxes)	3.63	6.31	7.36	9.66	11.86	14.80	30.19	17.96

Contd.....

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All households
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
				(Percentages)				
RURAL AND URBAN COMBINED								
1. Consumption goods	1.32	1.66	2.31	3.58	3.91	6.10	11.11	5.34
2. Intermediate goods	1.47	1.75	2.30	2.91	3.59	4.75	9.17	4.53
3. Capital goods, partly capital goods and parts thereof	0.16	0.22	0.28	0.36	0.42	0.55	1.68	0.67
4, Total (all indirect taxes)	2.95	3.63	4.89	6.85	7.92	11.40	21.96	10.54

6.19 It is observed that of the total incidence of 10.54 per cent of consumption expenditure for all households, the share of consumption goods is 5.34 percentage points, amounting to about 51 per cent of total incidence. 4.53 percentage points are accounted for by intermediate goods. Only the remaining 0.63 percentage point is contributed by capital goods, partly capital goods (including capital goods which are also used as household durables) and parts thereof. (This amounts to about 6 per cent of total incidence). More or less, the same proportions are observed in both the rural and urban sectors, even though the level of the incidence on urban households is nearly double that on the rural households. In both the sectors, consumption goods account for around 50 per cent of the total incidence and the share of capital goods, partly capital goods and parts thereof amounts to about 6 to 7 per cent of the incidence. The remaining portion of incidence is attributable to intermediate goods. One point that deserves to be noted is that in the rural sector, the incidence of taxes on intermediate goods is higher than that of taxes on consumption goods for the lowest two per capita expenditure groups. For all the groups above them, the incidence of taxes on consumption goods is higher; whereas in the urban sector, the incidence of taxes on intermediate goods is slightly lower for the same two per capita expenditure groups.

6.20 When we look at the figures of incidence of Central excise duties and import duties according to types of goods as given in the Tables 4 and 5 below, we get a somewhat different picture. In respect of excise as well as import duties, intermediate goods claim the largest share of the incidence both in the rural and the urban sectors.

TABLE 4 - BURDEN OF CENTRAL EXCISES AS PER CENT. OF CONSUMER EXPENDITURE ACCORDING TO TYPE OF GOODS

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All households
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	(Percentages)							
RURAL								
1. Consumption goods	0.39	0.39	0.61	1.16	1.21	2.11	3.64	1.57
2. Intermediate goods	1.03	1.10	1.39	1.74	2.04	2.70	4.13	2.24
3. Capital goods, partly capital goods and parts thereof	—	0.01	0.01	0.02	0.02	0.04	0.10	0.04
4. Total Central excise	1.42	1.50	2.01	2.92	3.27	4.85	7.87	3.85
URBAN								
1. Consumption goods	0.61	1.13	1.51	2.25	3.03	3.91	7.00	4.28
2. Intermediate goods	1.81	1.96	2.22	2.67	3.19	3.76	8.70	5.04
3. Capital goods, partly capital goods and parts thereof	—	0.02	0.02	0.02	0.03	0.10	1.08	0.41
4. Total Central excise	2.42	3.11	3.75	4.94	6.25	7.77	16.78	9.73

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
RURAL AND URBAN COMBINED								
1. Consumption goods	0.41	0.46	0.74	1.37	1.63	2.62	5.03	2.25
2. Intermediate goods	1.06	1.19	1.52	1.92	2.31	3.01	6.01	2.95
3. Capital goods, partly capital goods and parts thereof	—	0.01	0.01	0.02	0.03	0.06	0.51	0.14
4. Total Central excise	1.47	1.66	2.27	3.31	3.97	5.69	11.55	5.34

TABLE 5 - BURDEN OF IMPORT DUTIES AS PERCENT OF CONSUMER EXPENDITURE ACCORDING TO TYPE OF GOODS

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	(Percentages)							
RURAL								
1. Consumption goods	0.02	0.04	0.11	0.16	0.24	0.34	0.56	0.25
2. Intermediate goods	0.23	0.30	0.42	0.52	0.67	1.01	1.65	0.79

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
RURAL				(Percentages)				
3. Capital goods, partly capital goods and parts thereof	0.01	0.03	0.05	0.08	0.08	0.13	0.22	0.10
4. Total import duties	0.26	0.37	0.58	0.76	0.99	1.48	2.43	1.14
URBAN								
1. Consumption goods	—	0.09	0.15	0.20	0.28	0.34	1.37	0.65
2. Intermediate goods	—	0.48	0.60	0.76	0.97	1.15	2.54	1.48
3. Capital goods partly capital goods and parts thereof	—	0.06	0.06	0.07	0.11	0.14	0.30	0.17
4. Total Import duties	—	0.60	0.81	1.03	1.36	1.63	4.21	2.30
RURAL AND URBAN COMBINED								
1. Consumption goods	0.02	0.04	0.12	0.17	0.25	0.34	0.90	0.35
2. Intermediate goods	0.21	0.32	0.44	0.56	0.73	1.05	2.02	0.96
3. Capital goods, partly capital goods and parts thereof	0.01	0.03	0.05	0.08	0.09	0.13	0.25	0.12
4. Total Import duties	0.24	0.39	0.61	0.81	1.07	1.52	3.17	1.43

— indicates negligible

6.21 If we take Central excises, we find that the incidence of taxes on intermediate goods account for 2.95 percentage points, out of the total 5.34 per cent of consumption expenditure attributable to excises in respect of all households. In the case of import duties, the share of intermediate goods is 0.96 percentage points out of 1.43 per cent of consumption expenditure attributable to total import duties. In other words, 55 per cent of the incidence of Central excise duties and 67 per cent of the incidence of import duties are due to taxes on intermediate products. It is also note-worthy that in respect of both taxes, the relative contribution of intermediate goods to incidence was higher for the rural sector than for the urban sector. Taking into account this and the earlier conclusion regarding the burden of taxes on intermediates falling on the lowest expenditure groups, we can say that more reliance is placed on the taxation of intermediate goods for reaching the poorer sections and the rural sector.

6.22 In the case of State taxes, however, consumption goods account for a very high share of incidence as compared to the other two groups of commodities, for both the rural and urban sectors. As seen in Table 6 below, of the aggregate incidence of 3.77 of consumption expenditure attributable to State taxes, consumption goods contribute 2.74 percentage points.

TABLE 6 - BURDEN OF STATE TAXES AS PER CENT OF CONSUMER EXPENDITURE ACCORDING TO TYPE OF GOODS

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All households
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	(Percentages)							
RURAL								
1. Consumption goods	0.87	1.08	1.36	1.88	1.71	2.73	4.33	2.23
2. Intermediate goods	0.21	0.22	0.29	0.37	0.46	0.61	1.00	0.50
3. Capital goods, partly capital and parts thereof	0.15	0.17	0.21	0.25	0.29	0.36	0.54	0.31
4. Total State taxes.	1.23	1.47	1.86	2.50	2.46	3.70	5.87	3.04

	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
URBAN								
1. Consumption goods	1.21	1.84	1.96	2.71	3.05	4.13	6.41	4.24
2. Intermediate goods	--	0.46	0.56	0.67	0.84	0.89	1.33	0.96
3. Capital goods, partly capital goods and parts thereof	--	0.27	0.28	0 31	0.36	0.38	1.46	0.73
4. Total State taxes	1.21	2.57	2.80	3.69	4.25	5.40	9.20	5.93
RURAL AND URBAN COMBINED								
1. Consumption goods	0.89	1.16	1.45	2.04	2.03	3.14	5.18	2.74
2. Intermediate goods	0.20	0.24	0.34	0.43	0.55	0.69	1.14	0.62
3. Capital goods, partly capital goods and parts thereof	0.15	0.18	0.22	0.26	0.30	0.36	0.92	0.41
4. Total State taxes	1.24	1.58	2.01	2.73	2.88	4.19	7.24	3.77

-- indicates negligible

6.23 Table 7 below, gives a broad picture of the distribution of the burden of taxes on selected consumer goods and intermediates among urban households in different expenditure groups.

BURDEN OF TAXES ON SPECIFIC COMMODITIES

TABLE 7 - DISTRIBUTION OF THE BURDEN OF INDIRECT TAXES AS PER CENT OF TOTAL CONSUMPTION EXPENDITURE (1973-74) - FOR URBAN HOUSEHOLDS

Commodities	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All urban house-holds
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	(Percentages)							
Foodgrains and atta*	0.30	0.37	0.36	0.33	0.28	0.24	0.18	0.26
Sugar	0.61	0.46	0.60	0.55	0.54	0.51	0.38	0.47
Tea & Coffee	0.00	0.05	0.14	0.15	0.22	0.33	0.28	0.23
Vegetable product, oil & fats	0.00	0.33	0.46	0.52	0.50	0.50	0.40	0.47
Kerosene oil	0.00	0.48	0.51	0.54	0.51	0.50	0.45	0.50
Drugs and medicines	0.00	0.09	0.17	0.23	0.28	0.36	0.52	0.36
Tobacco products	0.00	0.34	0.57	1.03	1.16	1.55	3.12	1.80
Liquor*	0.00	0.13	0.02	0.20	0.16	0.74	2.46	1.03
Cotton fabrics	0.00	0.12	0.01	0.18	0.51	0.59	1.68	0.81
Art and rayon silk	0.00	0.00	0.00	0.02	0.15	0.25	1.31	0.52
Matches	0.00	0.05	0.07	0.10	0.09	0.06	0.05	0.07
Soap and detergents	0.00	0.08	0.11	0.11	0.12	0.12	0.11	0.11
Paper and paper products	0.00	0.03	0.03	0.09	0.21	0.20	0.31	0.22
Motor spirit	0.00	0.18	0.21	0.26	0.28	0.29	4.45	1.66

*taxes on these commodities are levied only by the States

Commodities	Monthly per capita expenditure groups (in Rs.)							
	0-15	15-28	28-43	43-55	55-75	75-100	100 and above	All urban households
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
				(Percentages)				
Refined diesel oil	0.00	0.33	0.35	0.52	0.73	0.7	1.36	0.88
Tyres and tubes	0.61	0.10	0.10	0.13	0.16	0.17	0.39	0.23
Iron & steel	0.00	0.48	0.54	0.68	0.76	0.80	1.30	0.91
Total for 17 items	1.52	3.62	4.25	5.64	6.66	8.00	18.75	10.53
Total incidence for all indirect taxes	3.63	6.31	7.36	9.66	11.86	14.80	30.19	17.96

From this one can see at what level of expenditure taxes on important consumer goods become significant and also whether the incidence of taxes on particular goods is regressive or progressive. Among the food products, the taxes on sugar and foodgrains and atta affect all expenditure groups. Even the lowest expenditure group pays nearly one per cent of its total expenditure of less than Rs. 15 per capita, per month, as taxes on these products. As might be expected, taxes on these products are regressive even with respect to total expenditure. However, in the case of sugar it cannot be assumed with certainty that the entire quantity of levy sugar purchased by the lower expenditure groups is consumed by them. To the extent that such sugar gets diverted for other uses, the regressiveness may be overstated. On the other hand, the incidence inregard to cotton fabrics may be understated, as the general tendency is to purchase them during certain seasons and the study may not have fully reflected such contingencies. The taxes on kerosene become significant at the level of the second lowest expenditure group (Rs. 15-28 per capita, per month), and its incidence tends to be proportional with respect to expenditure. This is also broadly true of the excise on matches, although the percentage burden is so low as to be of no great consequence. Taxes on drugs and medicines also affect the poorer classes, although in their cases the incidence is clearly progressive. A broad conclusion that emerges from this analysis is that a reduction in the weightage of taxes on mass consumption goods, such as, foodgrains, sugar and kerosene, that tend to be regressive or proportional, would serve to increase the degree of progression of the indirect tax system as a whole. As regards drugs and medicines, the same purpose could be served by reducing the weight of tax on the more widely used varieties of drugs.

6.24 Another important fact brought out by the above table is that the taxation of certain intermediate products, such as, iron and steel, diesel oil and tyres and tubes, has a pervasive effect. Thus, as pointed out earlier, the tax on tyres and tubes is one of the important elements in the tax burden of the lowest expenditure group; the tax on iron and steel and refined diesel oil reach all but the lowest expenditure groups. However, the incidence of these taxes turns out to be progressive. But when we look at the problem from the standpoint of equity and social justice, the mere fact of progression is not enough and our aim must be to have lower rates of taxation on what we regard as basic necessities and articles whose consumption we want to promote rather than discourage. From this angle, it would have to be examined whether the level of the levies on certain product groups, such as, drugs and medicines, or those which impinge on transport costs, would need some reconsideration.

SHARE IN CONSUMPTION AND INDIRECT TAXES OF DIFFERENT EXPENDITURE GROUPS

6.25 The share of the different expenditure groups in total consumption expenditure and their respective shares of indirect taxes have also been worked out. The information presented in Table 8 below also gives the percentage of the population in different expenditure groups.

TABLE 8 - SHARE OF DIFFERENT EXPENDITURE GROUPS IN TOTAL CONSUMPTION EXPENDITURE AND THEIR RESPECTIVE SHARES OF INDIRECT TAXES. (1973-74)

(figures given are in per cent)

Per capita consumption expenditure (Rs/month)	Share of			
	Population of households	Consumption expenditure of households	Consumption expenditure of households less indirect taxes	Indirect taxes
(1)	(2)	(3)	(4)	(5)
Upto 15	0.64	0.14	0.15	0.04
15-28	11.19	4.58	4.93	1.58
28-43	29.80	18.75	19.93	8.70
43-55	20.31	17.42	18.14	11.33
55-75	19.63	22.08	22.73	16.58
75-100	10.16	15.35	15.20	16.61
Above 100	8.27	21.68	18.92	45.16
Total	100.00	100.00	100.00	100.00

6.26 It is seen that the highest expenditure group, forming about 8 per cent of the population, accounts for 22 per cent of consumption expenditure inclusive of taxes and contributes about 45 per cent to indirect taxes. These taxes have the effect of reducing the share of this group in consumption expenditure from 22 per cent to about 19 per cent (See column 4). At the other end of the scale, the lowest two expenditure groups, forming about 12 per cent of the population, account for only 4.7 per cent of expenditure and contribute 1.6 per cent of indirect taxes. As might be expected, there is quite an unequal distribution of consumption expenditure with the share in population of the lowest three expenditure groups (41.6 per cent) being higher than their share in consumption expenditure (23.5 per cent). At the upper end of the scale, the two highest expenditure groups account for 37 per cent of expenditure while their share in population is only around 18 per cent.

COMPARISON WITH ESTIMATES OF INCIDENCE OF EARLIER STUDIES

6.27 As already indicated, at the all-India level, there have been 3 earlier studies of incidence of indirect taxes, one by the Taxation Enquiry Commission (for 1953-54) and the other two by the Ministry of Finance, Government of India (for 1958-59 and 1963-64). The results of the earlier studies, however are not strictly comparable with those of the present study. There are three main reasons for this. First, all the earlier studies used NSS data on consumption expenditure according to household monthly expenditure groups. The expenditure groups considered in the first two studies were. Rs.1-50, Rs.51-100, Rs.101-150, Rs.151-300 and above Rs.300; in the study for 1963-64 , the household expenditure groups considered were. Rs.0-50, Rs.51-100, Rs.101-150, Rs.151-300, Rs.301-500 and Rs.500 and above. In the present study, households have been divided into monthly per capita expenditure groups because the relative economic positions of different households are more accurately reflected by per capita expenditure levels. This difference in the classification of households between the present study and the earlier studies makes the results strictly not comparable. Second, as we have already indicated, indirect taxes estimated to have been collected on the purchases of goods by the Government administrative departments have been excluded from the total taxes allocable to households, whereas no such adjustment was carried out in the earlier studies. Again, in the present study, only one-tenth of the taxes on capital goods has been assumed to be shifted to consumers in the year of levy, whereas the total tax collections from capital goods were allocated to different consumer groups in the earlier studies. Third, owing to the availability of more disaggregated data, it has been possible to apportion tax burdens more accurately. In this connection, special mention may be made of the fact that we were able to obtain data on commoditywise sales tax collections from 13 major States, which have been used as a basis for the allocation of sales taxes. Moreover, we have also been able to use information obtained from the material balances given in the Technical Note on the Approaches to the Fifth Plan of India, 1974-79 for the purposes of allocating the taxes on inputs.

6.28 Subject to these qualifications, we might make a rough comparison between the results of the present study with those of the Ministry of Finance for the year 1963-64 in respect of only two expenditure groups. On the assumption that an average family consists of five persons, the per capita expenditure group of Rs.100 and above in the present study can be converted into a household expenditure group with an expenditure of Rs.500 and above. The incidence of taxes on this group and on all households can then be compared as between the two studies.. An attempt in this direction is made in Table 9 given in the following page.

TABLE 9 - A COMPARATIVE STATEMENT OF INCIDENCE OF INDIRECT TAXES IN 1963-64 AND 1973-74.

(Figures in per cent)

Indirect taxes	Rural		Urban		All India	
	Rs. 500 and above	All households	Rs. 500 and above	All households	Rs. 500 and above	All households
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1963-64						
1. Central taxes	10.47	5.76	23.16	11.07	15.65	7.08
(a) Central excise	7.47	3.95	16.10	7.70	10.99	4.89
(b) Import duty	3.01	1.81	7.06	3.37	4.66	2.19
2. State taxes	4.22	2.26	10.12	5.53	6.62	3.07
(a) State excise	0.67	0.52	0.94	0.48	0.78	0.49
(b) Sales tax*	2.59	1.24	7.02	3.67	4.39	1.88
(c) Others	1.41	0.82	2.16	1.38	1.45	0.70
3. All indirect taxes	14.69	8.02	33.28	16.60	22.27	10.15
1973-74						
1. Central taxes	10.30	4.99	20.99	12.03	14.71	6.77
(a) Central Excise	7.87	3.85	16.78	9.73	11.55	5.34
(b) Import duty	2.43	1.14	4.21	2.30	3.16	1.43
2. State taxes	5.87	3.04	9.20	5.93	7.24	3.77
(a) State excise	1.82	0.73	2.27	1.01	2.01	0.80
(b) Sales tax*	2.60	1.49	4.51	3.23	3.39	1.93
(c) Others	1.45	0.82	2.41	1.69	1.84	1.04
3. All indirect taxes	16.17	8.03	30.19	17.96	21.95	10.54

*Includes Central sales tax and sales tax on motor spirit.

6.29 It is seen that there are only marginal differences in the level of burden of total indirect taxes as between the two studies. The similarity particularly is noticeable in respect of all households. One of the reasons why the level of burden is not shown to have risen since 1963-64 is the fact that in the present study we have excluded as much as 15 per cent of total indirect tax revenues from the allocable pool. Therefore, the similarity in the levels of incidence between the two studies should not be taken at face value.

6.30 All the three earlier studies had also revealed a progressive distribution of indirect taxes with reference to consumer expenditure. The present study indicates a much more progressive pattern of indirect taxation than the earlier studies. In the MF study for 1963-64, the incidence for the rural sector varied from 5.77 per cent for the lowest expenditure group to 14.69 per cent to the highest expenditure group; and for the urban sector, the range was from 11.3 per cent to 13.28 per cent. In the present study, for the rural sector, the incidence varies from 2.91 per cent to 16.17 per cent and for the urban sector, from 3.63 per cent to 30.19 per cent. The more progressive distribution shown in the study for 1973-74 may be partly attributed to changes in the pattern of taxation. However, the difference in methodology would also have contributed partly to the difference in results.

ANNEXURE TO CHAPTER 6

THE INCIDENCE OF INDIRECT TAXES IN INDIA (1973-74)

A technical note on the definition and measurement of incidence of taxation

1. The question of incidence of taxation has been of long-standing interest and intense debate among professional economists. It is one of those economic questions the interest in which is shared by political leaders and the public, because taxes are seen and felt to affect the lives of households and fortunes of business. The incidence of taxation has traditionally been defined to mean the final resting place of the money burden of taxation. For every unit of revenue raised by the government, there is a corresponding reduction in the income of some one or another, and tracing the incidence of a tax is, therefore, to find out whose incomes are reduced as a result of the imposition of that tax. Going behind the monetary phenomena, one could consider the action of the government in terms of the use of real resources. Generally speaking, it could be said that the government uses the tax proceeds to divert real resources to itself and that this causes a reduction in the real incomes available for private use. The incidence of taxation is on those who ultimately suffer the reduction in real incomes equivalent in total to the amount of resources which the government has appropriated. A measure of incidence is hence obtained by expressing the money burden as a percentage of the money income of the individuals or groups concerned.

CONCEPT OF INCIDENCE

2. Besides enabling the government to transfer real resources to itself, taxes (may) have other effects: they often interfere with consumers' choice and distort expenditure patterns; they may lead to less efficient use of factor inputs and thus affect total output; and they may affect the rate of savings and investment and hence the rate of growth. All these effects may impose additional burdens and hence the total reduction in income available for private use caused by a tax may be greater than that corresponding to the amount of revenue obtained. However, these secondary effects are generally excluded from the concept and measurement of incidence of taxation and attention is concentrated on the direct money burden as being the most important aspect of the matter.

3. The traditional concept of incidence has been criticised in recent years, and new ways of looking at the question have been suggested. It is pointed out that taxation by itself does not cause a reduction in real income available for private use; it is public expenditure that absorbs real resources. Taxes may be increased or reduced for any number of reasons without changing the level of real public expenditure. It is argued, therefore, that taxation only changes the distribution of income and that the incidence of taxation should accordingly be defined as the change in the distribution of real income available for private use.

4. The magnitude and nature of change in real income can only be studied by comparing two situations: the state of distribution before the tax with that after the imposition of the tax (or situations without and with the tax). The problem here is that if we assume that a tax is imposed (or an existing tax increased), something else also changes; either public expenditure increases or

there will be a change in the budget balance. In either case, the change in the distribution of real income will be due to the combined effects of the tax and something else and not those of the tax alone. Professor Musgrave has suggested that the combined effect of an equal increase in tax and public expenditure might be termed "budget incidence". If the effect on the distribution of a given tax is to be isolated, other things must be held constant. This can only be done by replacing one tax by another of equal yield. The distributional consequence of substituting one tax for another of equal yield is termed "differential incidence". Currently, most fiscal theorists seem to prefer the concept of differential incidence.

5. However, the concept of differential incidence relates to a change in the tax system. It cannot, strictly speaking, be applied to measure the incidence of an existing structure of taxation. On the other hand, if one wishes to apply the concept of budget incidence, one would have to compare two situations — the state of distribution without a budget and that with the existing budget. But it is impossible to wish away the entire budget, for it would make no sense to make a comparison with a state of the economy without a government. Some writers try to get out of this difficulty by assuming that the existing tax system is being substituted for a hypothetical, neutral tax, such as, a proportional income tax of equal yield.* But this conceptual device would make no difference to the numerical results; one would get the same results if one simply measured the absolute incidence of the system as such.**

6. Despite the theoretical arguments that several economists have adduced in favour of the concept of differential incidence, the fact remains that the public are interested in knowing whether the existing tax system distributes the burden in an equitable manner. While from the econometric point of view, the concept of differential incidence lends itself to more accurate measurement, it would by no means be illegitimate to ask the question: "Who pays the existing taxes?", although there are difficulties in providing an accurate, quantitative answer. In the present exercise, according to our terms of reference, we shall be attempting to measure the incidence of the existing system of indirect taxes in India on the implicit assumption that the volume and pattern of government expenditure is given and that all the tax revenues are spent.

7. The theory of incidence in economic literature is largely based on deductive reasoning; it attempts to trace the direction and the relative magnitude of shifting of particular taxes under different circumstances. One way of measuring the incidence of a given tax or a set of taxes is to quantify the conclusions of such deductive reasoning. However, the results of this reasoning are not always logically conclusive; and furthermore, one would like to empirically test conclusions based on deductive reasoning before applying them to real world situations. Ideally, therefore, one should prefer the alternative method of specifying tentative hypothesis regarding shifting and of econometrically testing them. The results of the econometric exercise would provide the empirical basis for working out the incidence of the tax system. While this might be the conceptually

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* Pechman, Joseph A., and Okner Benjamin A., Who Bears The Tax Burden? Studies in Government Finance, the Brookings Institution, Washington D.C. 1975.

** Luc De Wulf, "Fiscal Incidence Studies in Developing Countries. Survey and Critique", IMF Staff Papers Vol. I XXII, No. 3 March, 1975, p. 97.

perfect solution, formidable statistical and other difficulties arise in carrying out the needed econometric exercises. In fact, in order to deal satisfactorily with broad-based taxes, such as excises and the general sales tax, we would need a full-fledged econometric model of the economy. The formulation and estimation of such a model lies in the future. Again, the econometric method is more relevant for the measurement of differential incidence than for estimating the incidence of an existing tax system. For these reasons, we have to take recourse to the method of quantifying the conclusion of deductive reasoning in the theory of incidence.

8. Commodity taxes could be selective or general. It is generally argued that the incidence of a selective tax on a commodity would be divided between the buyers and the producers (factor owners) in the proportion of the (price) elasticity of the supply of the commodity to the elasticity of the demand for it. Only if the supply were perfectly elastic, the entire burden would be shifted to the consumers; conversely, only if the demand were perfectly elastic, the entire burden would remain with the factor owners. The elasticity of supply depends crucially upon the capacity of, and the scope for, the factors of production in the taxed industry to move to untaxed fields. If a factor of production is specific to a particular industry, i.e., the industry that is taxed, then it would have to stay there and accept a cut in earnings. On the other hand, if the factor is capable of being employed in alternative industries, some units of the factor would move out, the supply of that factor to the taxed industry would be cut and the level of earnings would not be significantly affected. The price of the product would correspondingly rise. Now, in the short run, it may not be possible for several factors of production to move out of a taxed industry. In the long run, however, new vistas open up, old machines get worn out and need not be replaced, and similarly the existing work force is not fully replaced. As time passes, therefore, supply can be expected to become more and more elastic. Hence the assumption that in the long run supply is more or less perfectly elastic and that the incidence of a selective commodity tax will be fully shifted on to consumers.

9. Let us now consider a general excise or sales tax falling on all commodities and services. One school of thought believes that if such a tax were to be levied at one rate covering all goods and services, it would be equivalent to a proportional income tax on all factor earnings. This conclusion is based on the reasoning that since all industries are taxed, there are no untaxed fields to which factors could migrate even in the long run in an effort to avoid a cut in their earnings as a result of the tax. This means that all factors will have to accept a proportionate reduction in their incomes. One could even assume that prices rise as a result of the general tax. But since the general tax applies to consumer goods as well as capital goods, consumers as well as investors will be affected. In other words, the tax will fall on consumption and saving, which is equal to income. Thus, it is argued, whether the general price level rises or not, as a result of the tax, the burden of the tax will be distributed in proportion to incomes.

10. In examining the above view, one has to rule out the hypothetical case in which prices do not rise as a result of the general tax. Since we are assuming that all tax revenues are spent, the demand for factors and factor incomes will not fall and prices will have to rise. And this will happen given an elastic credit structure. The argument of such writers as Prof. Musgrave that even if prices rise, the burden of the general tax is distributed in proportion to income and not consumption, is based on the premise that the tax on the capital goods rests on the investors. A more plausible view is that in course of time the tax on the capital goods also will be shifted to the consumers

of the products for whose manufacture the former are used. If this happens, the burden of a general commodity tax will rest ultimately with the consumers.

11. Even this last conclusion will be fully valid only on the assumption of the existence of competition and the long-run mobility of factors of production and of the absence of controlled markets and wholly specific factors of production, such as land, that can be put to only one use. All these assumptions and the reasoning given in the previous paragraph are implicit in the view that all commodity taxes are, sooner or later, fully shifted on to the consumers. Since every one of the needed assumptions will not always be fulfilled, this view of incidence will not turn out to be entirely correct. Moreover, since considerable time may elapse before certain factors can move out of various taxed industries, part of the incidence of a number of taxes may be on the producers at any given time. What may broadly be true, however, is that the major part of the burden of commodity taxation as a whole will be on the consumers.

12. In the present exercise, we proceed on the assumption that the entire burden of commodity taxes is shifted to consumers including the government sector who bear it in proportion to their consumption of the various taxed commodities. Indeed, in a sense, our empirical effort amounts to nothing more than working out and applying techniques of quantifying that assumption. Most of the earlier studies, referred to in the text also had attempted to measure incidence on the basis of a similar assumption.

BASIC METHODOLOGY

13. As would have become clear from our earlier discussion, the present study aims at allocating only the money burden of indirect taxes levied by the Central and State Governments measured as equivalent to tax revenues collected from the non-government sector.* Moreover, it does not take into account the benefits accruing to different households as a result of government services financed by tax revenues. It is assumed that all taxes are passed forward to the consumers except a certain portion which is taken to be borne by the Government itself. The basic problem is to ascertain the tax element in the expenditures of household in different expenditure groups. NSS data provide details of consumption expenditure of households classified according to ranges of per capita monthly expenditure. Using these data, the taxes on different commodities could be allocated to different expenditure groups.

14. One way of doing this is to take the values or physical quantities of consumption of different commodities by each expenditure group and multiply them by the relevant tax rates. Apart from the fact that the data on the physical amounts of consumption are not readily usable, this method runs into a major difficulty, namely, that the total amount of allocable tax on a particular commodity obtained by multiplying tax rates with the value or volume of consumption is seldom equal to the actual yield of tax on that commodity. This discrepancy is partly due to the concessions and exemptions granted (for which proper allowance cannot be made while using consumption data) and partly due to evasion. Moreover, it is not always possible to match the classifications

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* For the purpose of the present study, the non-government sector is taken to include, apart from households and private businesses, departmental and non-departmental undertakings. The reason for this is explained later.

in the consumption data with that used in the tax laws. Because of these reasons, an alternative method has been employed by us. We have allocated the actual tax yield from a commodity among the expenditure groups according to the proportions of their cash expenditure on the consumption of that commodity. The same procedure was also followed by the MF studies in relation to the allocation of Central taxes.

15. A number of problems arise in the apportionment of tax revenues among the households in the different expenditure classes. We shall deal with a few important ones here. The details of procedure adopted for allocating taxes on major individual items that created special difficulties are described in Appendix 9.

16. The task of allocation would have been fairly straight forward if only consumption goods and services were subjected to tax. As it is, not only consumer items, but also items of machinery, intermediate products and services that enter into productive processes are also subject to various levies at different stages. We have assumed, as indicated earlier, that the taxes on capital goods and inputs are all passed on to the consumers of the products for whose manufacture they are used. A large number of inputs are each used in the manufacture of several products. Also, many goods are used both as inputs and as final products. Hence not only are taxes on two portions of several goods to be allocated differently, but also the proportions in which the output of each input is used in the production of different products have to be ascertained. What is ultimately to be done is to add the proper fractions of taxes on the inputs to the taxes on the concerned final products in order to derive the cumulative burdens on the latter. The cumulative burdens can then be apportioned on the basis of expenditure on consumer of final goods. Theoretically, the most satisfactory way of working out the cumulative burden on final products would be to use an input-output model for the economy. Given the tax rates on individual products and the input-output relations, a tax "matrix" can be prepared, which would enable one to allocate the taxes to "final products", i.e., units of goods used for consumption. Dr. Dey, in the study previously referred to, used the 144 sector input-output table constructed by Saluja for the year 1964-65.* His methodology marked a significant improvement over the approach of the MF studies in which the entire proceeds of taxes on capital goods and inputs were allocated on the basis of consumption of manufactured goods. The reliability of the empirical results derived through the use of the input-output model, however, depends on the reliability of the input-output relations as well as on the degree of disaggregation of data. Tax categories are usually more numerous than the commodity groupings in the input-output matrix; certainly they are more than the 144 sectors in Saluja's table.

17. For the present study, the original intention was to produce two alternative estimates: one based on a larger input-output table for 1968-69 being then constructed at the Planning Commission and the other to be derived through a more simple-minded, case by case allocation of taxes on inputs and machinery to the different expenditure groups on the basis of their pattern of consumption of final goods. As the construction of the input-output table was delayed for various reasons, we were unable to proceed with the first alternative. We are, therefore, presenting only one set of estimates, the manner of derivation of which is discussed later on.

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* M.R. Saluja, "Structure of the Indian Economy, 1964-65" Sankhya, Vol. 34, 1972 pp. 4-462.

18. Taxes on current inputs may be expected to be passed on to consumers without any time-lag. Taxes on machinery items, on the other hand, raise the cost of purchase of machinery and can only be passed on to the consumers of their products through higher depreciation charges over a period of time. In the MF studies, the entire taxes on machinery items were allocated to consumers in the year in which they were collected. By contrast, in the present study, the average life of plant and machinery is taken to be 10 years and, accordingly, only one-tenth of the taxes collected on machinery items in 1973-74 is assumed to be passed on to the consumers during that year.

19. Another major problem relates to the incidence of taxes on commodities and services purchased by the Central and State Governments. If all government purchases are by law free of taxation, the government sector could be said to be paying no indirect taxes. As no such exemption has been provided for (except in certain cases, such as the import of defence equipment), when a government buys, or pays for the use of, taxed materials, it may be said to be paying taxes to itself. In this connection, the government sector has to be defined carefully. If a governmental or public sector unit sells its services or goods to the public, then it may be expected to pass on to consumers any taxes it pays on its inputs by charging correspondingly higher prices. It is only when a unit acts as part of what is called general government whose services are given free, that the taxes cannot be shifted. Hence departmental and non-departmental commercial undertakings in the public sector should be excluded from the definition of government sector for this purpose, and the indirect taxes paid by them should be treated on par with those paid by private sector enterprises. But the taxes paid by the government sector proper should be excluded from the allocable pool.

20. In the MF study of 1969, it was stated, "As for the tax element in government's consumption expenditure, no adjustment could be made due to absence of data. It was, however, ascertained that the amount involved was not dimensionally significant and any adjustment on that account, if possible, would have at best made a marginal difference to the results of this study."* Since the government sector had expanded rapidly in the decade since 1963-64, we considered it important to make the needed adjustment. It is true, however, that information on the value of different kinds of goods bought by the Government is not readily available, and in some cases not available at all. We explored several possible sources of data. Ultimately main reliance has been placed on the information contained in A Technical Note on the Approaches to the Fifth Plan of India, 1974-79 published by the Planning Commission (1973). We have been able to make adjustments with respect to goods bought for government consumption and the construction part of government capital formation. Details are given in Appendix 9. We found that nearly 5 per cent of total indirect taxes in 1973-74 were to be allocated to the government sector.

21. One further problem may be referred to. Subsidies are in a true sense negative indirect taxes. Strictly speaking, they should be set off against indirect taxes. Thus, while consumers of electricity may be paying an electricity duty, the Government may be covering the loss of electricity undertakings through subsidies out of general revenues. Not taking into account the subsidies

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* Ministry of Finance, Incidence of Indirect Taxation, 1963-64 op. cit., p. 3.

would mean over-estimating the burden on the consumers of electricity. However, one might raise the question if subsidies should be brought in when other types of beneficial expenditures are not being considered. Moreover, subsidies are partly open and partly hidden and a vast new areas would have to be covered, with its own several problems, if adequate note is to be taken of all subsidies granted by the Centre and the States. We have confined our attention to positive taxes.

SCOPE OF STUDY

22. This study covers all the indirect taxes levied by the Central and State Governments, excluding taxes on exports. They are: import duties, Union excise, sales taxes, State excise on liquor, tax on passengers and goods, motor vehicles tax, entertainment tax, electricity duty and other (minor) taxes and duties. Taxes levied by municipal and other local bodies have been left out. The most serious omission is that of octroi, on which the required data could not be obtained.

SOURCES OF DATA

23. For carrying out this study, we need data on (a) collection of all taxes on goods and services except taxes on exports; (b) pattern of expenditure of households in different per capita expenditure classes and (c) in certain cases, value or quantity of commodities subject to tax. Since the patterns of consumption as between expenditure groups vary from commodity to commodity, data permitting, the tax on each commodity has to be allocated separately. We needed, therefore, to obtain commodity-wise data on tax collections. Some indirect taxes fall on specific goods or services, e.g., the tax on motor spirit or the entertainment tax. Problems arise only in the case of general taxes. As regards import duties and excises, commodity-wise collection of these taxes is given in the Statistical Year Book on Central Excises and Customs. * This source has been used. But the State Government Budgets do not give commodity-wise classification of sales tax yield. (The yield of sales tax on motor spirit is separately available.) However, a number of State Governments have started collecting information on the yield of sales tax on different commodities or commodity groupings. We were able to obtain this information for 13 major States. The proportions worked out for the 13 States were applied to derive estimates of commodity-wise break-down of total sales tax collections in India. The figures of collections of other State taxes are taken from the Budgets of the State Governments and Union Territories.

24. The 28th round of NSS, carried out during the period October, 1973-June, 1974, is the latest comprehensive survey of household expenditure. An advance tabulation of the 28th round data was specially carried out for this study at the request of the Ministry of Finance. In this tabulation, households were divided into seven monthly per capita expenditure classes, namely, Rs. 0-15, Rs. 15-28, Rs. 28-43, Rs. 43-55, Rs. 55-75, Rs. 75-100 and Rs. 100 and above. Further, as in earlier tabulations, a vertical division of these expenditure groups into rural and urban households was also given so that we could work out the incidence of taxes on rural and urban households separately. Again, expenditure on particular items were divided, wherever necessary, into cash and non-cash expenditure. This division was essential because taxes on many commodities are paid only if they are bought for cash.

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* Published by the Directorate of Statistics and Intelligence, Central Excise and Customs, New Delhi.

25. The MF study of 1969 used NSS data of the 18th Round for the year 1963-64. The maximum number of items for which expenditure data were collected during the 18th Round was 187. The 28th Round of NSS canvassed information on 395 commodities and services (including sub-items). This vastly increased disaggregation of expenditure data has made possible a more accurate allocation of the indirect tax burden than in the earlier study.

26. The number of urban households covered in the sample for the 28th Round (the basis of the present study) was much higher than in the 18th Round, while the number of rural households was kept lower. The faster rate of growth of urban population during the intervening period, raising the proportion of urban population to total population, has warranted this change. A comparative picture of the number of rural and urban households covered in the 13th, 18th and 28th rounds of NSS is given in the following table.

TABLE - HOUSEHOLDS COVERED BY NSS SURVEY IN RURAL AND URBAN SECTORS 1957-58 to 1973-74.

NSS round and the reference year	Number of sample households covered		
	Rural	Urban	Total
1. 13th (1957-58)	6738	3583	10321
2. 18th (1963-64)	21572	4337	25909
3. 28th (1973-74)	15467	7881	23348

For estimates of production and clearance, where necessary, we have used the Statistical Year Book on Central Excise and Customs, referred earlier.

LIMITATION OF DATA

27. The main limitations of the data may now be briefly indicated here, beginning with the NSS data on consumption. First, the NSS concept of a household does not refer to a family unit, since a household is defined to comprise all persons who share a common kitchen irrespective of the number of earners. Domestic servants are also included if they eat from the same kitchen. This tends to understate the per capita expenditure of richer households. Second, the estimates of the non-cash component of expenditure are based on imputation. It is feared that in many cases where comparable market prices are not available, imputation is really based on rough guesses. To the extent that the consumption of home produced and home processed goods is wrongly estimated, biases are introduced. Third, the survey is spread over a period of six months during which prices of different commodities change, particularly during times of inflation. These price changes introduce distortions to some extent. Lastly, higher expenditure groups may tend to understate their consumption. Moreover, the value of perquisites enjoyed by the employees of private and public sector companies is not likely to be reflected in the NSS consumption expenditure data. To the extent that the consumption of richer employees is understated for this reason, the incidence will be shown to be more progressive (or less regressive) than it really is.

28. The aggregate value of consumption expenditure for the population as a whole in 1973-74, worked out on the basis of per capita NSS data and the population figures obtained from the office of the Registrar General, differs from the estimate of private consumption derived from national accounts (given by CSO) for the same year. The CSO's figure is higher. Following earlier practice, we have raised the NSS estimate of consumption expenditure for each expenditure group in the rural and urban sectors so as to arrive at a total expenditure equal to the CSO estimate. The exact procedure of adjustment is as follows: First, the CSO estimate of aggregate private consumption expenditure was split into rural and urban households' expenditures on the basis of the proportions between them in the NSS estimates. Secondly, ratios were worked out between consumption estimates according to the CSO and those according to the NSS for the rural and urban sectors separately. And, finally, the per capita expenditure figures for the different expenditure groups in the rural and urban areas were multiplied by the relevant ratios in order to raise them, so that the total consumption figure was made equal to the CSO estimate.

29. Turning to the limitations of tax data as stated earlier, an accurate classification of sales tax receipts by commodity groups is not available. We are forced to make use of estimates of yield of sales tax on different commodities, based on information furnished by 13 States. This would not have been a major limitation in itself. But we understand that the figures given by some of the States are themselves based on estimates. However, since the bulk of sales tax revenue is derived from a fairly limited number of staple commodities, the inaccuracies in the data furnished by the State Governments are not likely to bias the results to any significant extent.

30. The more basic problem is that the classification of goods given in the consumer expenditure data does not often match the tax categories, i.e., the classification of goods under which tax collections are shown. Moreover, in cases where different varieties of the same goods are taxed differently, information on the total yield of the tax on those goods is not sufficient for our purpose. We need the break-down of yield by varieties as also information on how much of the different varieties was consumed by each expenditure group. We cannot often get these details. Hence several assumptions regarding the pattern of consumption have had to be made in allocating these burdens in such cases. Appendix 9 describes the procedures adopted in relation to major commodity groups.

CHAPTER 7

THE ROLE OF INDIRECT TAXES

7.1 In Chapter 1, we have brought out the importance of indirect taxes in the Indian economy and have shown how with the rise in the tax ratio, the proportion of indirect taxes to total tax revenues has also been steadily increasing. The reasons for the large reliance on indirect taxes in a developing country like India are fairly obvious. In a highly advanced economy, with a high per capita income and a production structure characterised and dominated by large business undertakings, the Government is able to derive the major part of its tax revenues through the direct taxation of individuals and businesses. Income taxation, in particular, takes on the character of a mass tax, partly because the average income itself is quite high and partly because large-scale wage employment enables the collection of income tax on salaries at a minimum cost through the system of withholding. Per contra, in a developing economy, characterised by low incomes and widespread self-employment, the administrative costs of collecting small amounts of direct tax revenues from a multitude of low income earners becomes prohibitive. Moreover, since the income tax is generally tailored according to individuals' ability to pay, it also becomes necessary to provide for a tax-free slab to take care of the subsistence needs of a family. With average income being so low as it is in India, even a moderate amount of exemption would keep the vast majority of the working population outside the net of income tax. However, the most important reason for the relatively narrow coverage of income taxation in India is the administrative cost of extending its scope. In view of these considerations, the vast majority of the population has to be reached through the medium of indirect taxation. Indeed, since one of the prime objectives of taxation is to restrain increases in consumption, particularly non-essential consumption, so that real resources may be diverted without inflation for purposes of development, taxation has necessarily to fall on the bulk of the population.

REASONS FOR LARGE RELIANCE ON INDIRECT TAXES

7.2 How heavy the burden of taxation - direct and indirect - should be, depends largely on political judgment about the extent to which the people could be taxed to step up the rate of growth and to provide for other needs of Government including defence, and partly on economic considerations relating to savings, consumption and capital formation. We cannot express any views on the level of indirect taxation as a whole. Our main concern is with the structural aspects of indirect taxation. Accordingly, we enquire into the ways in which the tax system can, while meeting the requirements of revenue, minimise the burden on the poorer sections of the community, promote economic efficiency and further, rather than hinder, the objectives of planned development.

7.3 It is well recognized that taxation, while raising resources for the Government, should also subserve important socio-economic objectives. The major economic functions of indirect taxation in a developing economy are to enable the Government to transfer real resources to the public sector without inflation, to help raise savings and investment, and to influence the allocation of resources in the private sector of the economy according to social priorities. Given the imperative need to raise the rate of savings in our country, the role of indirect taxation in this area may be said to be crucial. But this role should be interpreted in a dynamic sense.

ROLE OF COMMODITY TAXATION

With low levels of income prevailing in the country and with the demonstration effect of high levels of consumption in advanced countries, the tendency of the people is to raise their levels of consumption as their incomes rise. Commodity taxation can and should play the role of preventing non-essential consumption from rising as much as income rises as a result of past investment. Through the tax structure, the ratio of additional savings to additional income - or the "incremental savings ratio" as it is technically described - should be made to rise. If the proportion of additional income saved is raised above the existing overall rate of saving, the latter will increase over time.

7.4 The objective of curtailing expenditure on relatively less essential items of consumption so as to step up the incremental savings ratio is best achieved by having substantially higher rates of taxation on articles of comfort and luxury than on the basic necessities of life. Such a system would also be in accord with the objective of ensuring progression in the indirect tax structure. Thus, on the kind of things which the wage earners consume - the so-called wage goods - the rate of taxation should be kept low, while products which are consumed by middle and higher income groups would need to be taxed at progressively higher rates. In any such attempt many practical problems arise. The same product may be consumed both by the rich and the poor, e.g., cloth. Then again, patterns of consumption are not static. New lines of production get established and new demands from different income groups emerge. A product which at one time was considered to be a luxury may, if it becomes cheap and plentiful, merit classification with wage goods. The structure of the tax system may, therefore, have to be changed as the economy itself develops. In a sense the task before us is to attempt a readaptation of the existing system to the changed conditions of the 1970's.

7.5 There is a considerable body of academic opinion which holds that indirect taxation should be general and neutral, i.e., it should not, as far as possible, interfere with the choices of consumers between products, or the choices of producers as between inputs and techniques of production, or investors' choice between different channels of investment. Such a view cannot be accepted without reservation in the Indian context. Indeed even from the purely theoretical point of view, neutrality is a desirable attribute only in so far as taxation is looked upon as purely a means of raising revenue. Since State intervention is recognised as a necessity even in countries with no formal system of planning, taxation is legitimately regarded as a general economic instrument for furthering social objectives. In India, where investment and production are to be carried on according to planned priorities and reduction of inequalities is an accepted objective, indirect taxation will have to be used, where necessary, in a non-neutral way for bringing about reallocation of resources as between different consumer products and for introducing progression in the distribution of the tax burden.

7.6 Similarly, one cannot always place reliance on the "free" market price to bring about an efficient allocation of resources. The market price of a resource may not reflect its true scarcity value to society; in such a case, indirect taxation can be used as a tool to conserve that resource and to encourage the utilisation of substitute resources which may be less valuable from the long-term interests of society.

7.7 It is argued by some fiscal theorists that selective excise taxation imposes an "excess burden" in terms of loss of human welfare as compared to a truly general tax, because the former tends to bring about a divergence between the price ratios of two or more commodities and their

respective marginal cost ratios.* But apart from the fact that such a divergence may not always cause a loss of welfare in real world situations, it has to be remembered that even if a loss of welfare occurs in the short-term, it may be more than compensated by the increase in the long-term welfare brought about by Government intervention.

7.8 While we are thus convinced that there is a case for the use of indirect taxation for the purposes of beneficial intervention in the market, it is equally necessary to emphasize that when the objective is merely to raise additional revenues every care must be taken to avoid unintenced interference with the efficient allocation of resources. We would, therefore, re-interpret the concept of neutrality in taxation in the context of the conditions and institutional structure of the Indian economy to say that, in so far as the objective is to raise revenue, indirect taxation should be non-discriminatory, but where intervention on economic considerations is called for, indirect taxation may be selectively used for causing diversion of resources through changes in relative prices. However, care should be taken to ensure that undue complications and unnecessary refinements of an ephemeral character are avoided. The intervention should be purposeful and carefully determined. It should consciously promote and not inadvertently affect the effecient allocation of resources.

CRITERIA FOR RATIONALISATION OF THE INDIRECT TAX SYSTEM

7.9 Ideally, one could think of devising an indirect tax structure consisting of two major components: one that could be general or broadly neutral and which could be used to raise a substantial part of revenue and the level of which could be changed as needed; and the other consisting of elements for controlling and regulating the economy, though some of it could also be important as a revenue source. There would seem to be some advantage in providing the Government with a broad-based "tax-handle" which may be used for altering the level of revenue without affecting the allocation of resources. This would add an element of flexibility to the system since every revenue change would not then necessarily involve interference with productive processes.

7.10 An important test of a sound tax structure is that it should be capable of giving higher revenues over time without the need to raise the rates of taxation upwards. Generally, as incomes rise, as production increases and consumption goes up, the same rate of tax would result in higher revenues. However, the aim should be to ensure as high a degree of income elasticity in the tax structure as possible, which means that the percentage increase in revenue should be higher than the percentage increase in national income. If the tax revenues change proportionately with income, the income elasticity of the tax structure would be equal to one. But if an increase of one per cent in income results in a more than one per cent increase in the revenue yield at prevailing rates, the income elasticity is said to be greater than one, meaning that the revenue sources concerned are fairly elastic.

7.11 In an advanced economy, elasticity of tax revenues is largely contributed by income taxation. In India, given the limited role and coverage of direct taxation, one would have to rely on indirect taxation for obtaining a growth in revenues more than proportionate, or at least proportionate, to the increase in national income. If the tax system were made more income elastic than

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*In technical language, the rate of substitution in consumption is made to diverge from the rate of transformation in production.

in the past, there would be less need for raising the rates of tax on individual commodities from time to time. Studies referred to in Chapter 1 have shown the general sales tax and some of the other State indirect taxes to be income elastic, but the excise tax system, which brings in the bulk of revenue, to be clearly income-inelastic. One of the main aims of reform should be to make the indirect tax system as a whole elastic with respect to real income and prices.

FEATURES OF THE PRESENT SYSTEM

7.12 While to start with the revenue motive was dominant in the levy of indirect taxes, the Central Government has in later years also tried to mould the structure of taxation so as to achieve a number of economic and social objectives. Thus, attempts have been made to use indirect taxes to stimulate the flow of resources to priority areas while restricting the growth of industries producing non-essential goods. The device of raising the price of scarce inputs so as to discourage their use has frequently been used to promote the substitution of products which are mainly imported by those which are indigenously available. At times, indirect taxes particularly excise duties have been used for correcting short-term imbalances e.g., by introducing a wedge between supply and demand prices in conditions of shortage to mop up excess profits. These are legitimate and desirable uses of fiscal instrument to serve non-revenue objectives. In actual practice, many weaknesses are noticeable. Sometimes there are instances of tax differentials introduced on different products at different times giving contrary signals to those whom they are meant to influence. The pursuit of a multiplicity of objectives sometimes comes in the way of realising any one of them. A more common failing is that short-term correctives which were quite appropriate at the time when they were introduced have been allowed to continue even after the circumstances leading to their introduction have disappeared. In addition, we are constrained to observe that some features of the tax structure, which could perhaps be explained by the revenue motive, hinder the attainment of the more important objectives. Thus, heavy taxation of raw materials, which falls indiscriminately on consumers of different products, makes it difficult to achieve the desired degree of progression in terms of tax incidence on final products. Levies which fall on capital goods and intermediate products, such as those on different types of machinery, cement and steel, while bringing in revenue, raise the cost of investment and may be said to absorb part of private savings rather than raise the level of savings. Again, differential taxation of raw materials and other inputs, imposed mainly to raise revenue, affects producers' choices in unintended ways and thereby reduces the efficiency of the system.

SALIENT FEATURES OF THE DESIRED TAX STRUCTURE

7.13 One of the basic tasks of indirect tax reform is, therefore, to reconcile the revenue objectives with the objectives of establishing a structure of taxation that would subserve the ends of equity, growth and efficiency. In more concrete terms, we may, in the light of the foregoing discussion, spell out the salient features of the desired tax structure as follows:-

(a) it should ensure an adequate and rising flow of revenue to the Government so that the needed volume of real resources could be transferred to public consumption and public investment without causing inflation;

(b) it should be such as to enable Government to introduce the needed degree of progression with reference to consumer expenditure as between the different expenditure or income groups, without unnecessarily interfering with consumers' choice as between products within the same broad class or groups of goods;

(c) from the long term point of view, it should be such as to direct the flow of resources to priority areas in the private sector in terms of the plan strategy;

(d) it should serve the purpose of raising the rate of savings in the economy by restricting increases in non-essential consumption as national income grows; and

(e) it should promote efficiency and should avoid interference with producers' choices in unintended and undesirable ways.

7.14 In order that the tax structure can subserve the objectives referred to above, it is essential that there should be a harmonisation of at least all the major taxes that fall on different products. We have indicated the ways in which indirect taxes levied by the Centre and the States interact with each other. In discussing lines of reform, we shall have to keep in view the harmful results of this interaction as well as the inherent defects of each tax. We shall start by considering the reform of the excise tax system, which because of its preponderance in terms of revenue and impact, will necessarily form the bulwark of the reformed system. We shall then see how import duties and then sales taxes could be reformed and dovetailed into the excise system. The criteria which we have set forth in this Chapter will form the basic guidelines for reform.

CHAPTER 8

PRINCIPLES OF REFORM OF EXCISES AND CUSTOMS

8.1 We have shown, in Chapter 5, how the major indirect taxes levied by the Centre and the States interact with one another and often produce effects that are neither intended nor desired by any one of the taxing authorities. Also, it is clear that the ultimate incidence on particular final products is arrived at fortuitously and that the possibility of using indirect taxation as an allocative mechanism is thwarted in practice. In considering the lines of rationalisation, therefore, we need to look at the indirect tax system as a whole. In a reformed structure, each tax, while playing a distinctive role, should have a structure that harmoniously blends with others to result in an integrated tax system for the country.

8.2 The three major indirect taxes as at present are excises, import duties and sales taxes. Of these, Union excises, which account for about 44 per cent of the indirect tax revenues can be said to form the bulwark of the indirect tax system in the country. They are the most significant part of the system both in terms of revenue and of impact on the economy. The rationalisation of indirect taxation in the country, therefore, hinges on the reform of the excise tax system into which the other components could be dovetailed.

8.3 The Constitution has assigned to the Centre all the important taxes that have a nation-wide impact and with the potential for being used as instruments for the fulfilment of national objectives and priorities. In the sphere of indirect taxation, import duties and excises, which together can theoretically be extended to cover almost all domestic production and imports, have to be given their distinctive roles and tailored not only to yield sufficient resources but also to produce the desired economic effects.

8.4 If indirect taxation at the Central level is rationalised, then one could consider how the major indirect tax at the State level, viz., the sales tax, could be fitted into the system and an identifiably separate role could be assigned to it. A point we would like to stress here is that each of the three taxes should be looked upon as a building block for the total system.

8.5 We have indicated in Chapter 7 the broad role of indirect taxes in our economy and the basic principles on which they should be levied. We shall now consider how these principles should be applied to excise duties and import levies. These two taxes are to be treated similarly from one point of view, namely, that of raising resources for the Government sector. In so far as they are used as devices for securing revenues, they are to be based on the same set of criteria. But they also have distinctive roles to play; import duties have to serve as protective measures and, more generally, as one of the regulators of foreign trade and exchange; while excises are to be used as regulatory devices in respect of domestic production, thus helping to allocate resources according to social priorities. For fulfilling these non-revenue objectives, different principles have to be applied to excises and import duties.

8.6 From the purely economic point of view, there are considerable advantages in having a single integrated indirect tax system in the country extending from the import and manufacturing stage down to the retail stage, with adequate provisions for the avoidance of cascading. Uniform

or basically similar taxation (for raising revenue) of imports and domestic production of goods and services at all stages, while helping to avoid unintended distortions, gives a wide base bringing in the value of all output. On this basic tax, which would primarily be a revenue raiser, could be superimposed other components such as protective duties in the case of imports and sumptuary or regulatory duties, subsidies or concessions in the case of domestic production. However, political considerations, as in a federation, as well as administrative difficulties have to be taken into account and, in the ultimate analysis, a single integrated indirect tax system might have to be ruled out in favour of two or more taxes to be levied by more than one authority. Nevertheless, the basic principle underlying the system cannot be abandoned; rather an attempt has to be made to ensure that the separate taxes taken together would add up, more or less, to a single integrated tax.

A. EXCISE DUTIES

THE TAX BASE

8.7 The above framework must be kept in mind while considering the lines of reform of the excise tax system. Historically, as we have seen, there has been a gradual widening of the base of excise taxation and more recently a shift towards ad valorem duties. Confining attention to the revenue objective for the time being, we need to consider whether these trends should be pushed further or if there should be a reversal. We have noted earlier that the excise tax system has proved to be inelastic with reference to national income in the past. A narrow base and specific duties have been significant contributory factors to this result. While it cannot be argued that the income-elasticity of excises would always increase proportionately with the extension of the base - the inclusion of goods subject to a relatively low income elasticity of demand would serve to lower the income elasticity of the tax system as a whole - there can be no doubt that because continuous diversification of the production structure takes place in the course of development, the value or volume of output of a narrow range of goods will not grow as fast as total output. A tax system that automatically brings in new goods produced in the country will obviously be more income elastic than one that does not do so.

8.8 This is of course not to argue that all domestic production should necessarily be made subject to tax. For administrative and other reasons most agricultural production is exempt from excises. There may be special social or economic reasons why some industrial goods should be exempted. The need for such exemptions, however, does not weaken the case for a broad-based excise tax system. Exemption of any commodity or group of commodities has the twin effect of favouring the main consumers of the concerned good(s) and promoting the flow of resources into the industries producing them. These effects should be brought about as a result of conscious policy decisions in specific cases, and not be the unintended consequences of the basic structure of the tax system. Since substantial revenues are needed, the average rate of tax on taxable goods cannot be fixed so low as not to result in significant allocative effects. Even with the present wide base, the average nominal rate of excise duty (as of 1976-77) is around 19 per cent of the value of the base if goods falling under tariff item No.68 are included and about 22 per cent if they are excluded. With a narrower base, the required average rate would be correspondingly higher. High rates of tax on a limited number of goods would divert consumption to untaxed items, lead to harmful and/or unintended diversion of resources and introduce inequities in the distribution of the tax burden.

8.9 The argument that the tax on some items brings in only a small amount of revenue and that hence they should be freed of taxation, overlooks the non-revenue consequences of such exclusions when the rates on taxed goods are high.

8.10 An administrative argument against the extension of the tax base is also often adduced. It is that as the coverage is widened and as more units are subjected to excise levies, costs of collection go up. It was on this ground that the Venkatappiah Committee, with its main concern for procedural problems, had recommended the freeing of low revenue yielding items from excises, a view which had been expressed earlier by the Public Accounts Committee. We fully recognize the importance of keeping the costs of collection down. Procedural reforms to this end have already been initiated following the Venkatappiah Committee Report, and we are also making a number of recommendations in this regard. However, our considered view is that it would be better to levy excise duties on as wide a range of products - particularly manufactured products - as possible, making appropriate procedural reforms to minimise costs, than rely on taxing a select range of commodities at rising rates which, as we have shown, would have damaging side effects on the economy and at the same time would not adequately serve the needs of revenue. In fact, for most products, there is a point beyond which raising the rate of tax becomes counter-productive in revenue terms.

8.11 While a product as such may not be exempted, for both social and administrative reasons, there may be a case for exempting small producers. Again, although the Central Government enjoys the constitutional power to levy excises on agricultural products, administrative considerations alone would rule out levies on most of them. Besides such cases, it may be considered desirable to exempt some goods in the nature of necessities which are consumed mostly by the poor. Indeed there is considerable strength in the argument that with a large proportion of the population living in poverty, basic necessities should remain free from taxation. The difficulty in making out a list of goods to be exempted on this ground is that, as a rule, things which are consumed by the poor are also consumed by other income groups.

8.12 As things are, only a few goods such as maida, salt, unprocessed handloom cotton textiles, silk fabrics and readymade garments are fully exempt at the final stage. Food grains and other agricultural products are exempt from excises (but are generally subject to sales tax). In principle, one could agree that under the conditions prevailing in India, in addition to foodgrains, poor man's clothing should also be fully exempt from taxation. The problem in practice would be, as we have indicated above, to identify the type or types of cloth to be exempted and to ensure that the exemption is not largely availed of by the not-so-poor and the well-to-do.

8.13 Thus, while not questioning the case for exemptions for special reasons, we should like to point out that liberal tax concessions in the name of the poor may, in fact, often benefit to a greater extent those for whom the benefits are not intended. In any case, the need for special exemptions cannot be used as an argument against the general principle of widening the tax base.

8.14 The most potent argument against an extended system of excise taxation is that it involves taxation of inputs at successive stages of production as well as of final products. Such "multiple" taxation leads to cascading, unintended distortions in relative factor prices, general escalation of costs and prices and often uncontrolled incidence of taxation on different products. Indeed, almost all countries have, at one time or another, faced this dilemma in the sphere of indirect taxes: on the one hand, for revenue reasons, it became necessary to extend the base of taxation; on the other

hand, extension of taxation on a gross value basis created the familiar problems of cascading and distortions. With the single important exception of U.S.A., which relies largely on income taxation, other major countries, both developed and developing, have retained the extended system of commodity taxation but tried to recast it in a form that would rid it of the harmful effects of input taxation. In India too, the option of going back to a system of selective excises does not exist in reality. Hence, in a sense, the crux of the reform of excise taxation is the fashioning of an extended system with an adequate device for eliminating the harmful effects of input taxation, which constitute one of primary drawbacks of even the existing system.

AD VALOREM LEVIES

8.15 We have urged that the excise tax system should be made much more income elastic than in the past. For this purpose, it would not be enough to have a wide base. If the tax yield is to be made responsive to changes in both real income and prices, it would be necessary also to convert excise duties to an ad valorem basis. In Part I of the Report, we have set forth the pros and cons of specific and ad valorem duties indicating why, in our view, ad valorem duties are to be preferred. Since Government cannot afford to let its share of national income decline as the general price level rises, the real choice is either having ad valorem duties without the need for constant revisions or retaining specific duties and scaling them upwards to compensate for the reduction in relative burdens as prices rise. We would clearly prefer the former as too frequent changes in rates tend to create distortions and irrationalities.

OBJECTIVES OF RATIONALISED DUTY STRUCTURE

8.16 We have argued earlier that indirect taxation in India should have two major components: one that could be broadly neutral and governed mainly by revenue considerations and the other that could be an instrument of economic policy, seeking to influence production and investment in accordance with national priorities, and also, performing a regulatory function to correct short-term imbalances between supply and demand. In practice, the two components would have to be coalesced into one structure in so far as long-term objectives are concerned. However, conceptually the two elements have to be distinguished in order that we may logically derive the characteristics that are appropriate to each one of them. In so far as the revenue objective is concerned, it should be the aim to have a structure of standard rate that would be, as far as possible, neutral in relation to producers' choices, but would, at the same time, enable us to distribute the burden of indirect taxation, among the consumers in different income or expenditure classes, according to the desired scale of progression. In order to achieve progression, it would become necessary to introduce differentiation in the rates of tax on different classes on final products used by consumers through a regulatory excise duty. Such differentiation in itself would, of course, tend to bring about a re-allocation of resources as between industries. That, however, would be in line with social objectives since it is our desire to promote the output of goods consumed by the mass of the people and to discourage the production of goods consumed by the rich. In other words, the departure from neutrality brought about by the progressive scale of duties on final products is a desirable characteristic also from the point of view of allocation of resources. Nevertheless, the concept of neutrality is not to be wholly given up. The basic structure of the system should be such that it does not bring about unintended re-allocation of resources or influence producers' choices in relation to use of inputs, location of industries, etc., in a manner that leads to loss of efficiency and welfare.

8.17 In other words, as we have argued earlier, while taxation in India need not be neutral, it is to be ensured that the measure of interference with consumers' choice between products and producers' choice between inputs and techniques is such as is called for. Where there is no special reason for interference, like products should be taxed in a non-discriminatory fashion. While we must tax consumer goods which are largely consumed by upper income groups at higher rates to ensure progression and to restrict the flow of investment into the production of non-essential goods, it would be desirable to apply the same high rates to the entire range of products in this class unless we are satisfied that there are good social or economic reasons for introducing differentials. If, for example, a product makes a heavy draft on scarce resources, such as capital or foreign exchange or a particular input in short supply, we can single it out for higher levy than other products in the same class, which do not. Conversely, if a product consumed by the relatively better-off has a high employment potential, a lower rate of tax on it might be justified. But in general, products classifiable under a particular category, such as luxuries or comforts, should be all subjected to a single rate though it may be appropriately high. That is to say, while there should be difference in the rates on products falling under different categories, efforts should be made to apply the same rate as far as possible to products falling within a particular category. Such a structure of rates would, while ensuring the needed degree of progression, refrain from undue interference with consumers' choice.

RATE STRUCTURE ON CONSUMER PRODUCTS

8.18 As we have indicated in Part I, we do not consider that there is need for a multitude of rates on various consumer products, such as obtaining today, in order to achieve the objectives we have in view. On the contrary, a plethora of rates make tax administration as well as tax compliance a complicated matter. We have, therefore, argued that the various consumer products should, in course of time, be fitted into four or five (cumulative) rate categories. The simplicity of such a rate structure would in itself be a great merit. At the same time, it should be possible for us to achieve the needed degree of progression with half a dozen rates as effectively as we are able to do with a large number of rates as at present.

8.19 In assigning a particular consumer product to one or the other of rate categories, the primary factors to be kept in mind are the income groups which largely consume that product and the social interest or otherwise in promoting such consumption. Additionally, in some cases the proportion of income of the consuming group, that is likely to be spent on a product would have to be taken into account. Thus, matches are consumed by all sections of society, but because the outlay on them forms a small proportion of the total expenditure of even the poor classes, a high rate of duty has been imposed on them without causing real distress. Again, in regard to durable consumer goods a higher level of duties could be fixed because they are not bought every month or every year, while products consumed by the same income group, which have to be bought frequently, would deserve a lower rate.

8.20 The five rate categories that we have in view would not be adequate to cover all products. We recognise that certain products, such as those in the petroleum and tobacco family and matches, may have to be treated on a different basis. However, the great majority of products that are of interest to the consumer could be fitted into the limited number of rate categories that we have in mind. We discuss more fully about the rates that could be applied to the different classes of products and the manner and phases in which the change can be brought about, in Chapter 9. However,

it is necessary to emphasise that the scale of effective progression depends not on the nominal rates applicable to different products but on the cumulative burden to which they are subjected. That is to say, rates of tax falling on inputs influence the distribution of the burden of taxation on the consumers as much as the rates applicable at the final stage of production. While, in principle, a determinate degree of progression can be achieved by adjusting the nominal rates of duty on final products, after taking into account the burden resulting from input taxation in different cases, so long as no relief is available in respect of input taxation, the scale of progression that is arrived at after considerable research and adjustments of rates, would be disturbed as soon as rates of taxation on inputs are changed. Moreover, as the effective incidence of input taxation varies from product to product, in order to arrive at the same cumulative rate in respect of a number of products, different nominal rates would have to be applied to them. Thus, we might end up with a plethora of nominal rates just in order to compress all products into a limited number of cumulative rate categories. It is for this reason that we have suggested that, in the interim, we might introduce only a limited number of nominal rate categories even though it would mean that cumulative rates on like products would be different. However, in the long run, in order to get rid of the two major disadvantages mentioned above, we would have to adequately deal with the problem of taxation of inputs.

RATE STRUCTURE ON GOODS UNDER ITEM NO. 68

8.21 As of now, all goods falling under the catch-all category of tariff item No. 68 except for those specifically exempt are subjected to a rate of tax of 2 per cent. In the course of rationalisation, it would clearly be necessary to examine whether consumer products that are now taxable only at 2 per cent under the tariff item No. 68 should not be taken out of that list and be fitted into the appropriate rate categories having regard to the nature of the product, the income groups to which it largely caters and other relevant factors. Similarly, as new products are manufactured, they would be initially taxed under item No. 68, if they are not classifiable under any other tariff item. But when the production of these new goods is fairly established, a decision would have to be made, after the necessary examination, as to whether they should be left under tariff item No. 68 or should be taxed at a higher rate. However, there would be considerable advantage in introducing as early as possible a scheme of comprehensive classification under the excise tariff so that in effect tariff item No. 68 could be done away with and each new product would, from the very beginning, be brought under the appropriate rate category. We discuss the question of comprehensive classification in Chapter 15 on Procedural Reforms.

8.22 Later in the report while discussing taxation of capital goods, we recommend that a separate classification be introduced for capital goods presently covered under tariff item No. 68. Once this is done, it would become necessary to examine afresh the appropriate level of the general rate on products falling under tariff item No. 68.

8.23 In the Budget for 1977-78, the rate of general levy applicable to products under tariff item No. 68 was raised from 1 per cent to 2 per cent. Simultaneously, it was proposed that the general levy would be entitled to be set off whenever a commodity subjected to this levy is used for further production of dutiable goods. This provision was introduced to prevent widespread cascading that would otherwise have been caused by a general levy applicable to a wide variety of products. We welcome this provision not only because it is desirable in itself but also because it represents a step towards the extension of the principle of tax credit in respect of input taxation which, as we shall argue below, would have to be generalised sooner or later, if the indirect tax system

is to be put on a rational basis. We would recommend that this provision should be retained in any future step up of the rate for the residuary tariff item.

DIFFERENTIATION IN RATES ON PRODUCTS OF SAME FAMILY

8.24 We have indicated above that certain classes of products cannot be fitted into the general rate structure that we have prescribed. A departure from the general rate structure would also be justified in certain other cases in which products which belong to the same family cater to different income groups. Good examples are: cloth, paper, radio and TV sets. Thus, different varieties of these commodities are subject to tax at present at different rates depending on the specification, trade name, end-use or price. We have found that differentiation on the basis of specifications, trade name or supposed end-use often leads to difficulties and even distortions. For example, because of the sharp difference in rates between packing and wrapping paper on the one hand and certain categories of printing and writing paper on the other, printing paper, we are told, is often used as wrapping paper. And, there are also consequent disputes over classification and assessment. We are of the view that the yardstick of price before tax would be the best one to employ in determining whether particular varieties of a product should be considered as being primarily consumed by the rich or the poor. We have applied this principle to the case of cotton textiles while discussing the rate structure appropriate for the products in the textile family.

8.25 While differentiation in rates between costlier and cheaper varieties would be justifiable in a few cases, such differentiation should be confined to a limited number of cases. If this principle is generalised, we would again end up with a system of plethora of rates with all its disadvantages. We would urge that the general rule to be followed would be that a single rate should be applied to a class of similar products and that, if a clear-cut distinction is to be made between two varieties in the same group sold at two substantially different prices, then it might be preferable to fit them into two different rate categories in the general structure. The exception to the general rule would be where certain intermediate rate categories would arise as a result of differentiation based on price.

TAXATION OF INPUTS

8.26 We have so far considered only the rates of duty on what may broadly be called final products. We have repeatedly emphasised that nominal rates on final products diverge from cumulative rates to varying extent in the case of different products, because of the extended taxation of intermediates. The scale of progression and the impact on the flow of resources depend, of course, on the cumulative rates applied to different products, and hence the rate structure that we have suggested is in terms of cumulative rates. However, within the existing system, any attempt at tailoring the cumulative rates on final products exactly to fit a limited number of rate categories would lead, as indicated above, to a multitude of nominal rates, not unlike what obtains at present. The dilemma is that if, on the other hand, only nominal rates are rationalised, the basic objective of the scheme we are advocating would not be achieved, except in those cases where the divergence between the nominal and effective rates is minimal or negligible. Thus, even the objective of achieving an intended scale of differential incidence on final products cannot be fulfilled, unless we deal adequately with the problem of taxation of inputs.

8.27 The heavy reliance in the past on levies imposed on inputs was due mainly to the administrative convenience and the low cost of collecting duties from the relatively small number of larger producers of intermediate products like steel, aluminium, yarn, and certain basic chemicals, as

compared to imposing and collecting levies on thousands of factories which undertook manufacturing. Another factor that must have been kept in view is that there is less resistance in the community to a tax on raw materials which indirectly affects consumer goods than to a levy which visibly falls on them. A tax on aluminium sheets is more easily accepted than a tax on utensils, for example. However, a closer analysis brings out that taxation of inputs invariably places a greater ultimate burden on the consumer for collecting the same amount of revenues than taxation of final products.

8.28 As has already been demonstrated, the heavy reliance on the taxation of inputs, besides bringing about marked divergences between nominal rates and cumulative rates, has also led to several undesirable effects including cascading and unintended distortions in relative factor prices. Another unfortunate consequence of the taxation of raw materials is that it is extremely difficult to ensure that the incidence on consumer product is according to a progressive scale. It could well be argued, therefore, that now that the excise base has been extended, which means that administrative considerations no longer stand in the way of taxation of final products on a wider scale, the taxation of inputs could be eliminated as one way of getting rid of the distortions that it gives rise to. This would, of course, mean that in the interests of revenue, the nominal levies on final products would have to be correspondingly raised, that is to say, there will be a shift in the burden of taxation from inputs to final products.

8.29 However, such a solution would be open to a number of objections and would, in practice, not be feasible. First of all, no matter how much we widen the excise base, there will be areas which will remain exempt from it. Production outside the manufacturing sector would, in all probability, have to remain largely outside the sphere of excise taxation. Even in the field of manufacturing, there would have to be exemptions to be granted to units below a certain size both for administrative reasons and with a view to helping the small producers. Again, in the case of certain other industries, where the danger of evasion would be serious, if the levy is imposed only at the final product stage, it would be necessary to retain the tax on inputs.

8.30 While there are a number of products, which are exclusively or primarily used as consumer goods, there are several others which are used both as final products and as intermediates. Strictly speaking, from the point of view of taxation, the distinction between final products and inputs has to be based on the nature of use and not on the specification or inherent attribute of the products themselves. This being so, it is in practice difficult to implement a rule to the effect that only "final products" shall be taxed. The reasons for this are given below.

8.31 We have already referred to the fact that several raw materials are used by untaxed sectors. Construction is a good example. Construction activity, which is not subject to tax, makes use of several inputs including steel, asbestos sheets, bricks, tiles and cement. Households too make use of these and similar materials in the course of their own activities in the homes or on the farms. If such inputs are exempt, the flow of consumption services from these activities will also be exempt. Secondly, exemption from taxation of those inputs, which are not basic raw materials but which are in the nature of manufactured components, would lead to difficulties. If components and parts are freed of taxation, replacement consumption, that is, purchases of new components and parts by consumers, will escape taxation. This will mean not only considerable loss of revenue but also discrimination in favour of such consumption. Thirdly, if there is no tax on components, or if there is a wide divergence between the rates on components and on final products,

it would become profitable for the manufacturers to sell and the consumers to buy final products without a number of accessories and components. Thus, if a car battery is not taxable or is taxed at a much lower rate than cars, cars would be sold without batteries which could be purchased and fitted subsequently. In some cases, it would be cheaper for consumers to buy components and assemble them into final products.

8.32 For these reasons, we have to conclude that if we wish to adopt an extended system of taxation of final products, it would not be possible to unconditionally free from taxation goods that are used as inputs or components. The ideal solution to the problem we are discussing would be to make a distinction, for tax purposes, on the basis of the nature of use and not on the basis of category of goods. Whatever is used for further production by manufacturers, who are themselves subject to tax, should be given suitable tax relief, while the same product, if it goes direct to the consumer, will pay tax at the appropriate rate. Under such a system, it would be possible to have an extended taxation of final products with adequate progression. While units of all goods, irrespective of their nature, would bear taxation, since taxes levied on units of goods which are used as inputs would be eligible for a set-off, there would not arise any divergence between nominal and cumulative rates. The twin principles of taxing all units and then relieving from tax those used as inputs serve to make extended taxation effective while avoiding cascading and distortions.

8.33 Since taxation of raw materials and other inputs will have to continue under the extended excise tax system, we need to consider the general principles that should govern such taxation and the relative tax burdens to be imposed on raw materials, intermediates and final products. The present position is that products that may be described as basic raw materials are, as a class, subject to the highest average rate of duty. Studies undertaken by the National Institute of Public Finance and Policy, at our instance, have shown that as of 1975-76, if tobacco and petroleum products as well as the goods then subject to the 1 per cent general levy are left out, the average nominal rate of excise duties (that is, tax collected as a per cent of value of clearance) was 25.3 per cent on basic raw materials, 15.2 per cent on other inputs and 13.5 per cent on final products. There could be no economic justification for this magnitude or direction of differentiation in rates. Even if a general system of tax credits in respect of excise duties paid on all inputs were to be introduced, there would be no case for a higher level of taxes on raw materials; and with only a limited provision for set-off, as obtains today, the much heavier taxation of raw materials is clearly undesirable. One of the steps towards rationalisation of the excise duty structure would be to bring about a reduction in the average rate of taxation on raw materials.

8.34 Any significant reduction in the average rate of tax of raw materials would have to be accompanied by a compensatory upward revision in the rates on final products, as otherwise it would result in a substantial loss of revenue. It has been estimated, on the basis of rates prevaling in 1975-76, that if the average rate on raw materials were to be reduced by 5 percentage points, the nominal rate on consumer products would have to be raised by about 1.8 percentage points in order to prevent a loss in revenue. However, if the consumer products under tariff item No.68 were also to be considered for a higher duty, then the extent of the increase in the average rate on other products would be somewhat less. We have earlier pointed out that a substantial number of final products manufactured in the unorganised sector as well as in the small-scale sector are free from taxation. As a result, the loss in revenue due to any reduction in the average burden on raw materials has to be made up by increasing the rates of tax on final products which are already being taxed.

8.35 In this connection, it is necessary to note that while the average rate of nominal duties on consumer products is around 13.5 per cent, the average cumulative rate of duty is estimated to be nearly 20 per cent (again leaving out tobacco and petroleum products and goods falling under tariff item No.68). Any net reduction in the rate of tax on raw materials would necessarily mean that this cumulative rate would have to be raised further. If, however, tax credit in respect of raw material taxation is introduced and the rates of tax on the concerned final products are correspondingly raised, there would be neither loss in revenue nor an increase in the cumulative rate of tax on those products.* This is because in the latter case the products and activities that are not taxed at the final stage are not freed of taxation through the introduction of the tax credit, whereas a blanket reduction in the rates of duty on raw materials would do so. From this it follows that it would not be feasible or desirable to reduce the rates of tax on raw materials to such a low level as to obviate the need for a system of tax credit. However, in the long run, it would be necessary to effect reductions to bring about a proper relationship between the rates of tax on final products and on raw materials.

8.36 In the light of the above discussion, we may outline the general guidelines for the taxation of inputs:-

(i) Since we have pleaded that the rates of tax on final products should be limited to 4 or 5, and since, as we argue below, it is necessary to introduce a generalised system of tax credit in course of time, it would also be desirable to have only a limited number of rates on raw materials and other inputs.

(ii) Raw materials, which are substitutes for each other, should, as a rule, be taxed at similar rates to ensure the most economic allocation of resources. However, to the extent that the use of a particular raw material needs to be economised on wider considerations, a higher levy on it would be justified. Thus, a policy of differential taxation between aluminium, whose supply we can step up without difficulty, and copper, for which we rely largely on imports (to the extent of 55 - 60 per cent of demand), to encourage the use of aluminium in electrolytic industries would be justified. A policy of encouragement of aluminium in place of copper has in fact been adopted, but due to the various changes made in the duties the present rates of duty on aluminium and copper, we have been told, are such that but for other controls and subsidies, the trend for using aluminium in preference to copper would get reversed. We have mentioned this example to illustrate the importance of the tax structure either remaining neutral or if it does create a bias, ensuring that the bias is in the right direction.

(iii) If a higher rate of duty is considered desirable in respect of a raw material or other input for discouraging its use, it would be desirable to levy a separate differential duty on it which would not be eligible for tax off-set at later stages. This is one of the ways in which the tax system could promote economic use of scarce resources. In such cases, the differential duty should not be looked upon as a revenue yielder but rather as a device for raising the price of the concerned product.

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* But there would be a net gain to the consumer through reduced profit margins and interest charges, and net gain to the economy through elimination of distortions in factor prices.

(iv) At present, there is a wide variation in the rates of duty on individual raw materials ranging from 5 per cent for synthetic rubber to more than 100 per cent for certain synthetic fibres, apart from the raw materials subject to 2 per cent levy under tariff item No. 68. /We have given illustrations of such variations in Chapter 9/. There are also variations in duty between different varieties of raw materials within the same family. Steel products are a good example. One of the first steps towards reform would be to even out these variations keeping in mind the general principles we have outlined earlier.

(v) As regards inputs other than raw materials, at present, the rates of excise duty on them vary from 2 per cent (for those falling under tariff item No. 68) to 55 per cent ad valorem (for tyres for commercial vehicles). In general, those inputs which are capable of being used as final products (e.g., for replacement purposes) should be subject to such rates of duty as may be appropriate for them for finished consumer products, while components which are primarily used as inputs should be subject to the same rate of duty as applicable to the finished products in whose manufacture they are mostly used. In both cases, it would become necessary to provide tax credit in respect of duty paid on such inputs to producers who use them for further manufacture, under procedures such as rule 56-A, even if it necessitates some adjustments in the rate of tax on final products.

(vi) In the taxation of packaging materials, a distinction should be made between those which serve an important function in transport or safety of the product and those which may be used merely for consumer appeal. Another factor which has to be taken into account is the conservation of scarce resources and encouragement of packaging material made out of waste products. The present level of taxation of packaging materials is rather discriminatory and high in certain cases. It is necessary to rationalise the rate structure on packaging materials so that, in general, the excise duty burden on different products within this class is broadly the same, except for the discrimination in favour of packaging made of waste material. As a general principle, packaging material also should be made eligible for tax credit like other inputs. To begin with, we would recommend that wherever the duty on packaging materials adds considerably to the cost of manufactured commodities, which are essential in nature, the provision of tax credit in respect of duty paid on packaging materials should be considered.

8.37 The earlier discussion brings out the reasons why we cannot completely or even substantially eliminate the taxation of inputs. However, we have also been anxious to explain and emphasise all the harmful consequences of widespread input taxation. The point that we would like to stress again is that the way to eliminate the harmful consequences of input taxation is not to do away with such taxation as a general rule but to provide tax credit in respect of such taxation at later stages of manufacture. A generalised system of tax credit enables us to rid the system of cascading and distortions, while at the same time retaining some burden on products not taxed at the final stage. A Value Added Tax (VAT) system at the manufacturer's stage would be the best means of achieving the twin objectives of having an extended tax system and avoiding the distortions that flow from input taxation. As we discuss later, such a tax may take sometime to introduce, if Government

PROBLEM OF CASCADING

decide to do so. In the meantime, it would be necessary to make the fullest use of the existing provisions and procedures to give relief from the cascading effects of input taxation.

8.38 Under excise taxation, there are provisions, such as rule 56-A, set-off of duty, and what are known as Chapter X procedures, which are used to moderate the impact of input taxation or to favour specified end-uses. These provisions are generally available only for giving relief from excise levies on inputs. They are not made applicable to import duties on inputs. Some concessions and exemptions in respect of sales taxes on inputs are granted by State Governments, but they are not uniform and are often made conditional. Besides, total exemption is not generally granted. Our view is that relief from input taxation in respect of units used for further manufacture should be made available, ultimately, under all the three major indirect taxes. We shall discuss the needed reform under import duties in a later section in this Chapter and those under sales taxation in Chapter 13. We shall now deal with the question of extending input tax relief under excise taxation.

8.39 The general approach in extending the existing procedures for input tax relief in respect of excises seems to have been to treat them as concessions which should only be given if a special case could be made out to Government's satisfaction. Thus, relief of excise duties on tyres and tubes and batteries has been made available to passenger cars but not to commercial vehicles because the former were suffering from a severe decline in demand which did not afflict the latter. Similarly, in certain cases the consideration seems to have been that in the absence of such a concession the trend towards vertical integration would be strengthened and units which bought components from ancillary industries would be at a disadvantage against those which made their own components and could conceivably manage to produce them in a way that would not make them into identifiable products for purposes of taxation. Thus, a manufacturer of fans gets relief under rule 56-A from the duty paid on the motor but not in respect of all his inputs.

8.40 We recommend that until a VAT at the manufacturing stage is introduced, much fuller use should be made of the various existing procedures for giving relief from input taxation. In particular, there should be a substantial extension of the application of rule 56-A. The tax credit allowed under this rule should neither be confined to inputs having the same tariff classification as the finished goods - as is generally the case at present - nor be restricted only to raw materials or components, but should cover, wherever economic considerations so warrant, packaging materials and consumable stores also. While raising the rate of general levy on goods falling under tariff item No.68, Government have notified that this levy falling on inputs would be eligible for relief and can be set off against the finished product duty wherever such inputs were used in further manufacture. As indicated earlier, we welcome this step both for the recognition of the problem of cascading and uncontrolled cumulative incidence which it signifies, and as a step towards a generalised system of tax credit.

8.41 While we recognise that some of the other procedures might have to be employed in certain cases, we feel that, having regard to the need for simplicity in administration and for safeguarding revenues, the provisions of rule 56-A should be applied in respect of most of the products. Above all, the proforma credit system under rule 56-A is similar in many respects to the tax credit given under a VAT. The exceptions to this general preference for which rule 56-A procedure need only be in respect of two categories of cases, namely, –

(i) where the end product is either exempted or taxed at a very low rate, the existing Chapter X procedure should provide the necessary relief from the excise duty payable on the inputs in such cases (e.g. raw naptha used in the manufacture of fertilisers, low sulphur heavy stock used for generation of electricity, etc.); and

(ii) the residuary cases where though the taxes on end products are sufficiently high to absorb the input taxes, nevertheless rule 56-A cannot be applied on administrative or practical considerations; in these cases, what is generally known as 'set-off procedure' may have to be applied to relieve the end products of the burden of input taxation.

8.42 In particular, we would recommend that the relief for the general 2 per cent levy on inputs might be provided under provisions of rule 56-A with such modifications as may be necessary. The purpose of relief from taxation of inputs is not necessarily to lower the cumulative tax burden but really to eliminate or minimise cascading, to avoid giving wrong signals to producers and to bring about a general reduction in costs and prices. We would, however, like to make it clear that while procedures for input tax relief should be applied liberally in respect of the standard rates of duty on inputs, the regulatory excise duty that may be specially imposed on some raw materials for promoting their economic use should not be eligible for such tax relief.

8.43 We have indicated in para 8.34 above that a 5 percentage point reduction in the average rate of tax on raw materials (again on the basis of rates prevailing in 1975-76) would be compensated by a 1.8 percentage point rise in the average nominal rate on final products (leaving out tobacco, petroleum products and goods falling under item No.68). However, since the fall in the tax rate on raw materials would mean a reduction in the incidence of input taxation, the real increase in the average cumulative burden on final products will be less than 1.8 percentage point. A rough estimate would be that it might rise from just under 20 per cent to around 21 per cent.

8.44 A substantial increase in the mean cumulative rate on final products cannot be contemplated as that would, in effect, mean increases in the burden on mass consumption goods, which are the bulk revenue earners. If revenues prove elastic in the long run, further downward revisions in raw material taxation could be considered. But the extension of input tax relief under the proforma credit system is not inhibited by revenue considerations, and has to be the main method of solving the problems of cascading and uncontrolled incidence.

8.45 Logically, the steps towards rationalisation that we have considered above should be taken in the following order: first, rationalisation of the duty structure in relation to basic raw materials, keeping in mind the constraint that the resultant reductions in the average rate of tax on raw materials should not appreciably exceed 5 percentage points for the time being; second, rationalisation of the rate structure of final products (excluding certain groups such as petroleum and tobacco products, but including consumer goods now falling under tariff item No.68) in terms of nominal rates of duty ranging from 2 to 35 per cent; third, extension of the application of rule 56-A to the manufacturers of all products (whether final or intermediate or capital goods) in respect of which the difference between the nominal rate and cumulative rate is significant indicating the presence of appreciable cascading; fourth, corresponding adjustments in the nominal rates of duty on the same final products so that they will fall under one or other of the cumulative rate categories we have suggested; and fifth, more or less simultaneous adjustments in the rates of duty on packaging

materials, components and goods that are used both as inputs and final goods for replacement purposes. While this is the logical order of the various steps towards rationalisation, Government may, of course, find it expedient to take these steps in a slightly different chronological order. One guiding principle that may be kept in view in this connection is that the adjustments in final product rates should be made in a limited number of instalments.

TAXATION OF CAPITAL GOODS

8.46 Since the main purpose of taxation is to enable Government to transfer real resources to the Government sector by bringing about a reduction in private demand but without reducing savings and investment, it is a moot question whether capital goods, which represent investment in the economy, should be subjected to taxation. Under the consumption variant of VAT, adopted by the European countries, capital goods are freed of taxation because the taxes initially paid on them are ultimately set off against the taxes payable by the producer. There is a strong body of opinion which would favour capital goods remaining free from excise taxation because raising the cost of capital goods through taxation would go contrary to the objective of promoting savings and investment. Given a certain volume of monetary savings, a tax on capital goods leads to a reduction in the real volume of investment in the short run. It is only in the long run, if at all, that the tax could be passed on to consumers in the form of higher prices. In the meantime, investment gets adversely affected. It is also true that while Government are trying to stimulate investment through concessions in direct taxation such as investment allowances, it would not be logical to raise their cost through indirect taxation. As against this view, it has been argued by others that a levy on capital goods is a legitimate instrument to encourage the use of labour-intensive techniques and that in a country, where a great deal of unemployment exists, a case can be made out for such taxation. An in-between position would be to have higher levies only on such capital goods as will demonstrably displace labour while leaving other capital goods untaxed (or taxing them at low rates). On this reasoning, equipment for mechanical handling to replace manual handling could be taxed relatively heavily but not equipment for making steel. It must be remembered in this context that changes in the cost of capital goods would not lead to appreciable changes in the capital to labour ratio in a number of processes because the elasticity of substitution between the two factors is often not as much as is usually supposed. Where the probability of such substitution exists a somewhat heavier taxation of a capital good could be justified.

8.47 Until recently, plant and machinery with a few exceptions were exempt from excises. However, their cost of production included the duties imposed on their inputs. As at present, in addition to the duties on their inputs, most capital goods are also subject to the 2 per cent general levy. It has been estimated that the cumulative incidence of excise duties in a number of cases of industrial machinery classified under tariff item No.68 varies from about 2.6 per cent to about 5 per cent.

8.48 Taking all the relevant factors into consideration, we are of the view that, in general, capital goods in the nature of plant and machinery should not be subject to excise levy at a cumulative rate higher than 5 per cent. Higher rates should be applied only for identifiable economic reasons. That is to say, while we do not think that under Indian conditions capital goods should be freed of taxation as in most European countries, we would urge that they should be subject to only a fairly low rate of duty in order that distortions may be avoided and the rate of capital formation may not be affected. We have indicated above that the cumulative rate on most machinery items now range from 2.6 to 5 per cent. Pending the introduction of relief for input taxation for

machinery manufacturers, as a rough and ready solution, it would be preferable to leave the nominal rate of duty on these items at 2 per cent.

8.49 We make certain further recommendations regarding some items of machinery, and cement which is a special category by itself, in the following Chapter while discussing rationalisation of the tax structure relating to particular products.

8.50 If the excise system is rationalised along the lines recommended by us, we would have an extended tax system at the manufacturing stage with a widening base which would at the same time be free from the usual defects of multi-stage taxation to the extent that relief from input taxation is provided under procedures, such as rule 56-A. We would have then imparted to the system elasticity as well as a measure of stability. It would not be necessary, as in the past, to resort to changes in the rates of tax on particular products from year to year because ad valorem duties falling on a comprehensive and widening base could be expected to yield revenues which would grow proportionately, or even slightly more than proportionately, with growth in national income and/or increase in prices. If at any time it is desired to divert a still higher percentage of national income to the exchequer, then we would prefer that there should be a small and uniform percentage increase in the rates of tax on all products so that the basic structure of taxation and the relative rates on different products would not be disturbed. Such an across-the-board increase in the tax rates obviously spreads the increased burdens evenly among all the sections, and if substantial relief is provided in respect of input taxation, the increase in the rates of tax on inputs would have no secondary effects on the rates of tax on final products whose relative burdens would remain unaltered. Thus, if the basic rate structure is according to accepted norms of social justice and is consistent with our economic priorities, there should be no serious public opposition to a general increase in rates of a small magnitude.

8.51 We have so far discussed desirable long-term characteristics of the excise tax system primarily from the point of view of raising resources to Government, the basic consideration being that revenue should be raised without causing distortions or unintended allocation of resources or more than the minimum necessary increase in costs and prices. At the same time, the burden of taxation should be progressively distributed. The main method of achieving progression is, of course, to introduce differentiation in the rates applicable to different products. This in itself would serve one of the main long term non-revenue objectives, viz., that of bringing about an allocation of resources in the economy according to national priorities. Thus, our long-term investment priorities can, so to speak, be built into the long-term structure of the excise tax system. However, there are a number of other objectives which need to be considered separately and the means of achieving them, in so far as it is desirable to do so through indirect taxation, would have to be grafted on to the basic long-term structure. We have already referred to a few possibilities in this regard in our earlier discussion. We shall now deal with them in somewhat more detail together with other devices that may also be called for as under:-

NON-REVENUE AND SHORT-TERM OBJECTIVES

(i) One of our terms of reference requires us to consider the role of indirect taxation in promoting the economic use of scarce resources. One of the important ways in which economy in the use of the scarce resources can be promoted is to sufficiently raise its price. We have argued that a substantially heavy taxation could be imposed on certain consumer goods, in the nature of luxury products which absorb

scarce resources. We have suggested that in suitable cases the rate of tax on them could be even higher than the general maximum rate of 40 per cent. Similarly, it would be legitimate to impose a regulatory excise duty on inputs which are scarce and whose use, for some reason or another, Government wish to discourage. Since the purpose of the regulatory excise duty would be precisely to raise the price of the product concerned, the impact of such duty should not be included in calculating the cumulative incidence of taxation on final products in whose manufacture that input is used. Correspondingly, the regulatory excise duty should be made ineligible for input tax relief under rule 56-A, or under VAT which may be introduced in course of time.

(ii) Our recommendation that ultimately the duty structure on most final products should consist 4 or 5 rates that should not be altered from time to time carries with it the implication that the long-term flow of resources in the economy should be guided in the main by the degree of differentiation in those rates. Given the rates, entrepreneurs would try to produce consumer goods of various kinds in such quantities as can be sold at prices inclusive of costs and taxes. Their investment plans could be expected to be tailored to this objective. In this connection, we must refer to the role of investment licensing. In some ways, indirect taxation and investment licensing are substitutes for each other; they both can restrict the flow of investment into particular industries. Hence, licensing and tax policies in relation to a particular industry cannot be pursued independently of each other. If the tax rate is given, then licensing of capacity would have to be adjusted to the quantity that the market would clear at a price inclusive of the tax. If, on the contrary, licensed capacity is a datum, then the tax rate would have to be adjusted to the end that neither excess capacity is created nor is the producer able to reap abnormal profits. The pursuit of independent licensing and tax policies in regard to the same industry, and afortiori substantial changes in tax rates after licensing decisions have been made, lead to wide imbalances between supply and demand necessitating a change in one or other of the two policies. Such situations should be avoided.

(iii) In general, taxation should not be used to achieve minor or trivial objectives. There is considerable advantage in keeping the tax system as simple as possible and having only a limited number of rates. Concessions and exemptions made conditional on the fulfilment of complicated provisions, which are such familiar phenomena in tax system, add unduly to the difficulties of tax administration without yielding commensurate benefits. However, there are certain circumstances in which even temporary tax variations would be called for.

(iv) If there is a scarcity of a particular product, whether it is an input or a final product, its price is likely to rise. In some cases the situation could call for the imposition of price and distribution controls. But obviously these can only be applied in respect of items which have some special significance or importance in the economy. Ineffective measures of control can lead to black marketing or other malpractices. Thus, there have been situations in which processing units, having got scarce raw material at controlled prices, have found it more profitable to re-sell it in the black market instead of processing it as they were expected to do. Further, even if the raw material is utilised for the purpose for which it is

allocated, if there is no control on the price of the finished product, the manufacturer may get a windfall profit. One way to prevent abnormal profits being made in situations of scarcity, therefore, would be a temporary increase in the excise duty. However, when levies are raised on considerations of scarcity there should be readiness to lower them as the supply position improves. The present levies on steel and cement, for example, can be traced back to periods of acute scarcity, but when the supply position improved the fear of loss of revenue stood in the way of a lowering of rates. · Again, while an additional levy can be justified in conditions of scarcity, it must not be so high as to discourage fresh investment which would be necessary to relieve the shortage. It would, therefore, be preferable that the additional levy should be kept distinct from the basic excise duty, and its period of validity should be such that it would automatically be withdrawn when the next budget is presented, unless a decision is taken at that time to continue it for a longer period.

(v) A somewhat similar situation may arise on a much wider front if the Centre is faced with a sudden need to raise additional revenues to meet an unforeseen contingency like a national emergency, whatever its cause. In such a contingency there may be advantage, as we have argued earlier, in making a small surcharge applicable across-the-board to all the items which are subject to excise duties rather than upset the balance in the tax rate structure by making additional levies on a few selected items. In such a situation too, the additional levy should have a time limit on the lines indicated in the preceding paragraph. Of course, if the requirement to raise additional resources is not of a temporary but of a long term character, e.g., to have a larger plan, the additional levies may need to be more or less permanent. In such an eventuality, the basic rates themselves will have to be raised, though again if all the excisable items have been properly classified and fitted into appropriate rate categories, the question for Government's consideration would be what upward revision in the existing rates should be made in respect of each of the categories rather than to make an ad hoc selection of items which could be subjected to higher rates of taxation.

B. - CUSTOMS DUTIES

8.52 A reference has been made in Chapter 3 to previous attempts to rationalise the structure of import duties. In the main, the effort was to classify imported products into capital goods, raw materials, intermediates and consumer goods and to have more or less uniform levies on a rising scale on each of these categories. However, since countervailing duties are levied on almost all imported products, all the variations in excise duties have been brought into the import tariff. In effect, therefore, products in any one category are not being taxed at one rate.

8.53 Import duties have been treated in the past as entirely a class by themselves and their similarity and relation to excise duties seem to have been ignored. As we pointed out at the beginning of this Chapter, in a major sense, the two taxes are to be treated similarly: in so far as they are revenue measures, they should be levied on more or less the same basic principles, because they tend to have the same kind of impact on the cost structure and on the distribution of the burden of taxation among different groups. Import duties have also two important economic functions to

fulfil, namely, to protect domestic industries as decided upon by Government and, wherever necessary, to discourage the expenditure of scarce foreign exchange. If we set aside these functions for a moment and consider the revenue component of the taxation of imports, then it can be seen that in a truly rational system, the same duty structure should be applied to imports as to domestically manufactured products. Not merely that, it is also necessary that the same treatment - input tax relief - should be given to the revenue component of import duties on inputs as to the revenue component of excises on inputs.

8.54 In the absence of quantitative import controls, protection to domestic industries (that need or deserve protection) has to be afforded by the protective component of import duties. If the degree of needed protection is properly assessed, the protective duties may be fixed at such levels that the landed cost of imports plus the duties would be equal to the domestic costs of production of the concerned products. On these base prices of imports would be imposed the revenue component of import duties equivalent to the excise duties, so that imports are placed more or less on par with domestic products. This is the rationale for the countervailing duties on imports. If import control is in existence and is the major means of giving protection and conserving foreign exchange, the picture changes somewhat because it then becomes necessary to coordinate import control policies with the import tariff. But it is important to remember that even under a regime of import controls, the pricing of imports (inclusive of taxes) should be based on rational economic considerations, for, import prices affect domestic costs and the decisions of entrepreneurs as regards lines of investment and techniques of production.

8.55 Under a regime of import controls, if in the interests of conserving foreign exchange, imports of a number of goods are severely restricted and as a result a substantial excess demand is generated at prices equal to the landed costs of imports, it would become necessary to prevent the import licensees or others from making large unearned incomes. One of the ways of doing this is to levy heavy import duties. This method carries the disadvantage that an unduly high degree of protection is automatically given to domestic producers. Therefore, it would be preferable, wherever possible, either to canalise imports through a state agency so that the higher profits accrue to the exchequer or to arrange, particularly in the case of imports, that they go directly to the actual users with appropriate arrangements to ensure that the benefits of the low price is passed on to the ultimate consumers. If one of these latter two methods are adopted, the protective element of the import duties could be kept at the appropriate level so that potential domestic producers would get the right signals.

8.56 A fully rationalised structure of import duties should, therefore, consists of the following elements:

TOWARDS A RATIONALISED STRUCTURE

(a) A levy adequate to give the degree of protection deemed necessary for particular products;

(b) A revenue element, which would generally be the countervailing duty, being equal to the excise duty leviable on the same or similar domestic product; and

(c) A regulatory element, which will be based on such factors as reinforcing import restrictions, preventing excess profits on account of scarcity of products in domestic market, and generally to regulate imports from the angle of conserving foreign exchange.

Although in analytical terms, (a) and (c) are distinct elements, it has to be remembered that the level of duty imposed to conserve foreign exchange may itself, in certain cases, be more than adequate to provide protection to domestic industry. Therefore, it would be desirable not to assess (a) and (c) separately and add them but to allow whichever of the two is the higher to become the effective duty. However, for the purpose of arriving at the base for the countervailing duty - (b) - it would be proper to include only the landed cost of imports (excluding duties) and the national protective element, if that should be lower than the regulatory element.

8.57 The import duty structure, as it obtains today, does not satisfy a consistent set of principles. The tight foreign exchange situation, which prevailed until recently and what was felt to be a compelling need for revenues, have led to a structure and levels of duties that cannot be justified on rational grounds today. To give but one exemple, countervailing duties are generally clamped upon a base that includes an import duty that is far greater than what is needed for protection, and may, in all probability, be equal to the needed protective duty plus the excise on the similar domestic product. It is fair to say that the economic effects of such high duties have been severely ignored in the interests of revenue. One of the results of such high duties is that several high-cost, uneconomic industries have come to be established.

8.58 As pointed out in Chapter 3, very high levels of import duties were introduced in the mid-sixties when the country was facing a serious foreign exchange crisis. Then it was felt that the rupee was overvalued and that, though import controls existed, it was necessary to prevent abnormal profits being reaped by the few import licensees. Until the recent dramatic change in the foreign exchange situation and the simultaneous gradual devaluation of the rupee since 1974, it was still necessary to provide a strong disincentive for imports and to correct for the overvaluation of the rupee. But with a comfortable foreign exchange position and the external value of the rupee now being adjusted from time to time, we may proceed on to the assumption that tariff policy for the present need not be concerned with the proper pricing of foreign exchange; or rather we take it that that matter would be dealt with separately.

8.59 The rates of duty on most products today are much higher than what would be justified on the basis of the principles we have enunciated above. Such high duties were partly justified by the chronically difficult foreign exchange situation prevailing in earlier years. What is more, the duty hikes were looked upon as a source for large increases in revenue needed by the Government. This heavy reliance by Government on high import duties on raw materials, intermediates and even machinery would make it difficult to bring about a sudden shift to lower levels. Therefore, a gradual approach has to be adopted - though to the extent that with our improved foreign exchange position larger imports of a wide variety of goods becomes possible - there may be no loss of revenue when the rates of duty are reduced.

8.60 Imports into India now consist mainly of machinery, raw materials and intermediates. Consumer goods proper form a small proportion of total imports and are generally banned except for certain essential items like foodgrains and vegetable oil which are allowed to be imported in times of scarcity. But even they are not significant from the revenue point of view. In Part I of the Report and later in Chapter 10, we have made certain recommendations regarding import and tariff policy for consumer goods. In what follows, we shall mainly concern ourselves with the import duties on machinery and inputs.

8.61 We have taken the view that the revenue component of any import duties should be determined on the same basis as excise duties on similar products and wherever it is considered necessary to keep the rate of excise duty low, the revenue component of import duty also should be small. In respect of capital goods, we have argued that on economic considerations it is desirable to levy only a low rate of excise duty on them (not exceeding 5 per cent). It follows that the revenue component of import duty on machinery should also not exceed 5 per cent. The main question then is what should be the policies regarding the protective element of import duty and import control. One view is that the import duty should be fixed at a level sufficient to give protection to domestic industry and then their imports should be liberalised. As against this view, it has been argued that import duties cannot by themselves provide adequate protection because of the danger of dumping and also because of the preference of local manufacturers for foreign machinery which is often considered more reliable. According to this latter view, it would be necessary to continue a fairly strict import control policy in order to continue the protection to the domestic industry producing machinery. We feel that it is not possible to adumb-rate a general principle or policy of this kind. Government would have to examine each major case on its merits. For capital goods industries which are well established, it would be preferable to liberalise imports, the protective tariff being retained at a level which is enough to give adequate protection to domestic producers. In respect of industries which have been newly set up and which meet only a part of the country's requirements for those types of machinery, a much greater reliance on import control will have to continue because the general bias in favour of imported machinery can only be overcome over a period of time. Then there are items of machinery which are not likely to be domestically produced in the near future. In such cases, of course, imports would have to be allowed to meet the full requirements of the economy. We would like to emphasise that not only in respect of first category of products but also in respect of the other two, the rate of import duty should be fixed at a level that would be adequate to give protection to domestic manufacturers and not at any higher level. This is important in order that the right sorts of signals are given to potential producers.

CAPITAL GOODS

8.62 Basic raw materials at present pay an import duty of 45 per cent. This is the case even where there is no indigenous production and/or where the indigenous supply is, and would continue to be, negligible. In so far as intermediate and semi-processed materials are concerned, the present rate of duty is 75 per cent which in our view is too high to be justified on any rational economic considerations. The distinction between basic raw materials and semi-processed intermediate products is somewhat artificial. Chemicals used in the drug industry are as much raw materials as mineral ores or metals used in the metal fabrication and machinery industries. However, there is one distinction. While as regards the basic raw materials, a view can be taken that some of them have always to be imported, intermediates and semi-processed goods can be produced in the country by importing, if necessary, the basic raw materials. We feel, therefore, that where indigenous capacity of intermediates and semi-processed goods already exist, or is likely to be set up in the near future, the rate of duty on them, apart from the countervailing levy, should not be much more than what is just adequate for protection, provided the level of imports is sufficient to meet the full requirements of industries using such intermediates and semi-processed goods. This approach should also be followed while fixing the duties on basic raw materials.

RAW MATERIALS AND INTERMEDIATES

8.63 What the level of duties on individual products or categories (machinery, raw materials, semi-processed or intermediate products) should be, will have to be determined on an industry by industry study which might well be entrusted to an organisation like the Bureau of Industrial Costs and Prices to whom the industry as well as the importing agencies might be able to make suitable representations. While indicating the level of import duty, such an organisation could also indicate the level of imports necessary for proper utilisation of capacity of user industries within the country.

8.64 While, in the long run, duties on all products need to be brought down and rationalised along the lines suggested in paras 8.52 to 8.55 of this Chapter, as we have already conceded, the scaling down of duties will have to be both selective and phased. Selection of areas for priority action may be based on the following factors:

(a) Where a reduction in duty will help lowering the prices of the kind of things which, in our discussion in Chapter 9 we have included in the category of basic necessities such as food, clothing, shelter, education, health and transport;

(b) Where reduction in duties while lowering the revenue realisation per unit of import, would, in fact, augment revenues because the volume of imports would go up;

(c) Where the cheapening of certain imported products would have a long term favourable impact on the development process, including the promotion of employment; and

(d) Where the duty on a particular input is unduly high, compared with the levies on competing inputs.

8.65 Import controls, which continue to exist, have been so far the main instrument of protection. It is necessary, in considering changes in duties on any product, to coordinate tariff policy with import control policy. We shall deal with three major types of situations that might exist with regard to different industries:

(a) As regards items in which we are self-sufficient, imports are anyhow not allowed and duties are not really significant from the point of view either of revenue or of protection. However, the level of duties is important from two other angles. First, in respect of these goods occasion often arises to allow some imports because of domestic shortages. If the import duty is so high that the imported product will cost more than the domestic product, the attempt to import more in order to relieve domestic shortage gets frustrated. For this reason import duties have to be reduced on ad hoc basis; but on account of the inevitable delay in making the necessary arrangements, there takes place considerable damage to the economy which could well have been avoided, if the duties had been originally fixed at the right level. Second, while the country may be self-sufficient in respect of a number of products, if our exports continue to grow, the question has to be faced whether additional demand for these products, which is likely to rise with the growth of the economy, should be met partially or wholly out of imports. In other words, it may be advantageous to meet part of the future increases in demand for some of these products through imports, and to divert resources for the production

of other goods in which we have clear competitive advantage in the world market. However, an unduly high level of import duties would bring about increases in domestic capacity regardless of such economic considerations. Thus, on both these grounds, it would be necessary to fix import duty levels on these products so as to equate the landed costs of imports to domestic prices. Since imports of these articles are not normally allowed, there would be no loss of revenue, if duties have to be lowered.

(b) Similarly, in the case of inputs, a substantial proportion of the demand for which is met out of local production and only the relatively small gap between domestic production and demand is met by imports, licensed to actual users, the level of duty as we have earlier indicated, should be such as to keep domestic and import prices at par.

(c) Goods of which a small proportion of demand is met out of local domestic production and the bulk of the rest of the demand is met out of imports that are much cheaper, the proper way of protecting domestic industry would be either to give a subsidy to the domestic producer or to arrange for a pooling of prices. This would ensure that the product would continue to be available at a reasonable price without doing any damage to the domestic producer.

8.66 If our recommendations regarding the line of rationalisation of import duties on inputs are accepted, in course of time, they would, in general, be subjected to a duty which is sufficient to give protection to domestic industry and also to the countervailing duty equivalent to the excise duty on like products. As of now, these inputs are subjected to much higher duties than what would be justified on the basis suggested by us. As a result, import duties on inputs have become a major contributor to cascading and general escalation of costs, besides often producing distortions in relative prices. Even if they are scaled down in course of time, the levels of duties would still be substantial enough to cause harmful effects, if adequate provision is not introduced for giving input tax relief in relation to import duties as we have urged, should be done in relation to excises on inputs. According to present practice, relief is provided (under procedures like those prescribed under rule 56-A of Central Excise Rules) only in respect of excise duties on inputs. In principle, there should be no difficulty in stipulating that import duties on inputs also would become eligible for relief at the stage of further processing. Such relief should obviously be confined to the revenue component of import duties. We understand that such relief is granted in respect of countervailing duties in a limited number of cases.

TREATMENT OF INPUTS

8.67 The difficulties in extending input tax relief in respect of import duties at present are that they are very different from excise duties in most cases and that there would be considerable consequential loss in revenue, if upward revisions in the rates of excise duty on final products are to be avoided. We would, therefore, urge that in the immediate future input tax relief under rule 56-A procedure may be extended to the revenue element of import duties - which may be reckoned to be higher than the countervailing duty element in relation to a limited number of products in whose case cascading and other distortions seem to be particularly severe and harmful.

AUXILIARY DUTIES

8.68 As indicated in Chapter 3, the levy of auxiliary duty in addition to the basic import duty, is a revenue raising measure. As levy of separate duties only complicates the rate structure and there is no justification for the existence of two duties serving the same purpose, we would suggest that auxiliary duties should be merged with the basic customs duties.

COUNTERVAILING DUTIES

8.69 At present countervailing duties are levied on imports at the same rates as excise duties levied on like products, indigenously produced. Their imposition is justified on economic considerations, as they ensure that the domestic industry does not suffer a handicap while competing with imports. The assumption for levying these duties is that the protective duties are just sufficient to effect the cost disadvantage of domestic products and that they equalise the landed cost of the imported products with the ex-factory price of the indigenous producers. If so, a duty corresponding to the excise duty has to be levied on the concerned imports. In actual effect, as import duties are much higher than what would be justified for protection to domestic industry, the further addition of countervailing duties on the prices, inclusive of the customs duties, raises the prices of imported goods to an extent far greater than would be economically justified. In its report on Rationalisation and Simplification of the Tax Structure, the Bhoothalingam Committee had, in fact, suggested the abolition of countervailing duties on most products. We are unable to subscribe to this view as the principle behind their imposition is sound. Instead, we would favour the scaling down of the customs duties to the level necessary to give adequate protection to domestic industry.

8.70 Where the goods imported are not being produced indigenously there would be no justification for a countervailing duty as such. We are told that because the present classification of products in the excise tariff is not sufficiently detailed even these products often attract duties at quite high rates which place on them an unjustifiably high burden. Thus, at present, imports of certain categories of insulat' n paper used in electrical industries and baryta paper used in the manufacture of photographic paper, even though they are not produced indigenously, not only bear a high import duty of 120 per cent of the CIF price, but in addition, are subjected to a countervailing duty at the rate of 30 per cent - the rate which is applicable to the residuary categories of paper in the excise tariff. (Actually, the net impact amounts to 66 per cent of CIF price as the countervailing duty is levied on cum-duty price.) Such anomalies can be fully remedied only if the excise tariff classification is made more comprehensive - an issue which we discuss in Chapter 15. Meanwhile, we would recommend that on imported goods not being produced at homeand not competing with any indigenous products, no countervailing duty should be levied, even if it could be shown by a stretch of argument that they fall under some excise tariff head. Appropriate administrative arrangements should be made for the special treatment of such cases.

8.71 We do not, however, mean to imply that such products should be made completely free of duty. It would be legitimate to subject them to a revenue duty at the appropriate level. Such a level would have to be determined after a careful consideration of the duties likely to be applied to them, if produced at home.

EXPORT DUTIES

8.72 As we have observed in Chapter 3, over the years, export duties have lost their importance from the revenue angle. Exports are encouraged in certain cases, even if it needs subsidisation. However, occasions do arise when there is considerable disparity between the domestic and international prices which may justify driving a

wedge between the two by levying export duties. Whereas such an imposition to mop up a part of the profit of the exporters or intermediaries, as also to ensure that export demand does not unduly raise internal prices, may be justified, care should be taken to ensure that it does not become a damper on exports. A short-term gain in revenue could result in a long term loss of the market. This is more likely to happen if, instead of being considered as a kind of windfall, export duties are relied upon as a stable source of revenue for the budget. We would also recommend that where export duties are imposed to mop us profits of exporters/intermediaries at times of high international prices, there should be readiness to lower such duties when the prices come down, as otherwise it could damage the long-term prospects of our exports. It should not be ignored that when the export of a product becomes profitable, producers try to expand their output which, in the long run, expands the export possibilities. While considering export duties another factor to be borne in mind is that such duties on Indian products might, in some cases, afford a tariff protection to producers in other countries of like products or their synthetic substitutes.

8.73 The changes in the structure and level of import duties suggested by us could bring the import tariff into harmony with the reformed excise tax system. Together, they could constitute a rational basis for the indirect tax system in the country. We would then need to find out the ways in which the indirect taxes at the State level, in particular the sales tax, could be fitted into the basic structure and made to play a supplementary role.

CHAPTER 9

APPROACH TO RATIONALISATION

INTRODUCTION

9.1 Having outlined the principles on which the indirect tax system should be restructured we now proceed to a consideration of the ways in which these principles can be applied to different commodity groups. Not all the factors that need to be taken into account in determining the levies on particular products come within our purview. How much relief can be given to particular income groups having regard to the compelling needs of revenues, what are the dictates of national priorities in the economic field, what difficulties, in terms of costs or demand imbalances, afflict particular industries and other similar issues call for a judgment which Government alone can exercise. What we can do is to attempt an analysis of the tax structure as it affects certain sectors of the economy in the hope that it will be helpful to Government in taking the appropriate decisions.

9.2 Since we could not obviously extend the field of our study to cover the entire range of indigenous production on which indirect taxes impinge, we had necessarily to be selective. We decided to concentrate on inputs which are extensively used by a wide range of industries and on those consumer products which can be said to be articles of mass consumption. In regard to these, we requested the Secretariat to prepare factual studies tracing the evolution over the years of taxes on particular products and also analysing their impact and incidence. Special studies made by the Secretariat in regard to textiles, ferrous metals, non-ferrous metals and plastics are included in the Appendix to the Report.

9.3 We also felt that both because of its key importance to the economy as well as because it happens to be subject to indirect taxation by more than one authority and in more ways than any other industry, a fuller and specialised study of the taxation of road transport was necessary. We entrusted this task to Shri Asit Chandmal whose services in a purely personal capacity and on an honorary basis were made available to us at the Chairman's request by TELCO. Extracts from his study are also included in Appendix 13 to the Report.

9.4 Apart from the studies which we initiated or undertook on our own, we have had the benefit of the views expressed to us by various associations of trade and industry as well as by Government officials concerned with these industries in one way or another. On behalf of trade and industry, we received memoranda from, as well as had discussions with two apex bodies: the Federation of Indian Chambers of Commerce and Industry and the Associated Chambers of Commerce and Industry. Associations and Chambers of Commerce representing particular industries also were given every opportunity to present their views to us. A number of trade union leaders also presented at our request their thoughts on reforms in particular areas of indirect taxation. A list of the non-official bodies who made either a written or an oral presentation is included in Appendix 3A and 3B. The official witnesses whom we invited were specifically requested to express their personal opinion rather than reflect the views of the Department or Ministry to which they belonged. However, we did have in addition communications from many Ministries of the Central Government. While we have taken full account of the useful and helpful comments, criticisms and suggestions which we have received from these diverse sources, we have refrained from quoting or attributing specific suggestions to specific sources as otherwise the Report would have become too bulky and we would also have run into the problem of doing less than justice to the cases made out to us in trying to put them in a condensed summary form.

9.5 The task of rationalising the indirect tax system has to be viewed neither as a revenue raising exercise nor as an occasion for lowering the overall tax burden. We were happy to note that this approach was understood and shared by most of the responsible spokesmen of trade and industry who presented their views to us. Since in this Chapter we have necessarily to comment on a number of anomalies that have crept into the tax structure, which go against the declared objectives of policy or are leading to consequences which were neither desired not desirable, we necessarily have to indicate the areas where the existing rates appear to be on the high side. To the extent tax reductions are effected the revenue loss has to be made up. We indicate some possibilities in the course of our discussion in this Chapter, but, in the next Chapter, we address ourselves directly to the ways in which revenues can be safeguarded and additional revenues mobilised, if necessary, without disturbing the rationale of the restructuring.

TAXATION OF CONSUMER GOODS

9.6 We start our discussion with an examination of the tax structure applicable to consumer goods by which we mean products which are, by and large, used by households for satisfying their own wants. How much burden should be placed on the consumers as a class or the community as a whole through indirect taxation is something on which we take no position. Presently, if account is taken also of the levy on the inputs, which are generally passed on to the consumers through an increase in the cost of the final products, the average cumulative rate of excises on consumer products works out to something like 20 per cent (excluding tobacco and petroleum products as well as goods falling under tariff item No.68). However, the nominal rates on different products vary widely from as low as 5 per cent on vanaspati to as high as 100 per cent on air-conditioners. It follows that cumulative rates would also exhibit such a wide variation. What is more, the total number of rates within this wide amplitude is very large; the difference between the levy on one products and another being in some cases just one per cent or even less. Now, variations in the rates on different products can be justified on many grounds. With a view to ensuring progression, goods consumed by upper income groups can be taxed at substantially higher rates than goods consumed by lower income groups. Secondly, certain products can be taxed at higher rates on economic considerations such as to discourage the consumption of an article which makes a draft on scarce resources or to prevent investment flowing into industries of low priority. But a study of the prevailing rate structure does not indicate that the levies on different products have in fact been determined on such clearly defined criteria. Moreover, as we have already indicated, the marked divergence between nominal and cumulative rates frustrates any attempt to achieve a desired degree of progression through adjustments in nominal rates.

9.7 We are convinced that such a multitude of rates is not desirable either on considerations of progression or on economic and administrative ones. Different rates of tax applicable to similar products or products which are consumed more or less by the same income groups affect consumers' choice between different products. Where there are good economic or social reasons for such interference they can certainly be justified. But it seems to us that in a very large number of cases the differentials in rates are the result more of historical accident arising out of the exigencies of resource mobilisation, than of a deliberate judgment. Apart from the economic distortions which it often causes, the existence of a very wide variety of rates applicable to products variously defined leads to a great deal of administrative complications. One of the most frequent sources of dispute at the time of assessment of duties is the classification of the product because that determines which of the numerous would apply. In our discussion of procedural reforms we draw attention to the problems which arise on this account.

9.8 There is clearly a need for a drastic reduction in the number of rates of excise duty. We have recommended earlier that the aim should be to have, in the long run, 4 or 5 basic rates, such as 10, 20, 30 and 40 per cent. It may be noted that the mean cumulative rate on consumer products, excluding tobacco and petroleum products and also consumer goods falling under tariff item No.68, is at present around 20 per cent. In fixing different consumer products into the appropriate rate categories, the approach could be to examine whether there are reasons to tax a given product at a higher or lower rate than 20 per cent. It may be emphasised that the rates we are advocating are cumulative rates. However, rate fixation could only be in terms of nominal rates. In respect of products where the levies on inputs do not cause a divergence of more than 3 per cent between the nominal rate and cumulative levy of excise the final rate could well be fixed, ignoring the levy on inputs. Where however, the divergence is greater and input duty relief is not being provided under rule 56-A and other similar procedures, the rates of duty on final products could be fixed at appropriately lower levels to narrow the gap between nominal and cumulative rates, by making use of in-between rates of 5, 15, 25 and 35 per cent.

9.9 We hope that our incidence studies, which bring out how taxes on individual products impinge on different expenditure groups, will be of some help to Government in restructuring duties in order to bring about that degree of progression in the tax system which they consider to be desirable. Further, the detailed studies (vide Table appended to Chapter 5) which we have made of the cumulative impact of taxation of inputs on the final products will help in determining the suitable levels of nominal rates for attaining the desired degree of progression in terms of nominal rates.

9.10 In suggesting 40 per cent as a kind of a maximum, it is not our intention that it should serve as a ceiling. There may be reasons to impose higher rates on some products to discourage further investment in their production. There may also be occasions for a temporary higher levy on a product if the demand for it is far in excess of supply which can be made available from domestic production and imports. There may also be identifiable products such as matches on which a higher ad valorem rate can be borne by the community without its proving too burdensome because the amount spent on it is negligible as a proportion of the total consumer expenditure of the rich and the poor alike. What we do wish to emphasise, however, is that when a rate higher than 40 per cent is to be imposed on any product its implications should be carefully considered and recourse to higher rates merely as a revenue measure should be avoided.

9.11 The kind of restructuring we have recommended should not, in our view, lead to any loss in revenue. No doubt rates on certain products may go down. But at the same time there would be opportunity to identify products which are now relatively under-taxed in the sense that the cumulative levy on them is less than the average of 20 per cent and that there is no ostensible social or economic reason why this should be so. We discuss the revenue implications of our recommendations more fully in the next Chapter.

9.12 Having discussed in the abstract the ways in which excise duties on final products should be restructured, we proceed to offer our comments on the taxation of a number of articles of mass consumption.

FOOD ITEMS

9.13 In the list of consumer goods, food occupies the foremost place, being an item of daily necessity. NSS data on consumption expenditure of households (1973-74) a summary of which is given in Table 3 of Appendix 10 show that for the urban households with a per capita expenditure upto Rs. 15 per month, the expenditure on food items amounts to 68.5 per cent of the total and for those with per capita expenditure between Rs. 43 and Rs. 55 and between Rs. 75 and Rs. 100, expenditure on food items constitutes 70 per cent and 63 per cent of the total expenditure, respectively. For 80 per cent of the population, the expenditure on food items alone accounts for about 70 per cent of their total expenditure.

9.14 Foodgrains are not subject to excise levies, though both local and inter-State sales taxes are levied on them in several States. When we look at the rates of sales tax on foodgrains in different States we find that some States have fully exempted the levy, some charge a rate of 2 per cent, and others apply the ceiling rate of 4 per cent for "declared goods" which include foodgrains. Our incidence study shows that these levies on foodgrains are somewhat regressive. Thus, while the burden the indirect taxes on foodgrains is 0.37 per cent for the groups with monthly per capita expenditure from Rs. 15 to Rs. 28, it is only 0.18 per cent for the groups with per capita expenditure of Rs. 100 and above, as against the total incidence for all indirect taxes of 6.31 per cent and 13.19 per cent respectively, for the two expenditure groups. Even where a State exempts foodgrains consumed by its residents from sales taxation it cannot effectively ensure that foodgrains are available tax free to them unless it is self-sufficient in them, since the CST levied by surplus States fall on them. If the deficit State also charges a certain amount of sales tax on revenue considerations the net burden on the consumer is further increased. If relief to the lower income groups is considered to be desirable, powers under the CST Act can be used to lower the tax on inter-State sales of foodgrains. We discuss the role of inter-State sales tax in Chapter 13.

9.15 Next in importance to foodgrains is sugar on which indirect taxes at the product stage are levied only in the form of Central excise duty, because sugar is an item which is subject to an Additional Excise duty in lieu of sales tax. There are, however, State levies on direct inputs used in the manufacture of sugar such as cess or purchase tax on sugarcane. The excise duty on sugar turns out to be somewhat regressive in nature. Among the items which are subject to excise, sugar accounts for the highest proportion of the expenditure of those groups with per capita expenditure less than Rs. 75/- per month. We, therefore, welcome the reductions effected in the rates of duty on levy sugar and non-levy sugar in November, 1977 from 45 per cent and 15 per cent to 27.5 per cent and 12.5 per cent, respectively. Without going into the merits of the dual pricing system, we would add that while the rates on levy sugar may well be kept low, a wide disparity in the rates of tax on levy and free sale sugar can lead to some undesirable consequences, as it is by no means certain that the levy sugar does reach those who are most needy or that, when they get it, the price differential does not encourage them to resell some of it.

9.16 Apart from foodgrains and sugar, one of the main articles in the family of food products, which are of wide-spread interest, are edible oils in their many forms. We have recognised that in Indian conditions there is no escape from some taxation of such articles of mass consumption if revenue needs are to met. While it is for Government to decide the kind of rates to be applied to such products, we would like to urge that if we apply the principle that the consumers' choice between like products should not be unnecessarily interfered with by differential levies on them, there seems to be a case for some adjustments in rates which do not alter the overall tax burden. We find some

anomalies in the taxation of vanaspati and refined oils. The price of vanaspati is controlled and the manufacturers are compelled to use a minimum percentage of inferior oils as their input. Nevertheless, it is taxed at a higher rate than refined oil which is pure and is sold at higher prices. We feel that consideration should be given to applying the same ad valorem rate to both products.

TEXTILES

9.17 The basic objectives in the taxation of textiles have been to ensure progression, to encourage the use of raw materials available in abundance or to discourage the use of those which are scarce; and to provide protection to the decentralised sector from the mill sector. However, it seems to us that the existing levies which were originally inspired by these sound objectives no longer serve the purpose in an efficient and effective manner and in fact lead to some undesirable consequences from the social, economic as well as administrative points of view. In the evolution of taxes on cotton fabrics, man-made fabrics and woollen fabrics, each followed its own logic and a composite, overall view of the tax structure on the textile family as a whole does not seem to have been taken. In Appendix 11 a factual studies made by the Secretariat of the evolution of the tax structure on fabrics made of cotton, man-made fibres and wool have been included, setting out the considerations which led to the changes in each of these sectors.

9.18 Having ad valorem duties increasing with the price is one of the simplest ways of achieving progression. The burden they impose on the product will increase more than proportionately with price and it is reasonably safe to assume that in general lower income groups buy cheaper products rather than expensive ones. However, possibly on the consideration that it would create administrative problems to have ad valorem duties as textile prices were apt to vary from time to time, extensive reliance was placed on specific duties. In order to achieve progression, lower rates of specific duties were levied on cotton fabrics which were judged to be meant for consumption by the poor and higher levies on those which were regarded as fancy fabrics. Such discrimination makes sense in so far as the levies are higher on furnishing fabrics, suiting, corduroys and lower on dhotis and saris. However, at the same time, the view seems to have been taken that the poor prefer coarser fabrics and the rich use fine and superfine fabrics. In this view of the matter, the average count of yarn used was taken into account with the avowed objective of ensuring progression. It had two undesirable consequences. Firstly, it complicated the administration of the tax because laboratory tests had to be made of the average count of yarn used in a fabric in order to determine the levy on it. Secondly, the industry took advantage of the tax structure to produce expensive fancy fabrics which are mainly consumed by the upper income groups, but using counts of yarn which made them taxable at the low rates applicable to coarser fabrics. Meanwhile, as the domestic production of long staple cotton increased as a result of the official policy to encourage its production, fabrics including dhotis and saris came to be classified as medium or fine and got taxed at higher rates.

9.19 The situtation got further complicated as man-made fibres and yarn bagan to cater to the same needs as cotton and cotton yarn did. Very stiff levies were imposed on the former. Partly because they came to be regarded as luxuries and partly for foreign exchange reasons, their domestic production was discouraged and it became necessary to tax them at high rates. Whatever may have been the justification for the high taxation of man-made fibres and yarns in the sixties and early seventies clearly the situation today is very different. Our domestic production of cotton frequently turns out to be less than what is needed by our textile industry as a whole. It has also been

recognised that rather than bringing more land under cotton which would be at the cost of land under oil seeds, we should make greater use of man-made fibres and yarns. Domestic capacity is now on the increase. As regards imports, it is much cheaper from the foreign exchange view point to import man-made fibres and yarns than to import cotton. With the compulsion on the textile mills to use a certain proportion of synthetic fibres and yarns instead of cotton only and in the light of the reference in the latest Industrial Policy Statement of Government to the use of polyester fibre as a raw material for Khadi, it would be safe to presume that the initial policy of discouraging the use of synthetic fibres and yarn stands reversed. As regards the question of progression, there is now a goods deal of material available from various studies to show that lower income groups do make use of synthetic and blended fabrics and would in fact have some preference in their favour, provided their price is low enough. Such lowering of prices of synthetic fabrics is not possible unless the high levies are reduced substantially. In regard to production in the decentralised sector, it is necessary to be clear about the ways in which fiscal levies affect it. What the handloom sector undertakes is weaving. Levies on man-made fibres and yarns tend to fall equally on both handloom and mill sectors and their effect, for various reasons, is at best neutral and sometimes even negative in terms of affecting the competitiveness of handlooms against mills. Further, to the extent that there are higher levies on the products of the mill sector which are considered luxury fabrics, the handloom sector tends to go in for the production of those very same fabrics in respect of which it enjoys greater protection. If it is intended that handloom producers should cater more to the needs of the rural poor, greater reliance must be placed on imposing restrictions on the production of certain types of fabrics by the mills or on having appropriately high rates of levies on them also.

9.20 From this general discussion we proceed to make our suggestions regarding rationalisation and reform in respect of taxation of textiles. We have indicated earlier that the use of the criterion of the coarseness or fineness of the yarn as a basis for differential duties leads to the anomaly that some fancy and expensive fabric, which obviously is meant for consumption by the rich gets taxes at a low rate, while some varieties of dhotis and saris consumed by medium and low income groups get taxed at higher rates. The real test to apply in distinguishing between the cloth consumed by the rich and the poor should be the price factor and on this basis, the cheaper cloth should be taxed at a lower rate. An ad valorem duty will automatically mean a higher levy on the more expensive fabrics which are consumed by upper income groups. If progression is desired, those in the higher price brackets can be taxed at higher ad valorem rates. This should be done on a slab system. If the lowest rate of tax is applied to fabric costing, say, less than Rs.3/- a metre, the next higher rate could apply to as much of the price of the cloth as is in excess of Rs.3/- but below whatever is determined to be the ceiling for the next slab, and so on. Such a gradation, while ensuring greater progression, will also encourage mills to produce lower priced fabrics and at the same time eliminate the dangers of abuse which might arise if the entire value of the fabric gets taxed at a higher rate if its price goes above any specified leval.

9.21 We are happy to note that Government, in the Budget of 1977-78, did introduce changes on the lines recommended by us. But a number of protests came as a result of which Government while conceding that the approach we had recommended was 'logical and reasonable' and 'progressive in nature' made some modifications in the Budget proposals to restore some of the old flavour. This was done on the consideration that "a sudden change in the long standing rate structure .....would create disturbances in the market and might result in increase in the cost of certain varieties of coarse and medium fabrics, while simultaneously bringing about some decrease in the case of cheaper

varieties of fine and superfine cloth". A sudden jolt to the price structure is, of course, to be avoided. However, the fact that some varieties of coarse and medium cloth would get taxed at higher rates while the prices of some varieties of fine and superfine would come down is not something which we had not foreseen. Our main argument has been that the mere fact of the cloth being categorised as coarse or fine is not a good basis for discrimination either on social or economic considerations. The analysis we have made of the incidence of the prevailing tax rates shows that the cumulative levy on grey unbleached dhotis, if they get classified as superfine, is among the highest - 24.9 per cent which is higher than the levy on mercerised dyed printed voile (also of the superfine variety), namely, 23 per cent; and mercerised dyed printed coating of the fine variety, namely, 18.7 per cent.

9.22 Part of this anomaly is attributable to the way in which the yarn is taxed. Duty on the yarn is still specific with the result that on a given count of yarn the rate is the same, whether the yarn is grey, bleached or mercerised, whether it is on cross reel hanks or on cones. This means that the progression which an ad valorem duty brings out is lacking at the yarn stage and instead the rate depends on the count of yarn. Therefore, when it comes to the fabric stage the total levy on the fabric inclusive of the levy on the yarn tends to be less progressive than the nominal rates on the fabric. A switch over to ad valorem duties on cotton yarn would have the added advantage of reducing assessment disputes, laboratory tests and other complications which arise because a difference of even one count can make a material change in the tax liability.

9.23 In fact, we feel that in so far as Government find it necessary to discriminate in levies as between different types of fabric on account of the raw material used in their manufacture, it would be appropriate to introduce the necessary differentials at the yarn or fibre stage. Thereafter, at the fabric stage, the levy can be based on the price only; the counts of yarn as well as the question whether it is natural or synthetic should be ignored. This would eliminate laboratory tests on fabrics; they would be needed if at all only at the yarn stage. Further, the differentials will equally affect the mill sector and the decentralised sector. However, the latter being free from levies at the weaving stage the tax on mill fabrics will provide the requisite protection to the handlooms. About the extent of the discrimination at the fibre/yarn stage and the considerations on which it should be based, trends of Government policy as well as our own assessment of the situtation suggest that, for the reasons outlined earlier, the very wide differential between cotton and yarn of man-made fibre has to be steadily reduced. The revenue loss on the excise front would to no small extent be made up by larger imports at lower foreign exchange cost but with very heavy customs duties on man-made fibres. No doubt, the pace of change has to be staggered so as not to give a sudden jolt to the market. But we see little justification in today's conditions for the average cumulative incidence of excise duty of more than Rs.2/- per metre of man-made fibre textiles, while on cotton cloth it is less than 25 paise. If the average incidence of duty on cellulosic fibre fabric is excluded, the cumulative duty on the synthetic fabrics works out to be even higher.

9.24 In bringing about a reduction in the cumulative levy on fabrics produced of man-made fibres and yarns, we feel that the trend should be towards shifting the levy from the raw materials stage towards the more processed articles. Cellulosic staple fibre being a substitute for cotton which is duty free, the levy on it has to be low because there is a further impost on it at the yarn

stage which makes the cumulative levy on staple fibre fabrics much higher than on comparable cotton fabrics even though the duties on yarn are identical. Similarly, in the case of synthetics, the fibre stage levy should be lower than the yarn stage levy. Overall the attempt should be to shift as much of the burden of the levy as possible to the fabric stage and to fix the tax at the yarn stage at such a leval that its incidence on the fabrics woven in the decentralised sector is just adequate and thus the need to have excise surveillance and control on that sector is obviated.

9.25 The assessment of duty on man-made fibres and yarn and blended yarn entails laboratory tests to determine the denier/count and nature and extent of fibres used. Further, because of specific rates of duty on them, ad valorem incidence of duty varies considerably not only within the same group of yarn such as viscose, polyester and polyamide but some times even in respect of the same yarn and the same denier.* To overcome the cumbersome process of ascertaining denier/count/composition of fibres and to ensure progression and equitable incidence of duty, we recommend replacement of the existing system of excise duty on fibre and yarn by an ad valorem levy.

9.26 Turning now to woollens, an excise duty on woollen yarn was first imposed in 1961 to raise additional revenues and to bring within the excise net hosiery and certain other fabrics which did not bear any duty. The duty on imported raw wool jumped from nil to 45 per cent following release from GATT binding in 1971. Prima facie, both cotton and wool being natural textile fibres, would have warranted similar if not identical treatment. For reasons for which we have been unable to get any satisfactory answer, both in regard to import duty as well as in respect of import licensing, raw wool has been dealt with far more severly than cotton. If we take into account the wide disparities of climatic conditions in the country and take cognizance of the requirements of cooler tracts and of the people living at higher altitudes, woollens should not be ranked much below cotton in importance.

9.27 With the expansion of our export oriented carpet industry its demand for indigenous wool, which is exceedingly well suited for carpet weaving, has steadily gone up over time, resulting in a curtailment of the availability of domestic wool for the production of wearables. With the condition and limitations placed on imports and with a high import duty, not much of the imported wool has bee meeting the needs of lower income groups, as most of it has been used for the production of fashionable suitings for the rich.

9.28 But with the prevailing shortage of indigenous wool and liberalisation of imports, imported wool is being used even for the production of khadi woollens. Unfortunately, with the present level of import duty, despite the liberalisation of imports, the price of imported wool is three times as high as the price of similar indigenous wool from sheep farms which have been established after importing new breeds of sheep from other countries. This is a major impediment to the growth of the woollen industry particularly in the decentralised sector and militates against the production of cheaper woollen fabrics which would cater to the needs of the lower income groups. Given appropriate fiscal policies and organisational effort there is no reason why hand-spun and hand-woven tweeds as well as hand-knitted woollens should not find large overseas markets as handloom cottons have done.

9.29 Against this background, we are unhappy to note that instead of moving in the direction of shifting levies from raw materials and inputs to finished products, only recently, on the ground of

*Cf., Table under para 51 of Appendix 11.

avasion and malpractices in respect of woollen yarn, the duty on combing was reduced and that on spinning was abolished and to compensate for the loss of revenue the customs duty on imported raw wool (greasy wool) was increased from 45 per cent to 75 per cent. Another feature of the present duty structure on the woollen family is that the most highly taxed product of the mill sector is hand-knitting yarn, the cumulative levy on which, including customs and excise but not including sales tax on raw materials, is over 40 per cent. Considering that hand-knitting yarn has a potential of becoming a major source of employment both for domestic and export purposes, this levy seems to be much too high on any criterion.

9.30 We would, therefore, favour a rationalisation of duties on woollens on the lines we have already recommended for textiles. The duty incidence should be shifted forward and to start with the customs duty on raw wool should be substantially lowered. The duty on the final product should be graded in a manner which will weigh more heavily on the more expensive fabrics than on the cheaper ones. Finally, in the woollen family too, polyester and acrylic fibres function as substitutes of natural wool and are often blended with it. The high levies on the former create the same kind of distortions and undesirable repercussions as we have referred to in the case of blended fabrics of cotton and man-made fibre.

PAPER

9.31 We have selected paper for inclusion in this Chapter because it meets many consumer needs in the field of education and culture and also serves as an input in the shape of packaging materials etc. Excise duties at varying rates are levied at present on different varieties of paper and paper boards ranging from 5.5 per cent for a certain category of white printing paper to 30 per cent for most varieties of packaging papers and paper boards. The rates are different for the organised and small-scale paper mills. Concessions also exist for certain categories of paper boards. Appendix 12 gives the existing rate structure of excise and customs duties in regard to different categories of paper. The suggestions we have for restructuring the duties in the light of our analysis and of representations made to use are set out below.

9.32 In the case of printing and writing paper, a reduced duty of 5.5 per cent is applicable, if it is of prescribed grammage and tint. Its production is statutorily regulated, its price is informally controlled and it is being supplied (under an informal distribution scheme operated by the Ministry of Education) for use by the student class in the form of exercise books, text-books, etc. No one has questioned the justification for the lowest rate of duty being applied to this variety of paper. The present odd rate could, however, be rounded off to 5 per cent ad valorem.

9.33 As for the other varieties of printing and writing paper, we find that some of them get taxed at 15 per cent ad valorem based upon trade name and specifications, while the rest are charged to a duty of 25 per cent. Differentials in duty incidence based upon specifications and trade name add to administrative complications and throw open possibilities of abuse. It is difficult to distinguish and classify different varieties of paper by their trade name merely by visual examination. The grammage criterion needs frequent laboratory tests and becomes the subject matter of disputes as it varies with moisture content, etc. Moreover, such a differential rate structure tends to distort the pattern of production in different units inter se. The larger and more efficient units can easily increase their production of the low-taxed varieties while smaller paper mills may lack such flexibility. The wide tax difference can also adversely affect the production of varieties of paper taxed at relatively higher rates whose production may be otherwise desirable. It would be more rational for all printing and writing paper (other than varieties subject to an informal price and distribution control) to be taxed at a uniform rate.

9.34 As packaging varieties of paper are taxed at 30 per cent, we understand that printing and writing varieties are being diverted for packaging and industrial uses. The present differential in duties on packaging and printing varieties also leads to classification disputes as certain varieties claimed to be printing paper (such as for printing posters) are treated as packaging paper by the excise authorities. A reconsideration of the duty differential between packaging and printing paper appears to be called for. In short, serious consideration should be given to the possibility of having a uniform rate for all printing , writing and other varieties of paper (including packaging papers) except for those varieties which are under informal price or distribution control.

9.35 The concessional treatment accorded at present when unconventional raw materials are used for the manufacture of paper, is well conceived as it helps to relieve the pressure of demand on bamboo and other forms of wood pulp whose availability is limited. On the same consideration, there is a strong case for a lower duty on mill boards and straw boards vis-a-vis other paper boards, as the former are produced from waste paper, cereal straws and other agricultural residues thereby saving good quality pulp, which could be used for the production of superior varieties of paper and paper boards. Such a relief may also help the decentralised sector producing these varieties to grow.

9.36 The interests representing smaller paper mills have argued before us that the existing relief to them is inadequate and further that it should be extended to paper boards and certain categories of paper which are not covered at present. We feel that certain changes in the excise concession to them may will be justified. The case for relief to smaller paper mills may not completely fit in with the general scheme of concessions recommended by us for all small scale units, as their value of clearances will normally be much higher than Rs. 15 lakhs which is the limit recommended by us for determining eligibility, but there is no reason why the principle cannot be extended to them by fixing appropriately higher value limits. The capacity criterion for granting concession to smaller units is likely to create disputes between the administration and the assessee and the existing differential benefits for mills with different capacities would come in the way of growth and expansion of smaller paper mills. It would be more scientific and rational to link the concession with the value of production than base it on capacity considerations.

9.37 The present criterion of relief, introduced in the 1977-78 Budget, debars any concession in so far as paper boards or certain varieties of paper are concerned, even if they are produced in smaller paper mills. Unless it is Government's intention to discourage their production in smaller units, there seems to be no strong reason for the denial to them of the benefit of concessional duty on certain varieties of paper and all varieties of paper boards.

9.38 It has been represented to us that for certain industrial varieties of paper, some of which are at present not even produced in the country (like insulation paper), there is a case for import duty reduction. The application of rates of import duty - as high as 186 per cent - to electrical insulation paper or condensor paper or baryta paper, of which there is said to be no indigenous production does not seem to be the result of a conscious decision. A substantial part of the duty (66 per cent ad valorem) is accounted for by the countervailing duty which is attracted because these varieties of paper are covered by the residuary item 17(2) of the excise tariff even though they are not being produced indigenously. If excise tariff is made comprehensive and no countervailing duty as such is levied on products which are not produced indigenously, as recommended by us earlier, it would give considerable relief in duty to the varieties of imported paper under reference. Apart from this, we consider that there is also a case for lowering the present rate of customs duty of 100 per cent on these varieties since they are used as inputs and are not consumer products, and further since no consideration of extending protection is involved.

DRUGS AND MEDICINES

9.39 Drugs and medicines have an important role in maintaining the health of the community. What kind of a tax burden drugs and medicines as a class should bear is a matter which calls for a balancing of social and revenue considerations. The per capita expenditure on drugs and pharmaceuticals in the country is about Rs.10/- per year and only about 20 per cent of the population use modern drugs. Studies of the amounts spent on drugs by different expenditure groups do not indicate that the outlays are a very significant percentage of the total expenditure. However, statistics based on averages have in this case to be used with caution. An individual or a family may have no expenditure at all on medicines for months and even years and then run into a phase when the cost of medical treatment in which medicines are an important ingredient compels the family to become indebted.

9.40 The rates of excise duties on different medicinal products seem to have been kept rather low on a number of considerations. First of all, there was, till recently, a policy of not taxing all products of indigenous systems of medicine as well as homeoepathic medicines on the consideration that they are economic and meet the needs of a class of people who do not have access to or cannot afford what is known as modern or allopathic medicines. (These medicines are, however, now made liable to the general 2 per cent levy if manufactured in large establishments with turnover exceeding Rs.30 lakhs per annum). We have no comment on the preferential treatment accorded to such medicines. But, within the range of what are known as allopathic medicines, there are further sub-divisions. Some selected patent or proprietary medicines, generally known as life-saving drugs, are taxed at a specially low rate of 2.5 per cent. This is sound in principle but we feel that the medicines included in this category are too few. Some medicines have been recently added to the list of medicines qualifying for this special rate. However, several new medicines which come into the market might deserve similar treatment. Hence, the list of medicines in the nature of life saving, drugs needs more frequent review and suitable expansion.

9.41 For other medicines there are two rates depending on whether they are considered to be patent and proprietary or not. The difference is 10.5 per centage points between the rates for medicines marketed under a generic name (taxed at 2 per cent) and those which are considered to be patent and proprietary (taxed at 12.5 per cent). In making this distinction, Government's intention appears to have been to popularise products known by their generic names rather than those sold under some fancy brand names which might make the consumer believe that what he is buying is something special and, therefore, deserving of a high price. This is the basis on which brand names of products, which should have and do have a generic name, deserve to be discouraged. However, many of the products sold either in the patent category or proprietary category consist of formulations which are particular mixtures of a number of ingredients and have thus to be given a name under which they are advertised.

9.42 It has also to be remembered that the general trend now is for doctors to prescribe a formulation which is readily available and can be bought without any special dispensation in a Chemist's shop. People who cannot afford to go to a doctor also buy such medicines from shops if they can be sold without prescriptions. Moreover, even in areas where no medical aid is available people do have access to products of this nature. Besides, the concept of proprietary drugs has in practice been carried too far in the sense that anything such as a symbol which is intended to show that the product has been manufactured by a certain firm is deemed to make the drug a proprietary one even though it is being marketed under its generic name. On the other hand, it is not so deemed if the manufacturer's name itself is spelt out on the packaging. The effect of this distinction is that only a literate person can learn who the maker of a particular drug or medicine is. To the

extent that the manufacturer's name gives proof about the purity and reliability of a drug, those who are not educated will get denied the opportunity of ascertaining whether the drug is reliable or not.

9.43 While we recognise that a higher rate of duty on what are properly to be regarded as patent and proprietary medicines could cause a beneficial shift towards the production of medicines sold under a generic name, we are inclined to the view that the existing difference in rates, for reasons mentionedd earlier, should be narrowed down.

9.44 A worse kind of discrimination comes from the fact that some of the most important drugs in the pharmacoepia get taxed at very high rates merely because in their manufacture either alcohol or another wide family of drugs known as narcotics has been used in however small quantities. Thus, pethedine which is used to relieve pain in very serious ailments like cancer is taxed at the rate of 20 per cent. The levy on common cough mixtures is also very high because they all contain a trace of codeine. The duties on medicinal and toilet preparations containing alcohol or narcotics were raised in 1976-77 on the plea made by the State Governments that because of the low rates many preparations ostensibly called medicines were actually being used as intoxicants. In the process, even essential drugs got taxed at very high rates. We would recommend that a panel of qualified experts should be set up which should suggest (i) a list of drugs covered by the Medicinal and Toilet Preparations Act, which cannot possibly be used for non-medicinal purposes so that they could be excluded from the scope of the high levies; and (ii) a list of drugs which inspite of the possible risk of diversion may merit taxation at lower rate: because they are needed for treatment in critical ailments.

9.45 Another disturbing feature of the taxation of drugs is that while the nominal rates of excise duty on drugs have been kept low, the heavy taxation of imported inputs (drug inermediates or bulk drugs) in fact raises the cumulative levy on them to very high levels as Table 1 below shows:

TABLE 1

IMPACT OF DUTIES ON IMPORTED INPUTS ON PRICES OF DRUGS AND MEDICINES

Sl. No.	Product	Nominal excise duty on the finished product (as percentage of ex-factory price)	Imported duty paid on input (as percentage of ex-factory price)
(1)	(2)	(3)	(4)
A	BULK DRUGS USING IMPORTED INTERMEDIATES		
1.	Insulin (anti-diabetic)	2	21.1
2.	Chloroquin-phosphate (anti-malarial)	2	37.2

Sl. No.	Product	Nominal excise duty on the finished product (as percentage of ex-factory price)	Imported duty paid on input (as percentage of ex-factory price)
(1)	(2)	(3)	(4)
3.	Iodo-chloro-hydroxy quinoline (anti-dysentric)	2	39.9
4.	Pyrazinamide (anti-T.B.)	2	34.4
B	FORMULATIONS USING IMPORTED RAW MATERIALS		
5.	Dexamethasone tablets	12.5	29.8
6.	Ethambutol tablets	12.5	15.6
7.	Triflupromazine tablets	12.5	40.9
8.	Doxycycline capsules	12.5	31.2
9.	Gentamycin injections	12.5	33.2
10.	Hydroxy urea capsules	12.5	38.0

(Note : The figures under column (4) have been worked out by studying certain sample products in the field)

SOURCE: Bureau of Industrial Costs and Prices.

9.46 Another feature worth noting is that there are certain drugs which are treated as life-saving for excise purposes which have to use imported bulk drugs subject to a customs duty of 75 per cent. The price of these drugs at the retail stage goes up substantially due to the heavy import duty component. Thus, import duty paid on bulk drugs used in the manufacture of chloroquin diphosphate tablets itself works out to about 39.7 per cent of the ex-factory price of the latter while in the case of another life-saving drug, viz., chloramphenicol capsules the import duty component accounts for about 21 per cent of the selling price.

9.47 We recognise that import duties on bulk drugs as well as intermediates have to play a protective role as well. Therefore, in considering any adjustments in order to reduce the cumulative levies which are judged to be too high, it would have to be ensured that domestic production of like products if it exists is not hurt. In some cases even at present a price pooling arrangement with regulation of volume of imports is used. Such an arrangement is helpful to the consumer without hurting the producer. Where there is no domestic production, the import duty could well be lowered to a level which is deemed adequate for affording protection to new investment.

9.48 Having discussed food, clothing and some of the products needed for educational and health purposes, we now turn to the road transport industry. It serves a basic personal need of the million of people who make use of bus services for going to and coming from their places of work. It also forms a part of the infrastructure. The cost of transportation affects the prices of all products and as our incidence studies show, even the levy on truck tyres has a perceptible impact on the lowest expenditure groups. In fact, the road transport system happens to be one of the most heavily taxed sectors of the economy. A multitude of taxes imposed both by the Centre and the States affect its main capital goods, namely, trucks and buses, as well as products consumed in its operation. Road transport also gets taxed as a service over and above the taxes paid on the products needed for its operation. The Study Group on Motor Vehicles Taxation (1965) and the Keskar Committee (1967) had both come to the conclusion that the level of taxation on this industry was too high but no significant relief was given, apparently on considerations of revenue. We felt that since we were looking at the role of indirect taxation and the revenues it generates in its entirety, it would not be inappropriate for us to make a fresh study of the situtation. Accordingly, we commissioned a special study on the taxation of the road transport industry. Extracts from this report are set out in Appendix 13.

TRANSPORT

9.49 From the above study as well as the incidence study, the following noteworthy features emerge :

i) The indirect taxation of road transport has a perceptible impact even on the lowest expenditure groups as it raises the cost of every necessity.

ii) The pervasive and multi-stage taxation on manufacture and sales of trucks and buses results in a cumulative levy (including taxes on inputs of inputs) amounting to 58.9 per cent of tax-exclusive-price and 44.6 per cent of the ex-factory price.

iii) The system of taxation results in the locking up of extra working capital (due to the tax element in the value of inventories) which adds to vehicle costs without any gain in tax revenue and locks up scarce capital unproductively.

iv) Trucks and buses meant for mass transport are taxed higher than vehicles meant for personalised transport such as cars and scooters.

v) Taxes that affect the cost of operation of vehicles, such as Central excise duties on fuel, spares and lubricants and the various State and Municipal levies such as motor vehicles tax, tax on passengers and goods and octroi increase operating costs by about 50 per cent for trucks. In regard to buses, taxes represent 45 per cent of the operation cost (excluding taxes) per passenger km. These taxes though initially borne by the transport operators is ultimately passed on to the consumers.

vi) There is a considerable divergence between States in the tax rates on goods and passengers.

9.50 A strong case would thus seem to exist both on social and economic considerations for a reduction in the total burden of the various levies so as to reduce the cost of road transport. Unfortunately, the reliance on revenues from the taxation of the road transport industry is so great that it would not be too easy to compensate for the loss of revenue due to any reduction which may be made by getting higher taxes elsewhere. An equally important point to consider would be how it can be ensured that the benefit of any reduction which is made is passed on to the ultimate consumer and not retained by the road transport industry which by and large over the years has not been an unprofitable one.

9.51 Nevertheless, we feel that at least some move should be initiated to relieve the economy of the burden which the heavy taxation of the road transport industry imposes. Since both the Centre and the States take part in this taxation, progress can only be achieved by a concerted plan of action. Otherwise concessions given by one may well get offset by independent action taken by the other. At the outset, it would be worthwhile thrashing the problem out at a meeting of representatives of Ministries and Departments dealing with transport and finance at the Centre and the States. Without attempting in any way to prejudge the conclusions of such a discussion we would make the following suggestions :

(a) Since the States at present depend on revenues from the road transport industry more than the Centre, as a first step, the States need not be called upon to make any sizeable sacrifices. A measure of uniformity in rates of taxation among the States along with an understanding that no further increases in the rates will be made for, say, 10 years, may pave the way for other constructive decisions. One of them must be the pursuit of policies which will enable more vehicles to ply and thus ensure greater competition than seems to exist in this industry. It is only through really keen competition that any concessions which are made in respect of taxation would benefit the ultimate consumer.

(b) Against such a background the Centre could start considering which of its levies it can lower. Although operational costs are the more important we suggest that to start with the capital cost of vehicles should be brought down by giving reliefs from input taxation - these reliefs are available now only for passenger cars. If the capital cost of vehicles goes down, municipal bodies will be in a better position to augment their urban bus fleet. Small operators who have to borrow from banks for their capital needs will find it easier to expand their operations. The loss in revenue will be more than made up by the contribution which every vehicle makes in the course of its working to State and Central revenues year after year. It should also be noted that each commercial vehicle on the road provides employment to about 7 people.

(c) In regard to operational costs, the most important element is the price of diesel, the taxation of which forms part of the complex tax structure which has been specially evolved for the petroleum family. We offer some observations on the subject later. Other items which affect operational costs include lubricating oil subject to excise at 20 per cent, tyres and tubes at 55 per cent and batteries at 17.5 per cent. Apart from the effect which these levies have on the operational cost of the road transport system, it may also be pointed out that the tax on tyres and tubes may come in the way of their timely replacement with the risk of accidents. It is estimated that the replacement value of tyres for every commercial vehicle is over Rs.25,000/- per annum, of which the tax accounts for over Rs.8,000/-.

9.52 There is at present a plethora of taxes and fees that are levied by State Governments and local bodies which have a dampening effect on the operations of the industry. Even traffic passing through enclaves in other States and/or through intervening or corridor States is subject to road tax. The practices followed under the Motor Vehicles Act (A Central enactment) also varies from State to State. There are terminal taxes like octroi which have the effect of slowing down the movement of traffic. Undoubtedly, there is need for rationalisation of these taxes and bringing about some uniformity. We would recommend that in the meeting of the transport and finance representatives of the Centre and the States which we have proposed the question of setting up a National body should be considered which would look into the problems of the industry and the public in general arising out of the diversetreatment meted out by different States in the matter of taxation and regulation of passenger and goods transport by road.

9.53 Our suggestions in the preceding paragraphs should be regarded as a starting point and as a plea for the reversal of the past trend rather than as the long term answer.

THE PETROLEUM FAMILY

9.54 At this point, it would be convenient to discuss the taxation of the petroleum family whose price has an all pervasive impact on the key sectors of the economy - not only transport but also on both industry and agriculture; because the products of this family constitute an important source of energy. Following the hike in crude oil prices Government took a series of measures which in fact raised the prices of petroleum products even more than what could be attributed to the higher costs of imported crude. The anxiety at that time was to ensure that the outflow of foreign exchange on account of crude imports did not shoot up. This consideration necessitated curbs on domestic demand. One way to achieve it would have been to go in for widespread rationing which was rejected as an irksome arrangement opening the door for a lot of malpractices. It was, therefore, decided to use the price mechanism to restrain demand. Accordingly, ex-refinery price of petroleum products were stepped up and so were the excise and customs duties applying to these products. The measures then taken were clearly necessary in the circumstances then prevailing. The question whether the time has come when with the improved foreign exchange position prices of petroleum products should be lowered is one which we feel merits Government's consideration.

9.55 The views expressed to us on the subject have drawn attention to many undesirable side effects of the present price structure. The high cost of road transport - which we just discussed - has an adverse impact on the cost/price structure of the basic needs of the community. It also has a particularly unfavourable effect on those parts of the country which are really backward and in which no railway facilities are available or can be made available in the foreseeable future. We have also heard representations about the high price of petroleum and the point has been made that purely from the revenue angle if the duty was lower higher consumption would make up for any loss. As a source of fuel and energy kerosene is extensively used by relatively lower income groups. The use of furnace oil in some parts of the country and for some purposes would be more economic than other fuels. Diesel as a source of energy is widely used for agricultural purposes and still continues to have its application for power generation. The specially sharp increase in the price of lubricants is leading to reduced consumption in an area where the damage to expensive machinery because of inadequacy of lubrication results in a serious loss to the nation.

9.56 All these are weighty considerations. In so far as we are in a position to form any judgment, we do feel that in the altered conditions a reconsideration of the overall policy seems to be called for.

One factor which Government will doubtless take into account in any re-examination of the matter is that, with the limited world supplies of crude oil, if ever a situation arises in which there is some kind of a global rationing of crude, the fact that India has kept the level of consumption down much more than other countries may well affect India's quota adversely.

9.57 If for the reasons we have referred to above Government feel that the time has come for a lowering of the prices of petroleum products as a class we feel that revenue considerations should not be allowed to stand in the way. The increased levies were not intended to bring in more revenues nor had they been applied on the consideration that these products are better suited for mobilising additional revenues than others. Furthermore, since the object of any reduction would be to encourage higher consumption - and in this instance there is every reason to believe that lowering of prices will lead to increased consumption - even the revenue loss may be much lower than what the change in rates might suggest. As the change in prices has been brought about not merely through an increase in the levels of indirect taxation but also by a revision of prices, in any reconsideration a composite view will have to be taken of the price structure and the tax structure. If in Government's view the time has not yet come for a general revision of the kind suggested above, we would hope that a fresh look will be given to the prices and taxes applying to individual products and relief in respect of individual items will not be ruled out.

TAXATION OF INPUTS

9.58 Throughout our discussion of the taxation of final consumer products, we have had occasion to point out the way in which the widespread taxation of inputs creates distortions. We have shown, in regard to certain items of common consumption how the heavy taxation of particular inputs creates problems; e.g., the tax on fibre and yarn in the case of textiles, the levy on components and metals in the case of trucks and buses and the levy on chemical intermediates in the case of drugs and medicines. We now turn to the taxation of those inputs which are needed in the production of a very wide range of products of different degrees of importance and varying interest to different income groups. In the broadest sense, inputs include basic raw materials and semi-processed and fully manufactured components which are embodied in the finished product as well as materials and services consumed in the process of production such as fuel, power and transport and those required to deliver the finished product to the final consumer such as packaging material. In our earlier discussion we have pointed out the major shortcomings of relying unduly on the taxation of inputs: namely its usually regressive nature, the distortions in relative factor prices, the cascading effects and the divergence between the carefully determined nominal rates and the fortuitously arrived at cumulative rates. We have pointed out in Chapter 8 that the solution of making drastic reductions in duties on inputs and transferring them to the final products, attractive though it seems, in theory, would mean a sizeable loss of revenue because the taxation of inputs does serve the function of taxing products which are themselves not within the excise network. Our objective at this stage in proposing rationalisation of rates on inputs is to ensure firstly, that the rates are reasonable in the sense that they do not impose too heavy a burden on the non-taxed or decentralised sector; secondly, that in so far as they fall on the taxed sector procedures are made applicable to avoid cascading effects, the loss of revenue due to relief at intermediate stages being made up by fixing appropriate rates for the final products; and thirdly, to see that discriminatory tax rates do not lead to uneconomic use of resources by creating an unnecessary bias in favour or against any particular raw material.

9.59 The prevailing rates of tax applicable to the principal basic raw materials are set out in Table 2 below:

TABLE 2 :- RATES OF EXCISE AND CUSTOMS DUTIES ON CERTAIN BASIC RAW MATERIALS

Sl. No.	Description of basic raw material	Average incidence of excise on indigenous production.	Incidence on imported material			REMARKS
			Basic	Auxiliary	Total (estimated) including countervailing duty.	
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1.	Aluminium ingots:					
	Levy Non-levy	80% * 50%	40%	5%	139%	
2.	Copper ingots/ wire bars	30.8%	40%	5%	92.8%**	
3.	Zinc ingots	31.3%	40%	5%	93.4%**	
4.	Lead unwrought	7%	40%	5%	53.9%**	
5.	Iron and steel products - other than alloy and special steels	25%***	30%	5%	69%***	
—	Alloy and special steels.	7%	35%	5%	50%***	
6.	Plastic resins	40%	30% to 100%	5% to 20%	88% to 208%	
7.	Synthetic fibre -					
—	Polyester fibre.	115%	140%	20%	520%****	
—	Rayon fibre	17.5%	-	-	17.5%****	
8.	Wool	-	60%	15%	75%	

See asterisks indications on next page

* For levy aluminium ultimately consumed by State Electricity Boards, the incidence is about 33% (net or subsidy).. Countervailing duty impact is based on average international price in December, 1977.

** The incidence of excise (as well as countervailing duty effect) has been worked out on the basis of MMTC price for the quarter ending December, 1977 (for working exfactory excise incidence, MMTC price has been reduced by excise duty element).

*** Based on 1975-76 data but excluding the production of mini steel plants and ... ... rerollers. The impact of countervailing duty has been worked out presuming an average ad valorem incidence of excise as shown under col.(3)

**** The incidence of excise and customs duty has been worked out on the basis of average domestic and international price in September, 1977 respectively.

9.60 The first thing that stands out in this Table is that there is a wide divergence between the rates of excise duties applicable to one raw material and another, even in respect of those which are directly competitive. Secondly, the customs duty consisting of the basic auxiliary, and countervailing duty is very much higher then the excise duty. We have to consider whether and how far these differentials are necessary and justified. If raw materials which do not compete with each other are taxed at different rates no distortions of the type created by differential taxation of competing inputs arise. The level of duty in such cases would have to be examined by considering their incidence on the non-taxed sector and cumulative rates applicable to the final products as also whether input duty relief is being extended or is possible. Similarly, if the total customs duty is only so much higher than the excise as is necessary for protective purposes there would be no occasion for suggesting any reconsideration. Unfortunately, as our further discussion will show, this is not so. As regards the level of excise duty, the mean rate applicable to basic raw materials according to certain calculations which we have made seems to be about 25 per cent. We propose to treat this as a yardstick in considering whether the rates of duty on particular product families or on individual items within them are too high or too low.

FERROUS METALS

9.61 To begin with, we examine the levies on the more important metals which are basic raw materials for a wide range of products ranging from pots and pans to air-conditioners and automobiles in the consumer field and which are used extensively in capital investment in the shape of machinery, factories and buildings. Steel is easily the most important among them. The excise duty, although specific and varying from category to category, works out to an average of 23 per cent which is close enough to the mean rate referred to above. The import duties on mild steel (on which the average incidence

of excise is 25 per cent) add up to an unnecessarily high figure of 69 per cent when the domestic mild steel industry does not need any tariff protection at all. The excise on domestic steel was raised a few years ago because it was cheaper than imported steel though the same balance between imported and domestic price could have been achieved by lowering the customs duty. As we are presently exporting rather than importing mild steel sections the customs duty does not hurt any one but it gives no substantial revenue either. A reduction in the customs duty could well be considered at a time when no loss of revenue would be involved. The detailed study of the taxation of steel which is given in the Appendix 14 brings out that a fairly large proportion of rolled mild steel is consumed by sections such as house building as well as various small producers who are not within the excise net.

9.62 Although the average rate of excise on mild steel sections does not appear to be too high there is considerable difference in the rates applicable to different sections. What causes concern is that some of the highest rates are applicable to those sections which do not go to the untaxed sector but are in fact mainly used by industries which are themselves subject to excises or in respect of which on end-use considerations there seems to be a prima facie case for re-adjustment. Thus, the impact of the levy on skelp which is exclusively used for further processing by industries is over 35 per cent. Galvanised sheets which are used in low cost or emergency housing as well as in the constuction of storage and residential accommodation for the Defence services is taxed at rates varying from 33 to 40 per cent. As the zinc used for galvanising also bears a fairly stiff tax the cumulative levy on galvanised sheets exceeds 50 per cent in some cases.

9.63 There is another point which is relevant in the case of mild steel as in the case of many other products. The price of mild steel is regulated not by market forces but is determined by the Joint Plant Committee presided over by the Iron and Steel Controller. The prices for different sections take into account not only what accrues to the plant but also various other factors such as cost of equalising freights on an all India basis, the contributions which are made out of the sale proceeds for providing assistance to the export of engineering goods and for taking care of freight differential in respect of re-rollers and also we believe for fixing the prices of different sections with some regard to the essentiality of their end-use. Therefore, what Government have to consider is the price-cum-tax structure. If the prices of different steel sections are themselves determined with due regard to having such elements of discrimination as are socially and economically justifiable there is no particular reason why the tax structure should also seek to introduce differentials. A uniform ad valorem rate could well be introduced to determine the revenue element and thereafter the Joint Plant Committee could have the freedom to adjust prices of individual sections taking all factors into account. In any case, we would urge that the rates should be ad valorem rather than specific so that there is an automatic and proportionate change in the tax whenever prices change - with specific duties, we have observed that tax revenue changes have not been proportionate to price changes in the past. Also, we would suggest consideration being given to bring the rate down on the categories which bear rates of duty higher than 30 per cent to which we have referred above.

9.64 Turning from mild steel to alloy and special steel including stainless steel their average prices are much higher than that of mild steel. Consequently, the present incidence of specific duties on them is much lower than the average incidence on mild steel. As these categories of steel are used generally for industrial purposes in the production of final products mostly in the nature of capital goods, we would recommend a much lower incidence on them than on mild steel in terms of ad valorem levies.

9.65 As regards import duty, Government have already made certain reduction in the customs duties on alloy and special steel and stainless steel in the 1977-78 Budget. Without going into the merits of the new rates, we would only like to point out that too high a level of customs duty not only encourages high cost producers but it also reduces possibilities of additional employment at subsequent stages, which a cheapening of the cost of a basic raw material usually generates.

NON-FERROUS METALS

9.66 The evolution of duties on copper, zinc and lead has some interesting features as outlined in Appendix-15. As under the GATT import duties on copper, zinc and lead were bound, Government imposed an excise duty on what was an insignificant domestic production in order to derive revenues from the imported metal. When release was obtained from the GATT binding, appropriate customs duties were levied on the imported metal but the excise remained unaltered. The excise duties were added to the customs duty as countervailing duties. In the case of copper and zinc, there was a phase when world prices sharply increased and in order to prevent domestic industry from getting a windfall profit, there was a substantial step up in the excise duties. However, subsequently when international prices dropped and became much lower than domestic prices, the excise duty on domestic production was not reduced. (There was some reduction in regard to the excise on copper in the 1976-77 Budget but that was more to help the indigenous producer than the ultimate consumers). Thus, on copper and zinc whose domestic prices are mainly determined by import prices the total customs duty at present is above 90 per cent.

9.67 The Secretariat study given in Appendix-15 also brings out the pattern of consumption of these non-ferrous metals as well as the impact of the existing duties on various consuming industries . We feel that there is a good case for reducing levies on these metals which have a wide variety of applications in the production of electrical goods and accessories and capital goods. The kind of changes we would recommend would be a reduction in the excise on copper and zinc which would also reduce the countervailing duty. We would also favour conversion of the import duty on copper into a specific one because its price is subject to violent fluctuations which an ad valorem duty only accentuates. We also feel that imports of metallic concentrates should be made duty free so that smelters in the country based on imported concentrates do not have their costs raised. There exists at present a time-bound exemption for copper concentrates. This exemption could be continued and similar exemption provided for zinc concentrates.

9.68 Another non-ferrous metal of key importance is aluminium. We have hardly any imports of it and with our large deposits of bauxite even in the long run we should remain self-sufficient or turn into exporters. It is, therefore, necessary to focus more on the excise duty on aluminium rather than import duty particularly as Indian aluminium industry does not need a protective import duty. (International prices are at present higher than prices of Indian producers). The excise rates applicable to aluminium are about 50 per cent on the 'Non-levy' (usually commercial grade) metal and 80 per cent on the 'Levy' (electrolytic conductor or E.C. grade) metal. The manufacturers are required to produce a minimum percentage of the latter and deliver that portion at a specially low, controlled price. The basic objective of imposing a 'levy' to get E.C. grade aluminium at a specially low price was obviously to ensure that the State Electricity Boards got adequate quantity of such metal at a reasonably low price. It also aimed at encouraging the substitution of copper by aluminium in the electrolytic industries. The excise on 'levy' metal has been kept much higher in order to prevent such aluminium from being diverted, because of its cheapness, to non-electrical purposes. However, to compensate for the high excise on levy metal a subsidy is being given to the

electricity undertakings. This subsidy does not fully compensate for the excise levies. Thus, as against an excise duty of about Rs. 5, 276 per tonne paid on 'levy' ingots, the State Electricity Boards get a subsidy of Rs. 3, 130 per tonne of metal used in the manufacture of conductors bought by them. Even after making allowance for the subsidy, the impact of excise duty paid on aluminium is estimated to be around 15 to 20 per cent of the price of the conductors. Thus, the capital cost of extending transmission and distribution of power gets sharply increased. The electricity undertakings are usually making losses. They can undertake only such capital outlays as they are specially given resources for. In effect, the duty on 'levy' Aluminium used in the manufacture of conductors does not result in a net accrual of revenues but it limits the expansion of power facilities to rural areas by artificially inflating its cost.

9.69 The other important users of 'levy' aluminium are manufacturers of transformers and other similar equipment and cables and wire units some of whom are under compulsion to use aluminium. We are told that the high cost of aluminium makes their product un-competitive with those using copper. Unlike State Electricity Boards, these users of 'levy' aluminium do not get any subsidy to compensate for the high duty paid on 'levy' aluminium. Thus, whereas the policy of Government is to encourage the substitution of copper by aluminium even though it is not quite as efficient a conductor, the tax rates give the opposite inducements.

9.70 In these circumstances, we feel that the present duty on this industry needs a fresh look. In regard to the 'levy' aluminium,two kinds of solutions could be considered. The system of 'levy' and 'non-levy' could be maintained, as it is, with full compensation to electricity undertakings for the high excise on 'levy' aluminium and extension of appropriate duty relief (under rule 56-A or under any other provision) to other users of 'levy' aluminium. Alternatively, the whole question of dual pricing and differential taxation could be looked at de novo.

9.71 The tax on the commercial grade aluminium (Non-levy metal) is also clearly high; much higher than on competing metals. Commercial grade aluminium finds multifarious uses and the present duty affects the prices of a number of consumer industries significantly, as shown in the study included in Appendix 15 . Though a reduction in excise duty on this category of aluminium may not be opportune at the present juncture, as we gather there is currently a scarcity of this metal in the country, in our view there is a good case in the long run for considerable lowering of the existing duty and extension of duty relief under rule 56-A in deserving cases.

PLASTICS

9.72 Another important input extensively used in the production of a wide variety of goods, ranging from irrigation pipes for agricultural purposes, sheathing material for electric wires and other similar industrial uses, to a number of consumer products like shoes, buckets, containers and suit-cases is to be found in plastic resins. Appendix 16 indicates the production and consumption pattern of the most important resins as revealed by a study carried out by the Secretariat. It also gives the changes in the rates of duty effected in the past and the impact of the existing levies on the prices of products of a few selected user industries.

9.73 Presently, most plastic resins are subject to an excise duty of 40%, while the customs duty on the imported ones ranges between 35% and 120% plus the countervailing duty. On the other hand, plastic manufacturers as a class are generally free from excise levies and even the 2% excise applicable under tariff item No. 68 does not affect most of them. Since plastic products

were in the nature of novelties, there was a general tendency to treat them as luxury goods. The excise duties on them were therefore, much higher than the kind of rates generally applied to inputs, and in the matter of customs duties, they were subject to the rates applicable to consumer products rather than raw materials and intermediates.

9.74 We have, time and again, drawn attention to the drawbacks of taxing inputs instead of the final products. Input taxation with no provision for set-off at subsequent stages of production creates several harmful effects and also tends to be regressive. On the other hand, we have conceded that it is not possible to avoid the taxation of inputs which generally are consumed by the untaxed sectors also, since otherwise the final products escape taxation altogether.

9.75 The high rates of excise duty on plastics appear to have been imposed for two main reasons. Firstly, at the initial stages, there was an understandable desire to limit imports of the needed raw material, the indigenous production being limited. Secondly, a high proportion of the plastic resins was used by small manufacturers in the unorganised sector whose products could not be effectively taxed. We feel that a reconsideration of the duty structure is called for because of the change in these conditions. There already exists considerable indigenous capacity for the production of resins and, we understand, there would be a substantial increase in capacity in the immediate future when a large public sector unit goes into production. At the same time, the excise administration has, through experience, acquired the capacity to collect taxes at the stage of final products and has also evolved simplified procedures for collecting duties from small manufacturers. In view of these developments, we feel that there should be a shift in taxation from the raw material stage to final product stage, as well as a net reduction in the average incidence on final products. A shift in the stage of taxation, as we have urged above, which is now possible, would enable greater progression being achieved as between fancy products consumed by the well-to-do and those which largely cater to the lower income groups. The net reduction in duty is required not merely because a lowering of price is necessary in order to absorb increased output that would be forthcoming in the near future, but also because the processing industry is largely in the decentralised sector, produces a wide variety of consumer goods, and can generate substantial additional employment.

9.76 A study of the trend in production of and demand for plastic resins indicates that the higher prices and levies have had an inhibiting effect on the growth of demand. It seems legitimate to infer that the demand for plastic products is likely to be elastic in the existing range of prices. Hence, a reduction in duty is likely to lead to a commensurate increase in demand and therefore there may be no loss in revenue. Apart from the question, of effecting a reduction in the rate of duty on resins it would also be necessary to provide input duty relief to manufacturers using these materials if in some cases the cumulative levy is found to be unduly high.

9.77 As regards customs duties, there are many varying rates as pointed out earlier and with the addition of countervailing duties, the cumulative incidence of Central taxation generally ranges between 89 per cent and 145 per cent; the rate going up to 208 per cent in respect of certain resins. To the extent that excise duties are lowered, some reliefs would naturally be there in regard to the levies on imports as well. However, it would be desirable, instead of having different rates for different resins, to have a uniform rate of customs duty for all of them.

9.78 In the preceding sections, we have dealt with the taxation of certain major inputs which find widespread use in industry. In selecting these inputs for detailed treatment, it was also our intention

to deal with cases where we found either undesirably high rates of duty or discrimination in rates which could not any longer be justified on economic considerations. In Chapter 8 we have outlined the main guidelines which should govern taxation of basic raw materials in general and other inputs. It is our view that at the first stage of reform, emphasis should be more on the rationalisation of duties applicable to similar raw materials and other inputs than on a substantial reduction in the average rate of duties. Such reduction in the burden of tax on raw materials as is likely to result from the rationalisation exercise could be partly made up by increases in rates at the final products stage and partly be compensated by increase in output. We deal with this matter in greater detail in the next Chapter.

INPUTS OF AGRICULTURE

9.79 Finally, we should like to comment on the taxation of certain modern inputs of agriculture. In some ways the inputs of agriculture have to be given the same tax treatment as those of industry. The main difference can be said to arise from the fact that the products of agriculture are by and large free from excise taxation, though sales taxes are applicable in many cases. When the duty on fertilizers was first imposed the argument advanced was that it would help in placing the burden on the better off agriculturists who were then being taxed at very low rates or not at all. From such examination as we have been able to make of the problem, we see no evidence to support the view that the taxation of agricultural inputs impinges on agricultural incomes. It raises the cost of production of agricultural products in the same way that the taxation of industrial inputs raises the cost of industrial products. In the case of foodgrains the cost of production are taken into account in determining their prices. As our incidence studies show, these levies do affect all expenditure groups. Prima facie, the burden imposed by such taxation does not appear to be too high. However, it has been argued that these levies hurt the small farmers particularly since their financial resources are limited and their access to sources of credit is also not as good as it should be. There appears to be some force in this argument. On balance, therefore, taxation of inputs of agriculture has to be determined on a wide variety of considerations including the possibilities of raising the requisite revenue from alternative sources.

CAPITAL GOODS

9.80 We now turn to levies on capital goods. Although they are finished goods and not raw materials they do stand in a class by themselves. The main purpose of indirect taxation on an extensive scale is to mobilise resources for investment. To the extent that taxation raises the cost of investment what it contributes by way of a resource gets nullified by the increase which it causes in the requirements of resource for sustaining a particular level of investment in real terms. In our earlier discussion in this Chapter we have struck a critical note about the heavy taxation of trucks and buses which constitute the capital goods of the transport industry. In general the past practice has been to spare capital goods as a class from excise taxation. The notable exceptions have been power driven pumps (5 per cent), diesel engines (5.5 per cent to 11 per cent), motor (5 per cent to 20 per cent) and refrigeration and airconditioning equipments (20 per cent to 100 per cent), possibly because they do not have the image of plant and machinery installed in factory. However, it should be remembered that pumping sets are the capital goods needed by agriculture as much as machine tools, and foundries and forges are of industry. The first general levy on capital goods came about when tariff item No. 68 was introduced. It was more by accident than by design that capital goods came under it because the item referred to all those not specified under other entries. Thereafter, all kinds of capital goods became subject to a levy of one per cent ad valorem which has since been raised to two per cent.

9.81 A low excise levy on capital goods does not have an appreciable impact on the cost of finished products; but if it were pitched at high levels the impact would become significant and suffer from some of the weaknesses of the taxation of inputs to which we have drawn attention. A further point to be considered in this context is that the plea is sometimes made for stepping up the taxation of capital goods on the ground that country is short of capital and there should be some discouragement to the excessive use of capital equipment. If their cost is raised, it is argued, there would be greater use of labour-intensive techniques. In our view, while this line of reasoning has merit, in practice it must be applied discriminatingly and with caution. In our excise system we do legitimately discriminate in favour of products which are made by greater use of manual labour than those which are machine-made. Similarly, to discourage mechanisation in sectors where labour can do the job, selective increases in the levies on the concerned equipment can be made. Levies to prevent mechanisation of certain types of agriculture or industrial operations also would be fully justified. But it should not be forgotten that by far the greatest use of plant and machinery is in line where the production can be achieved through the use of capital equipment alone. On this consideration, in direct taxation, various concessions are given to encourage investment in plant and machinery. Finance for the purpose is provided through special institutions which Government have set up. It, therefore, does not seem desirable to raise the cost of capital equipment in general through indirect levies on the ground that all capital equipment displaces labour, while in actual fact over a wide field it plays a complementary role to labour and help generate employment.

9.82 Although machinery as a class has till recently, been free from excise levies on the final products, the fairly heavy taxes on its main raw materials, namely, metals, has meant that capital goods generally have been contributing to revenues on a not insignificant scale. The cumulative incidence of excise on a number of cases of industrial machinery (which are at present subject to 2 per cent nominal duty) varies from about 2.6 per cent to about 5 per cent. Having regard to all these considerations we feel that a levy of the order of 5 per cent (including the taxation of inputs) could in the interests of revenue be retained without any serious undesirable consequences. To achieve this objective, the present 2 per cent on capital goods and machinery under tariff items No. 68 may continue but in respect of those items of capital equipment where the levy on inputs would make the cumulative rate much higher than 5 per cent appropriate reliefs from input taxation should be allowed. To ensure that the treatment of machinery remains distinct from the miscellany of goods covered by item No. 68, a separate tariff classification should be created and machinery items should be taken out of tariff item No. 68. At the same time Government may wish to re-examine whether there are adequate economic reasons for retaining the higher levies on some of the individual items of machinery named above, particularly those which are needed for improving irrigation to which very high priority is presently being given.

9.83 What we have said above relates to excise.Customs levies on machinery are much higher - around 40 per cent - and some individual items particularly components get taxed even more. Regarding customs duties, our line of reasoning throughout has been that they should be just high enough to provide adequate protection to domestic industry and the revenue element of the customs duty should be governed by the same principles as similar products of domestic origin. We have had quite a number of representations before us for a reduction in import duties in respect of certain types of capital goods either on the consideration that the domestic industry does not

need as high a level of duty to protect it as the prevailing customs duties or on the ground that there is no domestic production and what has to be imported is necessary for development. We do not quite accept the view that machinery items which are not indigenously produced at present should be allowed to be imported without any duty. The existence of an import duty encourages new lines of production to be established.

9.84 About the same time that we started our study Government had appointed a separate Committee headed by Shri Mantosh Sondhi to go into the question of import duties and import restrictions in respect of capital goods. The Committee has already submitted its report to Government and we do not wish to duplicate the effort by undertaking a separate study on our own. We have, therefore, confined our comments to the excise levies and some general observations regarding customs duties. We trust that our comments read with the specific recommendations of the Sondhi Committee will help Government to take the appropriate decisions.

9.85 We have earlier remarked that it would be a mistake to consider capital goods as being synonymous with plant and machinery. There are several other goods which go into capital formation. We have given some examples such as trucks, agricultural equipment and power transmission lines.

CEMENT

Cement is another item having some characteristics of capital goods to which a special reference needs to be made. Major projects such as dams, roads, bridges and canals require cement as their main input. Cement is also needed by almost every industry for factory buildings. Moreover, it is an essential ingredient in the construction of houses for people in all income groups. In fact all housing except, luxury type of residential construction, has to be treated as a form of essential investment in the economy.

9.86 In our view about the undesirability of subjecting investment goods to high rate of taxation is accepted, there would be a case for reducing, as a long term proposition, the existing rate of taxation on cement. While the long term rate of tax on cement would have to be kept higher than the 5 per cent rate that we have recommended for capital goods as a class, we feel that the present rate of duty of about 28.5 per cent is very high, raising the cost of all capital projects. If the needed supplies are forthcoming, such a high rate of duty would tend to inhibit the growth of labour intensive and socially desirable activities such as house building. It is also to be remembered that Government Departments themselves pay a substantial part of tax on cement as they are among these major users.

9.87 Because of the high cost of new capital equipment, it is more than likely that, with the expansion of cement production, additional supplies would become available only at higher prices. Given this probability, the course of action that we would suggest is that the rates of duty on cement should be gradually reduced as more supplies become available so that the higher costs on new production would get absorbed by the reduction in the duties. In other words, while an immediate relief in duty may not be thought of because the present supply position is one of shortage, the aim should be to bring about a reduction in the longer run.

9.88 For Government to move in the direction, which we have indicated, it is eessential that public opinion should support the changes. One of the things which we hope our Report will do is to make it clear to the community that the burden imposed on the consumer by taxation of

inputs, merely because the effect is concealed, is no less onerous and indeed is often somewhat more so than the levies on final products. Further, it should also be clear from our Report that there is no possibility of mobilising the kind of resources which we need if we exclude mass consumption products as a class. In any restructuring, rates on many final products, even those which are consumed by lower income groups, may have to move up. What is important in the assessment of the burden on different expenditure groups is not the incidence of duty on any particular product but of the entire range of products consumed by that group. The changes we have recommended in a downward direction will call for some off setting changes in the upward direction. We have to ensure, however, that the net effect on the lower expenditure groups is favourable and that progression is enhanced and not reduced.

CHAPTER 10

THE REVENUE ANGLE

10.1 Basic to our approach to the problem of reform of the indirect tax system has been the consideration that Government's needs of revenues must be adequately met. We have emphasised this time and again, pointing out that the total burden to be imposed on the community through indirect taxes is a matter for Government to decide. We have seen our task primarily to be the examination, consistently with revenue needs, of possibilities of imparting greater progression to the indirect tax system, by reducing the burden on the lowest income groups, and of recommending changes in the structure of taxation in order to reduce and if possible eliminate any undesirable side effects of the existing framework. Our examination in the preceding chapters and indeed in the Report as a whole of various taxes and their impact on consumers and producers has brought to notice instances where we have felt that a downward revision would be desirable. On a superficial reading of our Report, therefore, it might seem that although we have emphasised the importance of revenue considerations, we have in fact lost sight of them when it came to formulating our recommendations. We, therefore, feel it necessary to re-state, within the compass of a single Chapter, the ways in which the revenue aspect can be fully taken care of, while implementing our recommendations.

10.2 At the outset, we should like to recapitulate the reasons why a number of the existing duties, whose contribution to revenues is high, are such as cannot be justified on rational considerations. When the existing levies were made, it could be assumed that they were carefully scrutinised from different angles. Again, when the need for additional revenues arose, Government should have likewise given adequate consideration to all relevant factors in selecting the products to be taxed. How is it then that taken as a whole the tax structure today seems to be in need of major changes?

FACTORS LEADING TO EXISTING SYSTEM

10.3 One of the reasons for this, we feel, is that while most of the existing high levies had adequate justification when they were imposed, it was but rarely that there was any subsequent re-examination of these to see whether the circumstances which had warranted them had changed and a reduction would be desirable. This was because each year when framing the Budget, Finance Ministers both at the Centre and in the States, have had to face the problem of raising more resources and the question of considering the possibility of identifying items deserving a reduction in the levy just did not arise. It is only when a particular tax was seen to be causing serious damage to a sector of the economy which was vocal enough and important enough to warrant Government's attention that reductions were contemplated. But in general, taxes which had been imposed on entirely different considerations were allowed to continue on revenue considerations even after the reasons for which they had been imposed had disappeared. This trend got reinforced by the general tendency for people to put up with old taxes, however, irrational or high, if not cheerfully, at least, with a sense of resignation, while the imposition of a new tax, even a moderate one, evoked loud protests.

10.4 In respect of excises, the heavy reliance on the taxation at high rates of a few product families and basic inputs - from which arises the major weakness of the existing system - was to

no small extent due to administrative considerations. At a time when bringing in more products under the excise net meant posting additional staff at the premises of each of the factories concerned, it seemed cheaper and easier to raise the rates on items already subject to taxation. Further, in order to minimise the number of units under excise control, the manufacturers of inputs who were few were taxed in preference to industries using them who were more numerous. These considerations have lost much of their validity with the greatly widened scope for self-assessment procedures. Further, as has been pointed out earlier, there has been in recent years a steady expansion in the number of items subject to excises due to the compulsions to mobilise resources, culminating in the introduction of tariff item No. 68 which makes almost all manufactured goods not otherwise taxed subject to a levy. Hence, the pattern based on old practices and procedures has lost its rationale. A more even spread of the burden is called for.

10.5 As regards customs duties, because in the British days the customs tariff was so adjusted as not to impede the maximum import of manufactured goods from Britain - protection being afforded only to a selected few industries, and that too after they had come into being and been subjected to a meticulous scrutiny - there was a general sentiment immediately after Independence in favour of raising customs duties so as to give the maximum impetus to the rapid industrialisation of the country. Later, with the anxiety to conserve foreign exchange, there were repeated hikes in customs duty rates. In the process, prices of many important products have been considerably raised through heavy taxation of imported raw materials and intermediates without public awareness of it. Since the high customs duties afforded to Indian industries much greater protection than they really needed and sheltered even high cost and inefficient units enabling them to make good profits, there was no protest against high customs duties from the industry as a whole. On the customs front too conditions today are propitious for making changes. The country has now a comfortable foreign exchange position. And we were happy to note that several representatives of industry who appeared before us, agreed with the proposition that customs duties over a wide range of producer goods-plant and machinery as well as raw materials - were much higher than could be justified from the protective angle.

10.6 Developments in the economy thus necessitate changes in the indirect tax structure as a whole having regard to the social and economic impact of the existing levies. Essentially, as our revenue needs are great and rising, this should mean not a reduction in the tax burden, but its redistribution. While we have drawn attention to the anomalies, which partly for understandable reasons, have crept into the tax structure, and identified areas in which reductions in duties are called for, we are of the view that the resultant loss in revenues has to be made up by increases in the rates in other areas. In order that Government may be able to take appropriate decisions in the matter in a manner which would avoid distortions, we spell out in the following paragraphs the considerations that should guide the effort.

REVENUE IMPLICATIONS OF RESTRUCTURING EXCISE AND IMPORT DUTIES

10.7 We have pointed out earlier that on the average the tax burden on what might be called consumer products of all sorts inclusive of the levies on their inputs is around 20 per cent (leaving out tobacco, petroleum products and consumer products falling under tariff item No. 68). We have also suggested that instead of a pattern in which some product groups are very heavily taxed while other have remained either totally exempt or have been taxed at very low rates, the attempt should be to tax all consumer products including those now falling under tariff item No. 68 at rates of 10, 20, 30 or 40 per cent (cumulative) though some exceptional products may need to be taxed at lower or higher rates on

special considerations. We believe that such a restructuring of consumer product rates would throw up revenue possibilities of a sufficiently large order. Thus, items other than capital goods falling under tariff item No. 68, which are now taxed at the low rate of 2 per cent (nominal), are capable of yielding an additional revenue of Rs. 20 crores for each percentage point increase in the nominal rate of tax even though this tariff item, rightly in our view, does provide for relief in respect of products which are used as inputs in the manufacture of other dutiable goods. If, for the sake of argument, we assume that Government decided to subject all items, other than capital goods, covered by this entry to the mean cumulative rate of 20 per cent, then, assuming an average input duty incidence of 3 per cent on these goods, the nominal rate would have to be raised to 17 per cent, i.e. by 15 percentage points. This would yield an additional revenue of about Rs. 300 crores. We do not, of course, suggest that a generalised and massive increase of this order would be the best answer. There may well be items in this miscellaneous category - we have already identified capital goods as a class which should not be taxed at a cumulative rate higher than 5 per cent - which would warrant a lower rate of taxation than 20 per cent. The appropriate course, therefore, would be to fix suitable rates for identifiable groups of products covered by this tariff item. This would make a sizeable contribution to revenue.

10.8 A number of products had, in the past, been exempted from taxation because the rates applicable to them under the appropriate tariff head had been considered to be too high. Since they are specified elsewhere they are also not subject to the two per cent general levy. It should be examined whether they deserve to continue to be totally exempt, as at present, or taxed at least at the lowest rate under the residuary tariff item No. 68.

10.9 Side by side, an examination should be made of the existing rates applicable to all consumer products (other than those falling under tariff item No. 68) to see whether the difference between the existing cumulative incidence on them and the average rate of 20 per cent is justified. In some cases, the rates will deserve to be lowered rather than raised. Cases for relief which the exercise throws up should not be ignored "On revenue considerations" because rationalisation must lead to reduction at some places compensated by increases elsewhere. But we feel that, on the whole, such an exercise would be quite rewarding in terms of identifying products which are now taxed at low rates by accident rather than design.

10.10 We have recommended a reduction in duties on several inputs. If the consequent reduction in the cumulative tax burden on certain products using these inputs turns out to be more than what Government feel would be justified having regard to the nature of the final products and classes to whom they cater, the revenue loss can be recouped by appropriate increases in the nominal rates of duty. We have ourselves recognised that reduction in duties on inputs can proceed only upto a point. We have, therefore, laid stress on the extension of appropriate input duty relief to take care of the problems of cascading and distortions. Here again, if the existing cumulative levies on the concerned final products are more or less at the appropriate level, input duty relief will have to be accompanied by a suitable upward revision of the nominal rates.

10.11 Throughout the Report we have pointed to the desirable direction in which changes should be made. In doing so, we have neither listed all the products in respect of which a revision of the existing rate is called for nor quantified the extent of the change. The final judgment on these will have to be exercised by Government having regard to the broad criteria which we have emphasised. We believe that when deciding upon the broad changes to be made it would be possible to ensure that the reductions in duty are broadly balanced by enhancements in appropriate cases.

10.12 We also feel that it may not be possible or even desirable to make all the changes that are considered advisable in one single Budget. Phasing may be desirable not only on revenue considerations but also to avoid too severe a disturbance at one stroke in the existing intersectoral balances between costs and prices. The pace of change may well be spread over three years or so. However, we would very much hope that a complete phased programme for bringing about all the needed changes will be accepted by Government even at the first stage. Otherwise, there is every danger that the first phase would get implemented and thereafter the need for considering other modifications would tend to be forgotten. In evolving a phased programme a judgment regarding priority action will need to be exercised taking into account the growth potential of different industries and the importance attached to them. One of the things we would emphasise is that if a reduction in excise duties stimulates production or reduction in import duties leads to higher imports and - in the case of inputs - to increases in domestic production, the loss of revenue may well be amply compensated because though the rate of duty would have gone down the volume of goods to which it applies will have gone up. In fact one of the considerations which has influenced our thinking is this very possibility of a lowering of duties resulting in a larger offtake.

10.13 This consideration is particularly valid in today's conditions when we think of import duties. The present levels came about primarily on account of the desire to conserve foreign exchange. In today's conditions, there is all round emphasis on taking steps to increase the utilisation of foreign exchange. An addition to the reserves increases money supply in the economy which has an inflationary impact. Government have, therefore, liberalised imports of a wide range of products. We have emphasised earlier that when there is a tight regime of import control a lowering of import duties only increases the profits of the importer and does not benefit the community. However, it is clear now that for a range of products, whose imports have been liberalised, the customs duty does tend to restrict the volume of imports. Government have in certain cases already lowered import duties on some products. We feel that in so far as reductions in duties have to be phased, priority should be given to a reduction in customs duties over a reduction in excises because in terms of resource mobilisation imports not only contribute to the Exchequer by the amount of duties they bear but they also help to cushion the impact of budgetary deficits by bringing about a contraction in the money supply to the extent that the foreign exchange reserves as well as external credits are drawn upon. However, as pointed out above, a reduction in the import duty should follow and not precede an appropriate liberalisation of imports. The process of liberalisation can be carried much farther than has been done so far. The Industrial Policy statement of Government has recognised the desirability of doing so and making customs duties provide the measure of protection that domestic industry needs.

10.14 So far, the liberalisation of imports has not been extended to what might be called consumer goods which bear, as a class, an import duty of 120 per cent. While certain types of consumer goods may well continue to be under a ban because their importation would entail a wasteful use of foreign exchange, which after all is a precious reserve, there is considerable scope for allowing imports on a more liberal basis of products needed by various consumer groups including the professional classes like scientists, doctors, photographers, sportsmen and even students, though the duties on them need only be lowered where it is the intention to bring the product within the reach of the less affluent sections of society. From the point of view of curbing smuggling too, liberalisation of imports and scaling down of duties on some consumer products would seem desirable. In

fact very high customs duties on items which are easy to smuggle can be counter-productive. The items where there is an incentive to smuggling could also be identified and considered for liberlisation of imports and if need be, for lowering the rates of import duties. In respect of such cases, we can confidently expect an increase in revenues.

INCOME ELASTICITY AND INCREASE IN TAX BURDEN

10.15 We would expect the measures we have recommended to impart greater income elasticity to the Central taxes. Through conversion of more duties to an ad valorem basis and widening the tax base, revenues could be expected to rise at a higher rate than national income from year to year. If a need is felt for even higher increases in revenues or for raising the total tax burden on the community, this could and should be brought about by a general increase. In other words, we would favour the kind of resource mobilisation which is spread in an equitable way across the board, rather than selective increases, which inevitably lead to distortions. Thus, if a general one percentage point increase is made in excise duties on all consumer goods (leaving those which are classified under tariff item No. 68) the additional revenue on the basis of the present level of consumption would be around Rs. 100 crores, which is, by no means, a small order of resource mobilisation. We are not for a moment suggesting that a flat percentage point increase in levies on all finished products would be desirable, because it would mean a much sharper increase in the levy on lower taxed products than on those which are taxed more heavily. It would, therefore, tend to be regressive. The better method would be to have a surcharge and a surcharge equal to 5 per cent of the existing rate of duty on different consumer products (other than those classified under tariff item No. 68) will bring in the same amount of revenue as a one percentage point increase in duty on them. A point worth considering in this context is whether this would not mean a general price increase which would be undesirable. While obviously an increase in indirect taxation does raise the burden on the consumer, given the small proportion of industrial consumer goods to our total rational product in which agriculture still has the largest single share the impact on the price level of the kind of increase we have been speaking of, would be only around 0.03 per cent which is, by no means, a formidable figure. This method of mobilising additional revenues will obviate the need for raising the rates applicable to inputs which, in the future, we feel should only be undertaken if it is intended to discourage the use of particular inputs because of their short-term or long-term scarcity.

10.16 In Chapter 13, we make recommendations for a reduction in the rate of CST and for relief under sales tax for inputs. The ways in which any consequential loss in revenue could be made up are also discussed in detail in the same Chapter.

10.17 During the course of our enquiry the fear had been expressed by some spokesmen of trade and industry that it could well happen that Government would accept our recommendations for raising taxes and reject all those which favour a reduction. On the other hand, some official spokesmen have expressed to us the concern that we shall be making recommendations which may seem very attractive but which cannot in practice be implemented because they would entail a loss of revenue. Our attempt has been to formulate a package of recommendations which taken together will not have any adverse effects on revenue. We have, therefore, attempted not only to point to areas where a reduction in tax seems to us to be justified but also to indicate ways in which revenue interests can be safeguarded and ways in which the resources mobilisation effort can be strengthened.

CHAPTER 11

STIMULUS TO PRODUCTION AND INVESTMENT

11.1 In our planned economy, the Government uses a variety of instruments to promote industrial development in general and to give encouragement to particular industries. These include measures of direct assistance, such as, availability of credit on preferred or concessional terms as well as fiscal concessions in the fields of both direct and indirect taxation. Sometimes, the technique used takes the form, not of giving a concession to the industry or the unit concerned, but of having a higher levy on its competitor, e.g., when customs duties are raised to provide protection to domestic industries. The very fact that there are many different ways in which the requisite assistance can be provided to deserving industries makes it clearly necessary to select in each case what would be the most suitable and economical way of achieving the object in view. Because excise duties are seen to be impinging on particular industries and particular products, there is a general tendency to look upon excise concessions as the most obvious way of helping an industry no matter what its problem is. A more discriminatory approach in which the fullest consideration is given to other possibilities is called for. Among them direct subsidisation should also be included. Often an excise duty concession is also a form of subsidisation because it entails a sacrifice of revenue. Although, psychologically, a sacrifice of revenue gets more readily accepted than an outflow from revenues which a straight subsidy entails, the fact that subsidies by their very nature attract constant attention of Government and Parliament tends to ensure that they are neither excessive nor continued beyond the period for which they are really needed. Excise concessions once given tend to be lost sight of and may continue to confer benefits even when they are no longer warranted because conditions may have changed.

11.2 We also feel that excise concessions which discriminate between different units of the same industry should as far as possible be avoided. It is one thing to give protection to an industry as a whole by curtailing the competition offered by imports. However, as between industrial units within the country, the general rule should be to allow and encourage free competition except when an identifiable class of producers, rather than individual units, need protection on wider social considerations, e.g., the small scale sector whose special position we discuss in the next Chapter. . With this note of caution, we proceed to a discussion of the various concessions in regard to indirect taxation which have been given to fulfil different objectives.

11.3 Excise duty concessions have often been used in serseveral ways for encouraging production in particular industries or industrial production generally. The most comprehensive of such concessions is the excise duty concession announced in the 1976-77 Budget under which clearances in excess of a certain norm, which is different for new units and older units, qualifies for a 25 per cent reduction in the rate of excise duty applicable to such clearances. On a more limited scale, excise duty concessions have taken various other forms. There has been the Tax Credit Certificate scheme meant to encourage higher production, which was in operation from 1965 to 1970 in respect of selected industries. In some industries (e.g., paper), excise duties have been kept lower for units with installed capacity below a certain level. There have also been cases in the past when the concession was available to units whose clearances did not exceed a certain limit (e.g., tyres, aluminium). Finally, there is the case of sugar where the excise concession has traditionally been related to earlier crushing or late crushing, on the ground that such a concession partly or wholly offsets the disadvantage of early or late crushing, thus creating an incentive for maximising production.

THE PRODUCTION ANGLE

11.4 These variants are illustrative of the use made in the past of the excise duty mechanism as a means of encouraging particular types of production or giving a boost to industrial production generally. The first point which arises is why any excise duty concession is necessitated. Here two types of cases need to be distinguished. The concession results in a lowering of the price to the consumer or it improves the return which the producer gets per unit of output sold. In the first type of cases, the boost to production really comes from a reduction in the tax inclusive price of the product. In such cases, the lowering of the excise duty, other things remaining the same, brings about a change in relative prices and thus encourages demand for the particular product. A case in point is the duty reduction on television sets with an ex-factory price below a certain level (introduced in 1976-77 Budget) which resulted in an immediate and significant increase in their offtake. Passenger cars offer another example of production and sales picking up as a result of concessions in indirect taxation.

11.5 Excise duty reductions are more likely to be effective in cases where the prevailing level of excise duty is significant and where the price elasticity of demand for the product is relatively high. If, because of the high consumer price inclusive of excise duty, the effective demand for a product is less than the potential domestic supplies from existing capacity, there would be a case for a reduction in excise duty to boost demand. However, in coming to a decision, a number of considerations will have to be borne in mind. Firstly, the duty reduction will have to be significant if it is to really boost demand. Secondly, there would be the consideration of the impact on revenue. To some extent the loss of revenue per unit would be made up by the increase in the number of units produced and sold. A more important consideration is whether the concession would mean stimulating the flow of resources into a low priority area.

11.6 Perhaps the point can be best illustrated by discussing a specific case which had been presented to us during the course of our enquiry. Manufacturers of airconditioners represented to us that as a result of the stiff increase in the excise duty to 100 per cent, not only had their production and sales gone down, resulting in capacity and labour being rendered idle, but even the revenue had gone down. What is more, the bulk of their sales after the duty hike was to Government departments and corporate bodies, both in the public and private sectors. Therefore, as substantial proportion of the revenue now derived was directly or indirectly coming out of the Exchequer. Purely on revenue considerations, therefore, a good case for a reduction in duty could be made. On the other hand, there is the question of priorities ultimate judgment on which can only be formed by Government. The only comment we would offer in respect of cases of this type is that when investment has already been made with appropriate approvals from Government and subsequently it is felt that the industry should be accorded a lower priority, it would be preferable to take steps to prevent new investment being made in that industry than to render the investment already made wholly or partly infructuous.

11.7 The other type of case is where as a result of the excise duty concession the producer is able to increase his realisation by keeping to himself a large part or whole of the benefit accruing from reduction in duty on part of his production. This is more likely to be the case when the duty rates and the elasticity of demand are relatively low; small changes in final consumer price are unlikely to have much effect on total demand, but even a small improvement in realisation per unit of output could have a significant impact on the unit's profitability and, therefore, the producer would have an incentive to produce more than the normal. This is, however, possible for an industry as a whole only if the demand is growing at an adequate rate. Otherwise, the effect of an excise duty benefit of this kind would largely go to the relatively more efficient units in the industry which would tend to increase their share of the market, the size of which is not appreciably enlarged by the concession.

11.8 The possibility of extending the concession in such a way that it applies not to the industry as a whole but to that sector of the industry which is facing difficulties does exist. The benefit, in other words, would accrue to what one might call — depending on how one looks at it — the weaker units or the less efficient units. Differential taxation of units within the same industry should not be lightly thought of, though in our conditions it cannot be entirely ruled out. What is important in adopting this device is to ensure that the benefit accrues to a sector which is deserving of the concession and whose difficulities are not of its own creation or a result of its own mis-management.

11.9 At times, recourse has been had to differential taxation as between old and new units, the latter being taxes at a lower rate with the object of stimulating additional investment and compensating the new units for any cost disadvantage. In such cases, obviously, the market price for the product being more or less uniform the newer units in effect would be able to realise a higher net price. This is because their duty liability will be lower as compared to the other units. To the extent that such higher realisation compensates the newer units for a specific disadvantage, such as, higher capital costs, they do not pose a threat to the viability of the existing units.

11.10 In theory, it is possible to conceive of an excise duty relief which compensates a manufacturer for increasing his output beyond the lowest unit cost point on the cost curve. This may even be justifiable if in a capital scarce economy, increased capacity would involve substantial capital costs or there is a lumpiness in investment which necessitates production on the rising portion of the marginal cost curve. Such use of excise duty reliefs for increasing production, however, is likely to be useful only if passing on the concession to the consumer in the form of lower prices is not insisted upon. Thus, the use of excise reliefs for boosting production has some economic limitations and should not be looked upon as a sure method for increasing production or encouraging investment in certain areas.

ALTERNATIVES TO EXCISE DUTY RELIEF

11.11 Therefore, when considering grant of excise relief for boosting production, it should also be examined whether some alternative instrument, either under the direct tax system or in the monetary field or in the price policy field, cannot be more fruitfully used to achieve the same objective. Since certain incentives for investment are available in the direct tax structure also, in considering further reliefs in the indirect tax system for encouraging any activity, a comprehansive view has to be taken of the total relief available under the fiscal system. For example, if a higher quantum of benefit has to be provided for investment in a critical industry for which investment allowances under direct tax laws is already admissible, it might be much better to increase the quantum of such allowance for that industry rather than use the excise duty instrument in addition to the investment allowance. In this context, it should be remembered that if new capital investment is more expensive it is often more productive and the cost disadvantage is not quite proportionate to the difference in the price of new machinery and old machinery which has already been written down in value.

11.12 Another point to be borne in mind is that to the extent that new production is likely to have a higher cost sooner or later the community must get ready to pay the higher price. If the excise system were to begin to absorb increases in costs in order to maintain prices unchanged, its revenue potential will be seriously eroded. For industries which are subject to or are amenable to price control, an appropriate price policy might be a preferable alternative. In certain cases, however, where the liquidity position of new firms has to be improved in the initial years when production itself would be not quite up to the mark, it may be helpful to use the excise duty instrument to ease their

financial position. But the general conclusion is that attention should be paid to reliefs which might be available under the direct tax system, and also to the possibility of using some other instruments, such as, price policy and credit facilities, before deciding upon excise concessions to new units to overcome their problems.

11.13 In the light of the above considerations, the Committee has briefly examined the working of the excise relief scheme linked to excess production as well as some other forms of excise reliefs which have been provided for giving incentive for production. The Committee's conclusions in regard to utility of the schemes are given in the following paragraphs.

EXCISE RELIEF SCHEME FOR HIGHER PRODUCTION

11.14 This concession was introduced in June, 1976 following the Finance Minister's announcement in his speach presenting the Budget for 1976-77. While announcing the scheme, the Finance Minister had stated that the scheme visualised grant of relief in respect of selected commodities to the extent of 25 per cent of duty payable on goods produced in excess of production in a selected base year and was meant to encourage higher production. The detailed scheme, which was introduced in June 17, 1976, was originally extended to 43 excisable products and became operative from Ist July, 1976. Subsequently, in July, 1976, paper and paper boards (except for converted papers and paper boards) were included in the list and, in September, 1976, wool tops and seven items of man-made textile fibres and yarn were added.

11.15 The salient features of the scheme are :

(a) The scheme is applicable to the entire operations of a manufacturer and is related to all clearances made by him or on his behalf, though for convenience the concepts of 'base year' and 'base clearances' are defined with reference to a factory.

(b) The determination of 'base clearances' for the purpose of deciding the availability of excise relief and the quantum thereof is as under :

(i) 'nil' in respect of factories from which specified goods are cleared for the first time on or after 1.4.76;

(ii) one-third of the aggregate of clearances of specified goods during the financial years 1973-74, 1974-75 and 1975-76 taken together, in respect of factories from which such goods were cleared for the first time on or after 1.4.1973 but not later than 31.3.1976;

(iii) the aggregate of the clearances of specified goods in the year in which clearances of such goods during any of the financial years 1973-74, 1974-75 and 1975-76 were the highest, in respect of factories from which such goods were cleared for the first time earlier than 1.4.1973;

(iv) in the case of a manufacturer having more than one factory, each of which had its first clearance before 1.4.1973, the highest clearances effected by the manufacturer (taking the clearances of all his factories together) during one of these years, namely, 1973-74, 1974-75 and 1975-76.

Note :—Factories which commenced production between 1.10.1972 and 1.4.1973, if their entire production during that period did not ex exceed 5 per cent of the production during the financial year 1973-74, are deemed to have commenced production on 1.4.1973. In the case of a manufacturer having more than one factory, the clearances from the factory(ies) affected by power cut, natural calamities (e.g., flood, fire) or on orders of Government requiring curtailment production, are excluded both for calculating base clearances and current year clearances.

(c) For the purpose of determining the base clearances as well as current year's clearances, only duty paid clearances for home consumption, clearances for use in the production or manufacture of other goods, and clearances for export, are taken into account.

(d) In most of the cases, base and excess clearances are determined in physical terms, viz., by weight, number or volume. In a few cases, where clearances are to be determined in terms of value, an attempt has been made to neutralise the effect of price escalation with the help of the average index number of wholesale prices for 'manufactures'.

(e) The exemption could be denied to a manufacturer who alters, without adequate justification, the pattern of production substantially during the current year vis-a-vis the base period.

(f) The scheme is operative upto the 31st March, 1979.

11.16 When the scheme was introduced it was widely hailed as a measure to boost production. In its working, however, a number of problems have cropped up because the structure of the scheme is somewhat complex. A widespread criticism of the scheme has been that, in conferring benefits, it has discriminated between industry and industry as well as between units within the same industry, in a manner which was perhaps neither intended nor can be considered to be justifiable. Opinions have also been expressed to the effect that such excise duty concessions do not really help achieve the objective of higher production but at the same time cause distortions in the production pattern and even in regard to prices.

11.17 Further, it has been pointed out that the base period with reference to which the increase in production got the benefit of the tax concession had to distinguish between wholly new units, units which had come into existence in the previous three years, and those set up earlier. The newer the unit the greater the benefit it derived. In consequence, older units have complained that they have suffered while the new units feel that the extent of relief has not been sufficient. Another weakness that has been pointed out to us is that the choice of the base year is favourable to some units but unfavourable to others. Sometimes, the gains have been fortuitous, e.g., , when the production of the factory in the base year was unduly low because of any special difficulties such as, lack of power or raw materials or labour problems, and the subsequent increase in production was going to take place any how as the impediments to it had been removed. Then again, the maximum benefit of the duty reduction went to industries which had the highest rates of duty. The relief of 25 per cent of the duty payable meant much more to industries like tyres and polyester fibre which

were subject to ad valorem duties of 55 per cent and 100 per cent respectively, than to industries like caustic soda and soda ash on which the duty is only 10 per cent. It has also been pointed out to us that in the case of industries which had an insufficiency of demand the scheme did not mean more production overall but only a redistribution of the same level of production among different firms. In short, a seamingly uniform formula has resulted in benefits which are far from uniform as between industries to which it applies and even between units in the same industry.

11.18 Operationally, the scheme has presented a few problems which, though not insurmountable, need to be taken note of. First, where a manufacturer has more than one factory, the determination of base clearances and allowing of the duty relief has been found to be difficult. Second, in the case of tea and coffee the benefit does not actually accrue to the growers but to selling organisations. Third, there is still considerable confusion in the minds of departmental officers as well as the industry about the passing of the benefit of duty exemption to the consumers. Many departmental officers have also preferred payment of excise relief as a lumpsum at the end of a month or a quarter though not envisaged in the scheme. A quick study made of the operation of the scheme shows that there is no perceptible spurt in the production of the selected commodities to which the scheme has been made applicable. From the study made it is seen that during 1976-77 in all about 1230 manufacturers have claimed benefit under the scheme. The duty concession derived by these manufacturers during 1976-77 amounted to about Rs. 45.9 crores. Of this benefit about Rs. 23.7 crores was claimed by the old manufacturers who had effected their first clearances prior to 1.4.1973; about Rs. 21.1 crores by those who had first clearances during the period 1.4.1973 to 31.3.1976; and only about Rs. 1.1 crores by those who started their first clearances on or after 1.4.1976.

11.19 While, admittedly, it is too early to comment on the efficacy of this excise relief scheme and its effect on boosting production, if preliminary indications are any guide, the major impact of the scheme would seem to be a redistribution of the same level of production among different manufacturers in which the more efficient have been the net gainers. We would, therefore, not favour in principle the introduction of a scheme of this kind across-the-board.

11.20 However, since it is not desirable as a rule to modify concessions once announced during the period of their validity, we would advise against any modifications of the scheme while it is in operation. We feel that the scheme should be discontinued after the period of three years is over. Thereafter, if at all any concessions of this nature is decided to be given, it should take into account the weaknesses of the present scheme. In particular, schemes meant to encourage higher production from existing units should not be extended to wholly new units for whom it may be much more appropriate to devise a needbased scheme for each industry as discussed in the next few paragraphs.

ENCOURAGEMENT TO NEW UNITS

11.21 The question of fiscal concessions to newly set up manufacturing units either to sustain them during the initial period of their existence or to encourage investment in priority industries has to be viewed in its own perspective. The major disadvantage that the new units suffer from is that on account of inflation abroad as well as within the country and of other factors like stringency in credit and delays in delivery of equipment, the capital outlay is very much higher than before, per unit of production capacity created. As a result, their cost of production is higher. This, it is said, leaves them little scope to adjust their prices so as to carve out their own share in the market, in the face of competition from old units who enjoy additional advantages flowing from well established goodwill and brand preferences. In many case, it

is pointed out that keeping the prices on par with those of established units would give inadequate return, which acts as a damper on the setting up of new units. In view of the fact that direct tax reliefs are generally available only at a later point of time when gross profits are generated, while excise reliefs have an immediate impact and can even help in meeting day-to-day cash flow requirements, it is argued that to enable these new units to earn a reasonable return on investment while selling at the same price as the older units do, it is necessary to think of granting excise concessions to them for a given period of time after they have gone on stream.

11.22 Weighty as these arguments are, there are also other factors to be reckoned with. Though in terms of cost, new plant and machinery impose a greater strain on the finances of the new unit, it is probable that the newer unit would have higher productivity and also that the product itself would be of a better quality. Further, the price disadvantage on account of higher costs of capital equipment may not be as great as the difference in the price of such capital equipment suggests, except in the case of what are referred to as capital-intensive industries (where depreciation and gross return on capital employed form a substantial portion of the price of the product, say, 20 per cent or more). It is really in the case of the latter that fiscal concessions can be considered as a means of removing the inhibitive effect on new investment which arises on account of the higher costs which newer units may suffer from.

11.23 However, before settling on what the role of concessions in indirect taxation should be, we must take into account some other relevant factors. There are various allowances which have been given from time to time in direct taxation by way of development rebate, investment allowance, accelerated depreciation and the like, which are meant to deal with the difficulties arising out of the higher cost of new capital equipment compared with older ones. In general, incentives in direct taxation have a greater role to play in this sphere. But there is one type of problem facing new units in capital-intensive industries which cannot be taken care of by the kind of devices just referred to. In its initial years, the unit may be confronted with a situation when by selling its product at the prevailing market price it would make a loss not only because of the higher capital cost but because it takes quite some time before its level of production can come to optimum levels. Concessions in direct taxation can enable the unit to carry forward a loss which may reduce its direct tax liability when it starts making profits. But this may take 3 or 4 years. Mean while, it may be facing a situation in which, as referred to earlier, its cash outflows on account of the prime costs of production may be higher than its cash realisation through its sales. If a part of the sale proceeds has to be utilised to pay excise duty its liquidity problem may become very serious indeed.

11.24 In theory, it can be argued that the problem can be met by having recourse to borrowings from banks. In practice, this may not be too easy and will in any event be a rather costly alternative. Again, in the case of products which are subject to a regime of administered prices, under which different units sell their products at different prices to a centralised agency which then markets them at uniform prices, the problem could be dealt with by the centralised agency paying for the product of the new units a sufficiently high price. While these possibilities exist and should not be ruled out, there is something to be said for a system which would provide the necessary sense of security to the investor, rather than leave it to him to try to persuade financial institutions or the central agency, if there is one, to come to his rescue

11.25 The first question to consider would be what kind of industries should be eligible for any concession that might be proposed. We have said that the problem relates to capital - intensive industries

and the question may well be asked why in a country with scarcity of capital and such massive unemployment any fiscal incentives should be given to capital-intensive industries. The point which is missed by those who argue on these lines is that while there is every reason to discourage through fiscal devices and other means the use of capital-intensive technologies, the argument does not have validity in respect of industries which, if they are to be set up at all, have to be capital-intensive. We can certainly encourage, as we do, the production of textiles by handlooms rather than throguh expansion of the mill sector. But if we wish to produce our own nitrogenous fertilisers like urea rather than import them, if it is our desire to augment the supply of raw materials to the handlooms by producing our own synthetic fibres and yarns, if it is the national policy to create enough capacity for producing aluminium to meet the needs which range from transmission lines to pots and pans, there is no choice except to set up capital-intensive industries. To the extent that in our Plans we provide for the creation of additional capacity in such industries, either by way of substantial expansion of existing units or of setting up of new ones, whether they are in the public or in the private sector, we must accept the need to ensure that fiscal and price policies between them encourage the flow of adequate investment into these sectors. If we were ready to allow the new units to be the pace-setters in regard to prices, which would result in higher profits to older units which would in turn encourage them to expand, we could have the kind of solution which market economy countries adopt to deal with the problems we are discussing. However, in our economy, such an answer may not be acceptable for many products. Therefore, fiscal concessions may be useful at least as a transitional device, though in the long run, the level of prices must catch up with the cost structure of new units.

11.26 Indeed the principle of fiscal concessions already stands accepted so far as direct taxation is concerned. What we are considering is a situation in which concessions in direct taxes do not provide an adequate answer to the cash flow problem which gets accentuated by the excise levies for the reasons explained above. To deal with this problem, we feel that some concessions in regard to excise levies in the initial years of production, both to new units and to cases of substantial expansion of old units, would be justified. We suggest that the concession should not be expressed as a percentage of the full rate leviable on the product, because it gives a much bigger incentive to the more heavily taxed — and possible less aessential — products than to those which are moderately taxed. The concession could well be in the form of a 10 percentage point reduction in the full rate of tax on the product. It should become applicable from the date of commencement of commercial production and remain valid for a limited number of years not exceeding five. The total amount of the concession should be expressed as a percentage of the investment in fixed capital. Since concessions in respect of such investments are already available in the shape of investment allowance, it would be necessary to take a composite view to ensure that the total quantum of fiscal concession is reasonable and adequate, but not excessive. If such a scheme is introduced, a careful watch will neccessarily have to be kept for a proper evaluation of the benefits that may flow from it. The aim of this review should be not to withdraw concessions which have been announced and on the basis of which investments may already have been made, but to enable changes to be made or even the scheme to be withdrawn on account of changed circumstances and priorities, but with adequate notice.

RELIEF TO COMPENSATE FOR HIGHER COST OF PRODUCTION DURING CERTAIN PARTS OF THE SEASON

11.27 Having outlined our general approach to the use of excise concessions as a stimulus to production or investment, we now proceed to offer a few comments on some of the schemes applicable to particular industries. Excise duty relief to stimulate production of the sugar industry is in principle given partly for compensating the actual cost disadvantage in early or late crushing and partly to encourage maximum use of existing crushing capacity. As an incentive for increased production, an exemption

in excise duty is given for production in excess of the average of last three sugar years (October to September) on a month to month basis. The concessions on current rates of duty are substantial and much higher as compared to the 25 per cent excise relief on excess production admissible to other industries. In addition to the relief for crushing during the lean season the industry also enjoys the benefits of investment allowances.

11.28 Apart from the fact that the sugar excise duty rebate schemes have been highly variable from one year to another in the light of changing crop, market or demand situations, and consequently have failed to serve a long term purpose, there is also the consideration that in that particular industry the reliefs are in the nature of a subsidy. This is because from a social point of view crushing of immature or dried-up cane is not a desirable activity. The need for excise relief primarily arises from the fact that irrespective of the utility of the raw material the State-administered prices require a uniform payment for cane in terms of weight. The situation would be different if the payment for cane was related to the sucrose content for each lot of cane delivered to the factory. In such a case, special incentives for early/late crushing would not be necessary.

11.29 A question that arises for consideration is whether the incentive should be in the form of excise duty relief or whether the same purpose could not be served effectively by an assurance of a higher price to the producers in respect of the excess production. In an industry which is already subject to a dual pricing system, the incentive should, to the extent possible, be in the form of modification of the existing pricing system rather than be at the expense of the Exchequer. Such a price, of course, has to be attractive in relation to the realisation of both levy and non-levy sugar in the domestic market. The price would depend upon Government's assessment of the quantum of extra realisation necessary in the given circumstances. Such a scheme would assist higher production for exports and also to build a buffer stock for influencing open market prices. The incentive would also be clearly related to a public purpose and the scheme would enable each producer to make his own decisions regarding how early he should start crushing or how late he should continue.

EXCISE RELIEF FOR ENCOURAGING THE PRODUCTION OF LOW-PRICED CONSUMER DURABLES

11.30 The instrument of excise relief for encouraging the production of low-priced consumer durables has been in use for quite some time now. Thus, economy class refrigerators upto a capacity not exceeding 165 litres bear lower rates, viz., 40 per cent and 50 per cent, as against a 75 per cent duty on refrigerators of larger capacity. Similarly, with a view to providing wider access to entertainment and instruction to a greater number of people, the excise duty on television sets of a value not exceeding Rs. 1800 per set was reduced from 20 per cent to 5 per cent ad valorem in March, 1976. This value was further reduced to Rs. 1600 in June, 1977, for certain varieties. In the case of radios again, lower rates have been prescribed for low-cost smaller sets, so that even the poorer class can gain access to them.

11.31 In principle, such excise reliefs, which lend an element of progression to the tax system and also help achieve a greater utilisation of the existing productive capacity, have much to be said in their favour. In a country where the income levels are low and there is a considerable population in the poor and lower-middle class category, they serve also a desirable social purpose. In terms of increasing production also, such a measure can be effective as has been the case of television sets. Reports indicate that schemes of the above kind have had a decisive role to play in the shift in the production pattern from expensive models to standard low-priced models which could be bought even by lower income groups. We would, therefore, commend this form of excise relief in respect of

consumer durables, especially for those which are now out of the reach of the poor and lower-middle class people on account of their high price. A case by case examination would, however, be necessary and the prime considerations in devising the concessions should be to provide reliefs in cases where the price reduction could be sizeable and the product would become cheaper. The benefit of cost and price reduction should in effect flow in favour of a significant proportion of the wage and salary earners as well as self-employed groups with fairly low incomes.

11.32 Since the basic consideration in providing an excise relief of the above kind is to make available a cheaper product to a larger cross-section of the people, in our view, the criterion to be applied should be value rather than physical specifications. For, when a concession is given based on value limits, the tendency on the part of the manufacturer would be to effect cost reductions and offer a utility model at a cheaper rate. On the other hand, when physical specification is the dividing line between products taxed at concessional rates and those taxed at full rates, the desired objective of lowering prices might not be achieved in as much as the producer could get the benefit of the concession even without effecting the much needed price reduction. With the result, the accent will be on production of luxury rather than utility models, which meet the criterion of physical specification.

OTHER CONCESSIONS

11.33 Often there are excise concessions given to encourage the use of non-traditional raw materials which would otherwise go waste as also concessions given to sustain and encourage labour-intensive techniques of production which have considerable relevance to our country. Such concessions are in principle purposeful and legitimate. Thus, reliefs given to paper produced out of agricultural wastes, to khandsari and handloom textiles, in our view, are well justified. It would, however, be necessary to ensure that such concessions are not excessive and do not lead to wasteful or uneconomic use of some other resources which are scarce. In deciding upon the nature and magnitude of concessions, a distinction should be made between cases where the desired objective is to stimulate a particular type of economic activity and those where it is merely to protect and ensure the survival of the existing units.

11.34 Apart from the types of excise concessions discussed above, a large number of other concessions which have been given to subserve diverse purposes have come to our notice. We do not propose to comment on them individually.. However, considering the vast number of the notifications including those which prescribe a different effective rate of duty from the tariff rate prescribed in the schedule, we are inclined to conclude that the instrument of excise concessions has, on the whole, been used with more liberality than would be justified if stricter standards were to be applied and if due consideration were to be given to other alternatives. Quite a number of exemptions have also been given under rule 8(2) of Central Excise Rules, 1944. The Venkatappiah Committee had a good deal to say on the subject of the considerations and objectives which should govern the grant of concessions. We do not by any means question the use of fiscal concessions when they are clearly needed to fulfil well-defined objectives that cannot otherwise be achieved with equal effectiveness. We would, however, venture to point out that there is a point beyond which their use for purposes of fine tuning of the economy may be counter-productive. Further, there is also the danger that some at least of the concessions continue to be enjoyed even when the circumstances which warranted their introduction have disappeared. A review of the existing concessions is clearly called for. However, it would be an impractical and time consuming approach to undertake a wholesale re-examination of all the existing concessions in one single exercise. It would be better to break up the task by reviewing first concessionary notifications which are more

than 5 years old. Further, if our proposed recommendations regarding the method of extending concession to the small scale sector are accepted, a large range of existing notifications would any how need to be scrapped or replaced. We would recommend that in future any exemptions granted should have a time limit appropriate to particular cases, but not exceeding five years, so that their review is automatically ensured.

11.35 Summing up, we feel that concessions in indirect taxes, which are intended to stimulate production and investment, should be looked upon as part of a comprehensive scheme comprising allowances under direct tax laws, credit facility on concessional terms, price-pooling arrangements, and liberal infrastructural facilities. Excise concessions cannot be regarded as an effective method for boosting production or encouraging investment in particular areas, though in respect of new units which are capital-intensive in nature as well as those which use resources that would otherwise go waste, such concessions could be helpful. Excise reliefs could be also used to encourage the production of low-priced consumer durables. However, the grant of excise concessions on a liberal basis should be avoided; every such concession should be justifiable on sound economic and social considerations.

CHAPTER 12

ENCOURAGEMENT TO SMALL PRODUCERS

12.1 EVOLUTION

Ever since Independence, Government have been emphasising the importance of what is generally referred to as the small scale sector in the industrial development of the country. The Industrial Policy Resolutions of 1948 and 1956 specifically recognised the important role of small scale industries, as will be evident from the following quotations from the Industrial Policy Resolution of 1956.

> "10. The Government of India would, in this context, stress the role of cottage and village and small scale industries, in the development of the national economy. In relation to some of the problems that need urgent solutions, they offer some distinct advantages. They provide immediate large-scale employment; they offer a method of ensuring a more equitable distribution of the national income and they facilitate an effective mobilisation of resources of capital and skill which might otherwise remain unutilised. Some of the problems that unplanned urbanisation tends to create will be avoided by the establishment of small centres of industrial production all over the country.
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> 11. The State has been following a policy of supporting cottage and village and small-scale industries by restricting the volume of production in the large-scale sector, by differential taxation, or by direct subsidies. While such measures will continue to be taken, whenever necessary, the aim of the State policy will be to ensure that the decentralised sector acquires sufficient vitality to be self-supporting and its development is integrated with that of large-scale industry. The State will, therefore, concentrate on measures designed to improve the competitive strength of the small-scale producer. For this it is essential that the technique of production should be constantly improved and modernised, the pace of transformation being regulated so as to avoid, as far as possible technological unemployment. Lack of technical and financial assistance, of suitable working accommodation and inadequacy of facilities for repair and maintenance are among the serious handicaps of small-scale producers. A start has been made with the establishment of industrial estates and rural community workshops to make good these deficiencies. The extension of rural electrification and the availability of power at prices which the workers can afford will also be of considerable help. Many of the activities relating to small-scale production will be greatly helped by the organisation of industrial cooperatives. Such cooperatives should be encouraged in every way and the State should give constant attention to the development of cottage and village and small-scale industry."

The new Industrial Policy (announced in December, 1977) not only continues the emphasis on the important role of cottage and small scale industries but it in fact envisages a pivotal place for them side by side with large industries.

12.2 Over the years, the small scale sector, as it is popularly called, has emerged as a major and distinct entity in our industrial economy. To encourage its growth, and to remove various

handicaps which it suffered from, like lack of financial and technical assistance, suitable working accommodation and marketing problems vis-a-vis organised manufacturers, both the Central and State Governments have initiated various non-fiscal measures. Several agencies, at the Central and State levels, like the organisation at the Centre headed by the Development Commissioner. Small Scale Industries the National Small Industries Corporation, and Small Scale Industries Boards at all-India and State levels, have been set up specifically to plan and implement policies and programmes for the development of the small scale sector. The new Industrial Policy envisages new agencies at district headquarters called 'District Industries Centres' which will provide, under one roof, all the services and support required by small and village entrepreneurs.

12.3 A special class of industries, identified as pertaining to the small scale sector on the basis of the value of the plant and machinery installed not exceeding a particular figure, was freed from licensing control under the Industries (Development and Regulation) Act. Instead of the Directorate-General of Technical Development being entrusted with the responsibility, Directorates of Industries were set up in each State (and Union Territory) to assist in the development of industries in general and small scale industries in particular. They look after their different needs and make special arrangement, for procurement of scarce raw materials, allocation of quotas, certifying import requirements, etc.

12.4 In the fiscal field, a large variety of concessions have been given to small producers but the criterion for eligibility of these concessions has been independently determined from case to case and is not the same as the one used for exempting from licensing control under the Industries Act what is widely referred to as the small scale sector. Our discussion in this Chapter, therefore, pertains to a range of small producers which are not identical with the small scale sector in the sense understood or defined for purposes of industrial licensing. The small producers enjoying fiscal concession are, broadly speaking, of two types. First of all, there are the traditional labour-intensive industries making minimal use of power and relying mainly on manual labour and skills, such as, handloom textiles and hand-made shoes. Secondly, there are industries which may be making use of modern technology to produce sophisticated products like transistor radios, but whose operations are on a much small scale.

12.5 Encouragement to the former is being given largely on the consideration that they are labour-intensive industries, having a much larger employment potential per unit of capital invested than modern industries. A special emphasis is being laid on their expansion by Government in recent months in the context of a time-bound programme to eradicate unemployment.

12.6 The latter type of industries, whose distinctive feature is that it can produce products similar to large scale industry on a much smaller scale, is being encouraged partly no doubt on considerations of its employment potential, but much more because it enables those who do not have large capital resources of their own but are otherwise capable of undertaking entrpreneurial functions, to enter the industrial arena. Such units can lead to a more decentralised pattern of growth, both regionally and in terms of ownership control and management, than large scale industries which tend to concentrate in the already industralised areas and to be dominated by those who are already well established in industry.

12.7 The basic disadvantage suffered by the smaller producers has been recognised to be the inadequacy of capital which they have, combined with little or no access to the capital market. The Central and State Governments have taken measures to extend institutional and governmental credits to them on liberal and often concessional terms. State Finance Corporations have been set up for financing the small scale and medium scale industries and to meet their long, medium and short term requirements, including at times the finance needed for the equity base of their projects. In addition, special schemes for the grant of loans on liberal terms to them through commercial banks, especially after the nationalisation of larger banks, have also been evolved. A separate wing has been set up by the Industrial Development Bank of India to deal exclusively with the credit requirements of small, village and cottage industries. Industrial Estates have been set up to provide suitable working accommodation as well as infra-structural facilities like electricity, water, transport and railway sidings and certain common facilities to the small scale sector so that they can start production without heavy initial investments for which they cannot muster the resources.

12.8 Other measures initiated to promote growth of smaller units include technical and advisory services and training facilities, supply of machinery on hirepurchase basis, special schemes to develop small scale units as ancillaries to larger undertakings, and marketing support by measures like price preference in the matter of Government purchases from small producers vis-a-vis the large scale manufacturers, and reservation for exclusive purchase by Government departments and public sector undertakings.

12.9 Apart from assistance provided to the small producers in these ways, a policy of protecting them from competition from the large scale sector, as envisaged in the Industrial Policy Resolution, has also been followed. For quite a number of items steps have been taken to limit production in the large scale sector either by preventing its expansion in those fields or by limiting or banning their production in the large scale sector. A range of items were selected for exclusive development in small scale sector and no expansion or setting up of new organised industries was allowed for these products. The list of items which are reserved for the small scale sector has been gradually expanded. The new Industrial Policy accords special importance to this approach of promoting growth of small and cottage industries as may be seen from the following extract:

> "It is the policy of the Government that whatever can be produced by small and cottage industries must only be so produced. For this purpose an exhaustive analysis of industrial products has been made to identify those items which are capable of being established or expanded in the small scale sector. The list of industries which would be exclusively reserved for small scale sector has been significantly expanded and will now include more than 500 items as compared to about 180 items earlier..... An annual review of the reserved industries will be undertaken in order to ensure that reservation accorded to the small scale sector is efficient and is also continually expanded as new products and new processes capable of being manufactured in the small scale sector are identified."

12.10 The fiscal concessions to small producers are also primarily aimed at providing protection to them from the large scale sector which pays various indirect taxes at higher rates. Industries employing traditional techniques which provided a large amount of decentralised employment and which stood in danger of being wiped out by competition from highly mechanised productive units in the large scale sector located in metropolitan cities or in the major industrialised urban centres of the country, were

FISCAL CONCESSIONS TO SMALL PRODUCERS

protected by exempting them from excises, or by subjecting them to a lower duty than levied on units in the organised sector. Following the exemption granted to the handloom industry in 1948, more traditional items like hand-made shoes, hand-made biris, khandsari manufactured without the aid of power or machines, were given a similar concession. Quite a number of exemptions were given in the past not to help the small producer as such, but with a view to reducing the administrative costs and inconvenience of taxing very small units, e.g., exemption to non-power operated soap manufacturers. Apart from exemptions intended to encourage labour-intensive techniques or reduce administrative burden, excise duty exemptions - partial or complete - have also been given to particular industries in more recent years in order to foster the growth of smaller units.

12.11 As different criteria were used in selecting industries and as the quantum of benefits extended in different industries also varied, the excise tariff at present contains a very large number of exemptions which are generally meant to assist and encourage the growth of small industries. We refer to some of them below.

(i) For administering the various programmes of assistance, sometimes units are classified on the basis of investment in plant and machinery; industrial units having investment in plant and machinery not exceeding Rs. 10 lakhs are termed to be small scale units. This criterion has been adopted in certain cases for extending excise duty benefits also. Thus, at present, we have partial exemptions for manufacturers of wires and cables, and complete exemption for certain types of plastic films and lay-flat tubings if the investment in plant and machinery in the units concerned does not exceed Rs. 10 lakhs. In certain cases (like electric bulb units), however, exemption from excise duty is granted only if investment does not exceed a lower specified limit (of Rs. 3 lakhs).

(ii) There are cases where concessions are based upon the criterion of number of workers employed. Thus, a total exemption has been provided to footwear units employing not more than 49 workers, as also manufacturers of electric battery or its specified parts provided they do not employ more than 5 workers.

(iii) A large number of exemptions are based on the value of clearance. In some industries, a duty free slab is allowed (which varies) or partial exemption is provided in a financial year if the value of clearances in that year (or in the preceding year in some cases) does not exceed specified limits. In a number of cases, such as, tooth paste, motor-starters, safes and strong boxes, rolling bearings, metal containers, zip fasteners, playing cards, carbon black, etc., complete exemption is extended upto Rs. 1 lakh in value of goods; the exemption being available provided the total value of the clearance of a unit in the year does not exceed Rs. 2 lakhs. There are cases where this upper limit has been fixed at a higher level, such as, in the case of tapioca starch, where it is Rs. 5 lakhs per annum. There are other cases (e.g., bolts and nuts) where the first Rs. 5 lakhs of value of goods is allowed duty free clearance.

(iv) Similar to concessions based on value, there are concessions based on the quantum of clearances in any year, e.g., in the case of compounded lubricating oils

and greases, 100 metric tonnes are allowed duty free clearance, provided the total clearances in the year do not exceed 400 metric tonnes.

(v) There are other concessions, such as, allowing certain quantitative clearances duty free or on partial payment of duty, subject to a number of conditions being satisfied. Thus, the first 75 kilogrammes of cosmetics and toilet preparations, of which face powder should not exceed 20 kilogrammes, cleared in any month by a manufacturer are completely exempt, provided the production of cosmetics and toilet preparations of the manufacturer did not exceed 200 kilogrammes in any one of the twelve months, or 2000 kilogrammes during the 12 months immediately preceding the month in which the clearance is made.

(vi) Then there are exemptions based upon power criterion. Thus no duty is chargeable on footwear produced by units employing 2 horse-power or less. There are a large number of industries where complete exemption is granted if no power is used, e.g., confectionery, starch, various kinds of yarn, paper, steel furniture, bolts and nuts, grinding wheels, insulation tapes, paints and varnishes, aerated water, khandsari, soap, safes and strong boxes, metal containers and vegetable non-essential oils. There are also exemptions depending upon the kind of power used, for example, vegetable non-essential oils, if manufactured with the aid of water power, are exempt.

(vii) There are concessions extended on the basis of installed capacity, e.g., in the case of smaller paper mills having installed capacity not exceeding 10,000 tonnes per annum, varying exemptions have been provided for different installed capacities.

(viii) There are a number of instances where variations of the above principles have been applied, for example, concessions which are based on value of clearances linked with investment criterion. Thus, in the case of certain specified tools, polishes and creams and electric lighting fittings, for units where total investment in plant and machinery does not exceed Rs. 10 lakhs per annum, the first clearances upto specified limits (5 lakhs or 10 lakhs) are exempt. In certain other cases, these exemptions have been extended subject to a further ceiling on overall clearances. For example, in the case of goods classified under item No. 68, complete exemption to clearances upto Rs. 30 lakhs is extended to a unit whose capital investment in plant and machinery does not exceed Rs. 10 lakhs and whose total clearances of all the goods in the preceding year did not exceed Rs. 30 lakhs. In the case of paints and varnishes, if the investment in plant and machinery does not exceed Rs. 10 lakhs, the clearances upto first Rs. 2 lakhs are completely exempt, subject to overall clearances not exceeding Rs. 15 lakhs; otherwise, the first Rs. 50 lakhs' clearances are allowed a concessional duty benefit of 2 per cent, subject to overall clearances not exceeding Rs. 1 crore.

12.12 The case for fiscal preference in the form of excise duty concessions to small scale sector has been examined several times and by several Committees/Commissions in the past.

Most of them have accepted in principle the case for extending excise duty relief as a measure of protection to small scale sector vis-a-vis organised units as well as to encourage their growth. The TEC had recognised that the small producers suffered from higher cost of production and had relatively lower ability to bear taxes. It conceded the use of excise concessions to remove these handicaps as also to encourage labour-intensive methods which promoted greater employment. The following observations are of interest:

> "From the point of view of the Indian economy, there is a strong case for the special encouragement to small scale and cottage industries. The tax system may be used for this purpose but in a judicious manner. We would suggest a periodic review of the working of these concessions so that policy in this respect may keep in step with the changing needs of the economy."*

12.13 The Industrial Policy Resolution, 1956 as mentioned earlier, and also various Plan documents, enunciated that differential taxation should be used as one of the methods to encourage the proper growth of cottage, village and small scale industries. Even though the Chanda Committee argued against the grant of any fiscal preference to the small scale sector in the form of excise duty concessions, it had impliedly accepted the need for protection to this sector when it advocated the grant of direct subsidies. Recently, the Venkatappiah Committee had occasion to consider the various exemptions to the small scale sector in a comprehensive manner. It also accepted the case for fiscal preference to the small scale sector but simultaneously recommended that the existing scheme of concessions should be replaced by a more simplified and uniform scheme of benefits in order that the existing exemptions, whose administration had become complicated, were not abused or allowed to cause distortions.

12.14 During the course of oral evidence as well as in the various written replies to the questionnaire, it has been represented to us, both by the small-scale industries associations (at all-India and regional levels) as well as the Development Commissioner (Small Scale Industries), that there is a strong justification for encouragement of small scale sector through grant of excise duty concessions. While enumerating the various advantages of small-scale sector as compared to organised units, such as, higher dispersability, diffusion of entrepreneurship and decentralisation of economic power, generation of more employment per unit of investment and higher productivity for the same capital base, it has also been pointed out that smaller producers suffer from various disabilities and disadvantages which hamper their growth and make it difficult for them to compete with the larger manufacturers. It was argued that despite various efforts made by Government, the smaller units continued to suffer from paucity of overall financial resources, that their cost of production is higher than that of organised units due to higher price paid by them for most of their inputs and relatively less advanced techniques of production and various other factors; that they have a limited market and that their products fetch much lower price due to lack of any established name or sophisticated marketing techniques; that they receive delayed payments from customers; and that the severe competitions from larger unit compel them to sell their products at comparatively lower prices leaving a very small margin of profit. Even where smaller units function as ancillaries, larger manufacturers demand quality but pay only the lowest price reducing the margin of profit of the smaller producers. To offset these disabilities, it has been contended that the small-scale sector deserves further liberalisation of excise concessions apart from the assistance in other form.

12.15 An opposite view has also been expressed to us, namely, that the differential treatment in the matter of taxation for different sectors within the same industry should be avoided since it upsets

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*Report of the Taxation Enquiry Commission (1953-54)
Volume II, Chapter VI, Para 67, p. 314.

the economic equilibrium between them and also provides no encouragement to grow or become efficient. It may also lead to wasteful use of scarce resources. It is argued that measures, such as, concessional finance or cash subsidies, marketing assistance and infrastructural facilities, should be preferred to giving relief from excise duties.

12.16 We feel that the situation is not one which can be viewed as presenting a choice between fiscal concessions, on the one hand, and alternative ways of helping the small scale sector on the other. The question perhaps is one of evolving an appropriate blend of policy measures to ensure that the smaller industrial units derive and retain adequate dynamism. There is every justification to encourage their growth, especially in a developing country like ours where there is mass scale unemployment and capital is scarce. Though it would be advantageous to lay greater emphasis on measures other than taxation to encourage the growth of the small scale sector purely from the revenue angle, a factor that is to be reckoned with is that wherever there is a cost disadvantage to be overcome, a measure of protection through differential excise duties is as legitimate for the smaller producers as protection through import tariff is for an industry as a whole. The considerations of diffusion of entrepreneurship, regional dispersability, possibilities of using techniques of production which can flourish in rural surroundings and other objectives of social and economic policy, would fully justify special encouragement to smaller producers, some of whom may make use of traditional techniques and some, of the more modern equipment. A differential excise on them as compared to large-scale factories can afford them a kind of tariff protection, just as protective import duties shelter even the largest units in the country from foreign competition.

12.17 While making use of the tax system for achieving this purpose, a number of factors will have to be borne in mind. Fiscal concessions should be an adjunct to, rather than a substitute for, a positive well thought-out policy for developing decentralised production. The industries having potential for growth and new avenues of employment would certainly deserve fiscal concessions, but they should be such as may be judged necessary and supplemented by other measures to improve quality, design and marketing facilities so as to avoid over-dependence on fiscal benefits. We find that in the new Industrial Policy the emphasis is, rightly in our view, on non-fiscal measures.

12.18 While it is justifiable and desirable to provide tax concessions to offset the cost disadvantages which have been discussed in detail earlier, care has to be taken to ensure that the concession extended is not excessive. Otherwise, there would not only be an unnecessary loss of revenue but also a tendency for the concessions to attract a class of producers for whom they were not intended.

RATIONALISATION OF THE EXISTING EXEMPTIONS FOR SMALL SCALE SECTOR

12.19 One aspect of the existing scheme of concessions intended to benefit the small-scale sector which has come up for particular criticism in the past as well as voiced to us, in response to our questionnaire, is that the criteria adopted for granting concessions vary widely from product to product. The present scheme of exemptions causes administrative complications and gives rise to opportunities for malpractices. Sometimes the criterion not only does not foster the growth of the small scale unit but comes in the way of their development.

12.20 After going into the matter, we have come to the conclusion that the existing scheme of concessions need to be rationalised. The two major areas in the matter of concessions to small-scale

units which need review are :(i) the criteria which should be applied for the grant of concessions and (ii) the extent of concessions which should be given.

12. 21 The varied criteria followed at present for extending concessions to the small-scale sector, as briefly enumerated earlier, suffer from many weaknesses. The concessions related to the value of quantum of clearance in a financial year, as at present applied, come in the way of higher production because the moment the clearances exceed the specified limit, the concessions are withdrawn not only in respect of future production, but in most cases, also in respect of what might have been produced earlier in the same financial year and sold without providing for payment of excise. This not only causes hardship to genuine producers but also encourages the tendency to suppress production or to have recourse to fragmentation in order to avail of the benefits. Exemptions based upon the criterion of the number of workers employed discourage more employment. Even if one worker in excess of the prescribed maximum is employed, even for one day, the unit loses the concession. Thus, the concession intended to promote employment actually discourages expansion. Concessions based on power criterion are liable to abuse as the producers try to get part of the manufacturing process needing power done from outside their units. Those based on investment criterion are also not very rational as with the same investment the value of outturn could vary from industry to industry. It also encourages fragmentation. In our view, the value of production of a unit would be the most rational basis for granting concessions to smaller producers and it should generally replace the diverse criteria applied at present. The concessions should, however, be given on a slab system to minimise avoidance and mitigate hardship to the producers on the border line between the small and organised sectors.

12. 22 In our view, there should be a total exemption from excise upto a certain value of production; any excess over it should be taxed at a concessional rate subject to an upper limit; and if the production rises above that limit the excess should be made liable to the normal rates. If, in a given year, the production reaches a sufficiently high level, the producers should be subject to the normal rate of taxation from the following financial year.

12. 23 What should be the value limit for the different slabs or what excise concessions should be given to different industries are questions which may not admit of a general answer. In certain industries the value of production may be very large because of high cost of components and the actual value added by the units may be much lower. Though the 'value added' may be an ideal criterion for granting exemption to smaller units, it would not be administratively easy to implement. As an alternative, the value of production of a unit (which for administrative purposes could better be related to the value of clearances in a year as is generally done even now) may be the next best answer. To take care of the peculiar methods of production/assembly by smaller units in different industries there could be a case for differential slabs for groups of industries, depending upon the value added and other relevant factors.

12. 24 However, as a general approach we consider that a particular value limit could be fixed as a dividing line between a small producer and others for the purpose of granting excise concessions. To consider what should be the general cut-off point we looked into the pattern of production of the small scale sector as compiled by the Central Statistical Organisation. The latest available figures for the year 1975-76 indicate the following pattern of production by units in the small scale sector having different capital investment.

TABLE - PRODUCTION PATTERN BY SIZE OF CAPITAL

Capital range (gross value of plant and machinery)	No. of factories	Output
(Rs. lakhs)		(Rs. lakhs)
Upto 1.0	33596	236358
1.0 - 2.5	11013	166011
2.5 - 5.0	5724	129189
5.0 - 7.5	2582	86953
7.5 - 10.0	1459	63782
Total for small scale sector (upto Rs. 10 lakhs)	54374	682293

Source.— Annual Survey of Industries, 1975-76, Summary results for factory sector, Central Statistical Organisation, Department of Statistics, Ministry of Planning.

12.25 From the above table, it will be seen that the average value of output of a small scale unit having investment in plant and machinery not exceeding Rs. 10 lakhs in 1975-76, was about Rs. 12.6 lakhs per annum. Having regard to the growth since 1975-76 we feel that, in general, units whose value of clearances in the previous financial year did not exceed Rs. 15 lakhs could be made eligible for concessional treatment in the matter of excise levy.

12.26 While recommending this ceiling of Rs. 15 lakhs, we have also been guided by the results of our study of the industry wise pattern of clearances and duty paid by units having different outturn ranging from those having outturn not exceeding Rs. 1 lakh per annum to those having outturn exceeding Rs. 15 lakhs per annum (barring certain types of units like those completely exempt or working under compounded levy schemes). The details of the study are given in Appendix 17. It may be seen from this study that the number of units under the excise net having clearances not exceeding Rs. 15 lakhs per annum accounted for about 81 per cent of the total number of units in all the industries (with few exceptions not covered in the study), but they contributed less than 3 per cent of the total duty realised from these industries. The ceiling of Rs. 15 lakhs should, therefore, provide relief to a large portion of the total number of units under excise control, without making, at the same time, any serious dent on Government's revenue.

EXTENT OF CONCESSIONS

12.27 As for the extent of concessions which may be extended to the smaller eligible units, opinions could differ. The small scale industries associations have pleaded for complete exemption or substantial relief in duty to units in which investment on plant and machinery does not exceed Rs. 10 lakhs or upto a very high value of production if concessions are given on a value basis. The Development Commissioner (Small Scale Industries) was inclined to favour

concessions on value criterion on a slab basis, through a scheme in which certain initial clearances could be completely duty free and concessional duties on a graduated scale charged on the rest, so long as the total clearances do not exceed a prescribed limit.

12.28 We observe that in quite a number of industries (such as, tooth paste, motor-starters, rolling bearings, welding electrodes, zip fasteners etc.,) the small scale units are allowed duty free clearances upto Rs. 1 lakh per annum if their outturn in the year does not exceed a prescribed maximum. Taking into account the price rise since 1972 when the duty free slab of Rs. 1 lakh was first introduced for smaller producers in certain industries, there seems to be a good case for raising this value limit.

12.29 We find that on the Income-tax side the Department insists on the maintenance of certain accounts only if the value of transaction exceeds certain limits. Under section 44AA of the Income-tax Act, this value limit has been fixed at Rs. 2.5 lakhs per annum. We consider that this value limit could be adopted while considering the grant of excise duty concessions to the small scale sector. In other words, the first clearances upto Rs. 2.5 lakhs could be exempted fully for all units eligible for concessional treatment in an industry (that is, whose clearances in the preceding year did not exceed Rs. 15 lakhs).

12.30 It has been put to us that in a number of industries there is what may be called a 'tiny sector' consisting of a large number of small units having low capital investment as well as low annual outturn and it may be neither desirable nor worthwhile to keep any administrative control over such units. The new Industrial Policy also envisages giving special attention to tiny units (defined as those with investment in machinery and equipment upto Rs. one lakh and situated in towns with a population of less than 50,000 according to 1971 census figures and in villages). We do not favour, for reasons indicated earlier, concessions based upon investment criterion. We are, however, confident that complete exemption upto Rs. 2.5 lakhs value of goods will give very substantial relief to most of the tiny units in the small scale sector — if not exempt them from duty altogether. The exemption limit of Rs. 2.5 lakhs will also help in reducing the control over the smallest units which are free from the documentation requirements also under the Income-tax law. As for the duty to be levied on clearances of a unit in excess of Rs. 2.5 lakhs, we would recommend that clearances upto Rs. 10 lakhs could be charged to a concessional rate of duty and the amount in excess of Rs. 10 lakhs, charged to the normal rate of duty paid by the organised units.

12.31 We may now examine as to what concessional rate (or rates) may be made applicable for clearances in the value slab of Rs. 2.5 lakhs to Rs. 10 lakhs. The various disabilities suffered by small producers vis-a-vis organised units are not easily quantifiable. It would require a detailed analysis of costs as well as marketing arrangements in respect of products manufactured by small producers in any industry and their competitors in the organised sector, even if the intention is merely to neutralise the cost and other disadvantages of small producers. We have not gone into these details but consider that both as a measure of protection and encouragement for the growth of small producers, a concessional rate of duty, which may be lower by 3 percentage points as compared to the effective rate of duty payable by the organised units, for the value slab of Rs. 2.5 lakhs to Rs. 10 lakhs, should prove adequate for most of the industries. As seen from Appendix 17, the average incidence of excise duty borne by the products of all the industries taken in the study, produced by the bigger units (having an annual clearance exceeding Rs. 15 lakhs per annum), was around 16 per cent

ad valorem. A 3 percentage point reduction means, therefore, on an average, a relief of about 20 per cent of the average rate of duty levied on organised units. For a unit with an annual outturn of Rs. 10 lakhs, our proposals would give a benefit of about Rs. 62, 500 in duty, as compared to the average duty liability of Rs. 1.6 lakhs for organised units having the same outturn. In other words, the total benefit will be even more than one-third of the normal duty liability.

12. 32 Though we believe that the general approach, recommended above, should provide sufficient incentive to small units in most industries, there could be cases where different degrees of concessions may have to be given to small producers, e.g., in electronic industry, where the value of outturn is generally high due to the very substantial value of the components. Further, liberalisation in such cases could be considered if a case is made out for the same by the concerned units. We would also like to add here that we have avoided suggesting concessions to small producers as a certain percentage of the normal duty chargeable from organised units, as it only tends to encourage unintended bias in favour of small producers manufacturing high-rated luxury items.

12. 33 With the introduction of the concessions based on the value of production as indicated above, it would also be imperative that the existing concessions based on various criteria are withdrawn.

APPROACH TO EXISTING CONCESSIONS

The approach may have to be, however, different where at present complete exemption is granted to certain sectors of industries generally based on non-use of power. In the latter types of cases we have heard views on either side. Whereas some have suggested that there should be no differentiation between power-operated and non-power-operated sectors in the matter of grant of fiscal concessions, other have suggested continuance of the special treatment to non-power-operated sector wherever it exists for the present. In our view, though in the long run one may have to think of removing concessions based on this distinction and replacing them by those based on value of production, to fall in line with our general recommendation, a cautious approach may be needed in this regard as, apart from the administrative considerations, the fact that the exempted non-power sectors generate considerable self-employment and consist of mostly traditional sectors, cannot easily be ignored. A case by case review could be made and where there is a tendency to any significant abuse of the existing complete exemption, or serious distortions in the pattern of production between the different sectors of the industry, the withdrawal of the complete exemption and its replacement by the general scheme outlined above could well be considered.

12. 34 The scheme of simplified procedure of assessment for small producers (referred to in Chapter 2) is at present applicable to 46 industries. We find that the existing scheme confers differential benefits to smaller producers covered by the different industries under the scheme and could operate in a way which discourages their growth. Thus, in almost 50 per cent of the industries covered by the scheme (e.g., sodium silicate, dye-stuffs, patent or proprietary medicines), where there were no specific concessions for small producers prior to the introduction of the scheme, the benefit available is 10 per cent of the duty paid by organised units. For other industries under the scheme, the benefits vary — being substantially higher than 10 per cent — especially where duty free clearances are allowed upto certain value limit for calculating compounded

CONCESSIONS TO INDUSTRIES WORKING UNDER SIMPLIFIED PROCEDURE

duty liability. Thus, a bolt and nut manufacturing unit is completely exempt under the scheme if its base clearance does not exceed Rs. 5 lakhs, as prior to the introduction of the scheme such an exemption was available, which is now taken into account for calculating duty liability under the scheme. A number of suggestions to modify the scheme were received by us from various quarters including the Development Commissioner (Small Scale Industries). We ourselves made a review of the working of this scheme and briefly discuss our findings in the following paragraphs.

12.35 The Venkatappiah Committee had felt that while there may be need for concessions in favour of the small scale sector, the schemes in force failed in many ways to subserve the objectives underlying them. The administration of schemes of concessions for the small scale sector based on various criteria had, in that Committee's view, become complicated and the need for its simplification was imperative. It felt that this could be achieved —

> "(a) by identifying that part of the small scale sector-to one specifically characterised by complicated exemptions - which presents these problems in special degree; and
>
> (b) by devising for the segment of the small sector so identified, in place of the existing plethora of exemptions, an appropriate procedure of duty relief. This procedure may take the form of either straight exemptions and/or introduction of lower rate of duty than that applicable to the rest of the commodity concerned."*

12.36 For identifying the relevant segment of the small scale sector, the Venkatappiah Committee felt that for commodities which have a relatively large number of small producers and in which the composition of the industry or the duty structure or other relevant considerations do not militate against such classification — the duty paying units could be classified on the basis of their value of production. An appropriate cut-off point could be fixed and all producing units below the cut-off point should be considered small for the purpose and brought under a simplified form of control. The Committee felt that it would be simpler and more appropriate to adopt a single cut-off point at Rs. 5 lakhs in respect of the commodities which were identified for consideration of the simplified procedure. The essential features of the scheme of simplified procedure as contemplated by the Venkatappiah Committee were as follows.

(i) The scheme was to apply to such commodities as were notified and all existing schemes of duty exemption applicable to small units in the industries producing such commodities would be replaced by a single lower notified rate having regard to the average duty incidence borne by the entitled sector, the extent of fiscal concession warranted, and such other factors as may be relevant. They will be appreciably lower than the normal rates.

(ii) The duty liability of each unit will be related to the average value or quantum of duty paid clearance during the preceding three years or last year, whichever is higher. The liability of each unit will then be worked out in terms of the existing tariff structure (including duty exemptions where admissible and to the extent admissible) and also on the basis of the effective rate of duty notified by the Government for such producers. The lower of the two quanta so worked out would be treated as prospective annual liability.

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*Report of the Central Excise (Self Removal Procedure) Review Committee - Volume I, Chapter 14, para 4 (pp. 84-85).

(iii) The liability arrived at (in terms of the preceding para) would be treated as his annual liability for the three succeeding years — it will be realised in equal monthly instalments payable by him in advance before the commencement of each month in such manner as may be prescribed by the Department. Each 3-year period for which duty liability is fixed on a prospective basis will be treated as a single block.

(iv) The prospective liability so fixed will not be altered unless there is a change in the effective duty incidence applicable to the commodity concerned, in which case, the liability fixed would be suitably adjusted to take into account the change made. No extra liability would be attracted for exceeding the cut-off point or the value of production notified in any of the 3 years for which liability is fixed nor would any abatement of duty be allowed for any temporary break-downs or cessation of work. But where a unit closes down or goes out of production altogether, its duty liability would cease from the month following that in which the closure takes place.

(v) For new eligible units, appropriate provision will be made so that they do not suffer vis-a-vis existing units. For one year they would work under physical control after which — if their clearances did not exceed notified cut-off points - they would be brought under the scheme of simplified control for the remaining block period.

(vi) For a statistical purposes even units manufacturing goods which are actually exempted from duty or whose duty liability is fixed at 'nil' should also be covered by the simplified procedure irrespective of the value of the goods produced or cleared subject to the difference that the duty liability in respect of such goods would continue to be nil.

(vii) For the class of producers covered by the scheme, all procedural formalities other than those concerned directly with or having a bearing on determination of their continued eligibility were to be eliminated. Such units could thus be required to maintain only a simple day-to-day record of production and clearances, both in terms of value and quantity, effect clearances on simplified gate passes and submit a monthly or quarterly return.

12.37 The Venkatappiah Committee recommended the above simplified procedure as an experimental measure and suggested that not later than 5 years after its introduction, the whole scheme should come up for a review. The scheme was to be applied on a voluntary basis. However, any small unit, which although eligible for the scheme but does not opt for it, will have to be placed under full physical control. The Committee's expectation was that because of its various attractive features, almost 95 per cent of the entitled small units should opt for the simplified procedure.

12.38 The recommendations of the Venkatappiah Committee were carefully considered by Government and a scheme of simplified procedure of duty payment for smaller units was notified in respect of 46 commodities (listed in Table 2 appended to this Chapter) to be effective from 1st March, 1976. Though the scheme as notified by Government mainly followed the recommendation of the Venkatappiah Committee, it made the following important deviations.

(i) Instead of fixing the lower notified rates taking into account the various considerations mentioned by the Venkatappiah Committee, an ad hoc formula was adopted under which for the entitled sector the notified rate was to be 10 per cent lower than the normal rate applicable to the relatively bigger units. (Where there already existed certain concessions for smaller units in some industries, the units were made eligible to avail of these concessions while working out their duty liability, if that worked out to be more favourable to them than the 10 per cent duty cut allowed otherwise).

(ii) Though the Committee had recommended no change in duty liability once fixed on the basis of the unit's past production, irrespective of the actual production during the current year, it was considered that this might lead to a large risk to Government revenues and also create anomaly between units whose annual production is less than Rs. 5 lakhs in value and those whose production is more during the base period. The Committee's recommendations were, therefore, accepted with the following reservations.

(a) Once the duty liability of a small unit has been fixed on the basis of its performance, such a unit would be allowed to clear excisable goods the value of which does not exceed more than 50 per cent of the average value or the quantum of duty-paid clearances in the past 3 financial years or the last year, whichever is more.

(b) In cases where limits indicated in (a) above are exceeded but the increase is not abnormal (which was taken to mean 100 per cent of the base), then at the end of the year in which the excess occurs, the duty liability of the unit for the remaining portion of the 3-year block, if any, will be recalculated and refixed. In case clearances exceed by 100 per cent or more of base clearances, the units would be made ineligible for the scheme and brought under physical control, even if its final clearances were well below Rs. 5 lakhs. (The last provision has since been modified.)

(iii) Though the Committee had recommended withdrawal of all schemes of duty exemptions for smaller units after the introduction of the scheme, they have been continued. However, according to a provision made in the scheme, if a unit does not opt for the scheme, it cannot avail of any concession granting full exemption in a year to clearances of specified quantities or value of goods. Concessions based upon other criteria — partial or full (e.g., for non-use of power or for employing specified number of workers) — are available if the unit eligible for the scheme opts out and works under physical control.

12.39 To help us review the working of the simplified procedure, all Collectors of Central Excise were addressed and requested to give their considered views about the scheme, the reasons for a number of units not opting for the scheme, and the changes or modifications which may be considered necessary and desirable to make the scheme administratively more convenient and readily acceptable to the smaller producers. They were also requested to send detailed statistics about the units which were eligible for the scheme, those which had opted for it, and those which had not. The commodity-wise data based on Collectors' reports is given in Table 2 appended to this Chapter.

12.40 The following facts stand out from a perusal of the statistical data given in the above-mentioned Table.

(i) As on 1st January, 1977, there were in all 10637 units working under the simplified procedure, while 3670 units, though eligible, preferred to work under physical control.

(ii) Out of 10637 units which opted for simplified procedure, 7578 (i.e., more than 71 per cent) units were not paying any duty — being in the exempted category due to the benefits of exemptions existing prior to the scheme which were continued after its introduction for calculating a unit's duty liability. Only 3059 units were paying duty under the simplified procedure.

(iii) As most of the units which were exempt had opted for the scheme, the number of units paying duty under the scheme on monthly basis (i.e., 3059) is less than the number of units (i.e., 3670) which, though eligible, preferred to work under physical control and were paying duty at the time of individual clearances only. In other words, the response to the scheme has not been very enthusiastic.

(iv) The duty paid on an average by a unit working under the simplified scheme was about Rs. 1030 per month, while that by a unit working under the physical control (though eligible for the scheme) was lower (about Rs. 750 per month). It appears, therefore, that the existing concessions allowed under the scheme are inadequate and apparently affect adversely units if they pay duty under the scheme.

(v) The total duty paid by all units eligible for the scheme whether working under the scheme or under physical control, was only about Rs. 5.3 crores in 9 months (i.e., about Rs. 7.1 crores per annum), though it covered about 14300 licensees. (This of course did not cover some new units).

(vi) For only 379 units working under the scheme (i.e., about 2.6 per cent of the total) the production in nine months was 50 per cent higher than the base clearances. (Their duty liability had to be re-worked after the end of one year).

(vii) For 223 units the production in 9 months (April-December 1976) was 100 per cent higher than the base clearance due to which these units were denied the benefit of the scheme and brought under physical control.

12.41 It is thus clear that on the whole there has not been as much response to the scheme as was anticipated by the Venkatappiah Committee as well as by Government. The broad reasons for this poor response which were specifically brought to our notice by the departmental officers as well as trade and industry, are briefly summed up below-:

(a) The legal provisions of the simplified procedure scheme are not only difficult for the assessees to understand but sometimes too complicated even for the assessing officers.

(b) The three-year block period for which duty liability is fixed is too long, since it is very difficult for smaller units to forecast the demand and their production for such a length of time.

(c) the requirement of the advance payment of the tax (that is, six days before the commencement of the month) also places a strain on the financial position of the producer.

(d) The inadequate relief which the scheme provides in many cases has resulted in a situation where the duty liability of some assessees actually works out to be more than what it would be if duty is paid on every clearance.

(e) There is no provision in the scheme for exemption from duty when there is no production due to unavoidable circumstances, such as, lay-off,strikes, power break-down, etc.,

12.42 Basically, the simplified procedure scheme has much to commend itself. If appropriate modifications are made in the scheme there is no reason why it should not find greater acceptance by the small scale sector. The scheme as it was recommended by the Venkatappiah Committee appears much more simple. However, in an attempt to avoid all possibilities of abuses and unintended loss of revenue and to take care of all eventualities, while drafting the relevant legal provisions the scheme became complicated and difficult to understand not only by the assessee but even by departmental officers. We would recommend that the scheme should be made more simple and attractive and its scope extended. There is a case for liberalisation of the existing concessions to units eligible for the scheme as also for procedural simplifications. We would suggest the following changes in the scheme.

(1) Modifications in the scheme in the matter of grant of concessions be made to conform to the general approach recommended by us for giving concessions to smaller producers on value n slab basis. Thus, we would suggest that all units whose annual value of goods manufactured or likely to be manufactured (determined as per the scheme) does not exceed Rs. 10 lakhs per annum should be made eligible for the scheme, as against the present value limit of Rs. 5 lakhs. Further, the duty liability of the eligible units of any of the industries under the scheme should be calculated on a uniform basis under which for the first Rs. 2.5 lakhs value of the base there should be no duty, and for the value slab in excess of Rs. 2.5 lakhs and upto Rs. 10 lakhs, the rate of duty chargeable should be 3 percentage points lower than the normal duty applicable for the organised sector.

(2) As far the procedural simplifications, we would suggest the following:

(i) The notification which contains the various provisions of the scheme should be simplified and a version of it, which should be in non-technical language, be made available to make it easily understandable to the departmental officers as well as the assessees.

(ii) There should be a concerted attempt to educate the smaller manufacturers about the attractive features of the scheme, both by the Department and the Chambers and Associations of small scale industries.

(iii) The three-year block period for which the duty liability is fixed is, in our opinion, too long; Government should consider whether the period could not be shortened.

Under the French forfait system (which we discuss further in the Chapter on Value Added Tax and which Venkatappiah Committee appears to have relied while recommending this procedure), the duty liability is revised every two years while in the Brazilian forfait system the revision is made annually.

(iv) If the period for which the duty liability is fixed is reduced, Government should also consider whether there is any need for revision of the duty liability within the block period whenever the value of production of the units exceed by 50 per cent of the base value, as at present, so long as the producer remains eligible for the concession.

(v) The provision requiring advance payment of duty a week before the start of the month should be withdrawn. To help the financially weak smaller producers it may be generally provided that the duty could be paid within seven days of the commencement of the month.

(vi) A provision should be made for a downward assessment if there is a steep decline in production, not purely accounted for by seasonal factors; for example, in cases of shut downs for a period exceeding say, one month, due to reasons beyond the control of the assessee.

12.43 These changes in the quantum of admissible benefits and the procedural aspects of the scheme should, in our view, attract most of the eligible units under the scheme and make it more rational and growth-oriented. On the basis of our study of the pattern of clearances (given in Appendix 17) and the present effective rates, our recommendations may mean conferring additional benefits, roughly estimated at Rs. 15 crores per annum. This cannot be regarded as a large sum if one considers the fact that it would benefit about 17000 small producers (who may become eligible for the scheme under our proposals) and result in a substantial reduction in administrative burden for the department.

12.44 As stated above, the simplified procedure scheme is at present applicable only to a limited number of industries. It has been represented to us that the scheme should not only be liberalised but extended to almost all industries. The pattern of clearances in different industries, given in Appendix 17, indicates that in a number of other industries also production takes place in the decentralised sector, but no relief is extended to smaller producers in these cases. We feel that there is little justification to limit the benefits meant for smaller producers to selected number of industries and would recommend that the scheme should be extended — if necessary in phases — to all commodities with few exceptions (e.g., tobacco, petroleum products, matches and goods falling under a tariff item No. 68).

TABLE : SIMPLIFIED PROCEDURE - CERTAIN RELEVANT DATA

(Figures of value and duty are in Rs. 000)

Item No.	Name of commodity	No. of units which are working under the simplified procedures (as on 1.1.1977)		No. of units out of col. (3) which have opted only after 8th March, 1976.	No. of units which are eligible for simplified procedure but which have preferred to work under physical control (as on 1.1.77)	Base value of annual production in respect of units in col. 3 taken for determining their duty liability.	Amount of duty realised from units under col. 3 during the period April-December, 1976.	Value of clearance of units in col. 5 in April-December, 1976.	Amount of duty realised from units under col. 5 during the period April-December, 1976.	No. of units in col. 3 whose clearance, in April-Dec'76 have already exceeded 50% of the average of last three years of last year whichever is higher.	No. of units for which the clearance in April-Dec. 1976 exceeded 100% of their average of last three years or last year whichever is higher and who have been brought under physical control.
		Those which are not paying any duty	Those paying duty								
(1)	(2)	3(a)	3(b)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
..	Khandsari Sugar	1	8	1	10	1459	178	463	172	-	-
1A	Confectionery	280	17	30	7	8363	48	803	-	27	1
1B	Prepared or Preserved Foods	290	91	48	50	14031	354	5294	367	11	5
1C	Food products	141	27	43	19	6884	243	714	45	2	1
3	Tea	11	139	24	239	9639	634	15868	1853	13	5
12	Vegetable non-essential oil.	8	-	2	1	392	3	-	-	-	-
14	Paints & Varnishes	476	98	126	77	44984	1389	12734	1402	21	12
14BB	Sodium Silicate	21	113	37	87	24884	2281	9795	1192	6	2
14D	Synthetic organic Dyestuff	13	70	13	45	13405	1728	3653	767	9	6
14DD	Synthetic organic products	-	8	1	10	1212	145	683	125	2	-
14E	Patent or proprietary medicines.	15	253	31	182	21476	290	10238	1033	21	15
14F	Cosmetics and toilet preparations	969	79	78	88	9647	1252	1308	262	12	6
14G	Acids	6	-	4	-	724	-	-	-	-	-

Contd....

(Figures of value and duty are in Rs.000)

(1)	(2)	3(a)	3(b)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
15	Soap	22	4	2	2	1838	8	129	4	-	-
15AA	Organic surface active agents.	3	5	-	11	955	45	351	45	1	2
16A	Rubber products	8	94	24	109	11496	1404	4203	1155	19	16
16B	Plywood	19	29	8	28	5867	352	5842	485	-	3
17	Paper	33	173	47	118	26722	2709	13132	1206	16	3
18A	Cotton yarn	33	89	22	217	2282	22	2461	561	4	-
18B	Woollen yarn	-	7	1	10	1952	75	1206	104	-	-
19	Cotton fabrics	27	43	21	21	6440	552	1370	43	1	-
21	Woollen fabrics	1	2	-	5	201	1	1684	70	-	-
23A	Glass and Glassware	7	26	3	49	2597	550	2626	544	1	---
23B	Chinaware and porcelain-ware.	195	126	48	30	54971	2510	1291	281	19	2
23C	Asbestos cement products	5	94	11	66	12759	1054	3555	477	3	1
26A	Copper and copper alloys	11	107	27	12	12196	317	562	17	7	2
29	Internal combustion engines.	41	14	11	215	2023	27	3554	84	-	-
30	Electric motors	47	132	34	405	11607	1190	21005	2428	14	15
30A	Power driven pumps	398	90	140	162	20435	334	7477	655	11	7
31	Electric batteries	10	26	18	16	1657	49	896	161	-	1
32	Electric bulbs and tubes.	29	142	74	151	8622	693	3790	2899	9	13
33	Electric fans	5	92	23	264	7163	549	6664	771	9	8
33A	Wireless receiving sets	14	17	1	46	871	74	4023	453	3	1
33B	Electric wires and cables	11	226	74	94	40183	2254	10015	558	35	26
33C	Domestic electrical appliances	1	41	8	174	4117	561	6835	1549	3	1
33D	Office machines	3	30	6	66	3548	569	3489	512	3	4
34	Motor vehicles (Trailors)	314	55	79	192	13183	515	11628	495	15	12
34A	Motor vehicles parts and accessories	334	64	75	45	12763	372	2548	289	6	4

Contd.....

(Figures of value and duty are in Rs.000)

(1)	(2)	3(a)	3(b)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
37B	Cinematograph projectors	2	4	2	22	146	36	1028	204	-	-
40	Steel furniture	1822	141	306	178	58000	984	3200	256	53	32
46	Metal containers	337	125	39	65	30879	1324	8054	1105	17	12
47	Slotted Angles and channels	-	14	2	3	624	42	337	12	-	-
52	Bolts, nuts and screws	1885	99	254	32	113004	90	5616	19	5	3
59	Electric insulating tapes	1	21	5	4	2724	177	200	17	1	2
60	Adhesive tapes	2	24	5	3	5540	308	122	13	-	-
	Total:	7578	3059	1798	3670	635125	28292	200446	24681	379	223

Source : Reports from the Collectors of Central Excise.

CHAPTER 13

REFORM OF SALES TAXATION

13.1 Indirect taxes levied by State Government, particularly the sales tax, and to a lesser extent, the octroi duties levied by local bodies, play a not insignificant role in determining the spread of the tax burden between different income groups and between different parts of the country as well as in influencing the pattern of resources allocation in the economy. The yield of sales tax amounts to more than 50 per cent of the yield from excise duty levied by the Centre and was equal to 3.1 per cent of net national income in 1975-76. In chapter 4, we have indicated in detail the manner in which the existing systems of sales taxation by the State interact with excises and import duties and aggravate the problem of cascading. Steps to reshape Central taxes alone in order to ensure progression in their incidence and to make them help rather than hinder the pursuit of the nation's socio-economic objectives and priorities, will not give us the desired results unless ways can be found to bring about the requisite measure of harmonisation of indirect taxation by the Centre with indirect taxation at State and municipal levels. If the Centre and each of the States continue to act independently and without adequate co-ordination, the attempt to rationalise the indirect tax system of the country will become an impossibility.

EXCISE AND SALES TAX

13.2 One of the issues which has been discussed from time to time and is currently being hotly debated is whether it would not be much better to abolish the sales tax altogether and compensate the States for the loss of revenue by imposing additional excise duties, as indeed has been done in the case of three important products, namely, textiles, tobacco and sugar, following the agreement reached in the National Development Council in 1956. The communications as well as personal discussions which we have had with State Governments as a whole are strongly opposed to this proposal. They have drawn attention to the wide area of responsibility which has been entrusted to them under the Constitution and argued that powers of taxation allotted to them are in fact inadequate to meet their growing commitments and should, therefore, be enlarged rather than curtailed, They have further argued that the question is not merely one of ensuring an adequacy of financial resources which could be achieved by a higher devolution from the Centre. The extent or degree of autonomy and responsibility to their own electorate which the Constitution envisages can be sustained only if they have adequate and independent powers of taxation. It is also urged on behalf of this point of view that autonomy should also include the discretion on the part of the people of different States to have a smaller or larger public sector according to their respective choices. When a State makes its own tax effort for which it has to seek the support of the State Legislature, it has a greater sense of responsibility and would be inclined to explore every possibility of economising on expenditure. The increasing dependence of States on Central subventions tends to undermine financial discipline.

13.3 On the other hand, a plea for the abolition of sales tax has been made not only in representations from trade and industry but also by some eminent individuals who have argued, that in order to eradicate the harmful effects of multiple taxation by different autonomous authorities, a uniform system of internal commodity taxation under the aegis of the Central Government should be brought into being with arrangements for such sharing of the revenues between the Centre and the States as would safeguard the resource position of the State Governments. The advantage in a single authority levying all the taxes on a particular product would be that it could take into account all relevant

considerations - the burden on the consumer as well as impact on production and investment in industries. Such a levy would be easy to rebate when exports take place. There would be considerable saving in the cost of collection. Diversion of trade as well as of production centres from one State to another, which differential rates of sales tax lead to, would be eliminated. The difficulties caused by the requirements to comply with the laws, procedures and forms of different States which make life difficult for manufacturers who buy their raw materials and components from different States and sell their products in different States would be removed. Harassment to small traders and many corrupt practices would also be eliminated.

13.4 Superficially, it may seem that the sales tax is similar to, and a mere super-imposition on, the excise. In actual fact, while there are some areas of overlap, there are also considerable differences between the scope of the two tax systems. Though both excises and sales taxes exempt certain products, the criteria on which and the extent to which exemptions have been given are very different in the two taxes. The excise, despite the considerable widening of the base that has taken place in recent years, is still not and cannot also become universal in scope. Even though it may be within the legal powers of the Centre to impose excises on agricultural products, it would be quite impractical and uneconomic for it to do so. Again, within the sphere of industry itself, the production that takes place in numerous unorganised units has to be left out of the excise net for administrative reasons. The sales tax on the other hand is much more in the nature of a general tax covering all commodities except those where the intention is to spare the consumer. True, on administrative considerations, very small shopkeepers are also exempted from sales tax, but then the tax is collected at the earlier stage on the same products. Moreover, the scale of operations which is too small for excise purposes tends to be much larger than what is considered to be an adequate exemption level for sales tax purposes. Because of the very much wider coverage, although sales tax rates are well below excise rates, the total revenue realised is a little more than half of what is derived from excises. A very sizeable increase in the rates of excise - slightly more than 50 per cent on the average - would be needed to compensate for the loss of revenue arising from the abolition of the sales tax. According to estimates (vide Table 1 below) by the National Institute of Public Finance & Policy, there are about 22 broad items (excluding residuary items) not liable to excise, the sales taxes on which were estimated to yield around Rs. 500 crores in 1974-75. (These estimates were based on information supplied by 13 major States for 1973-74). Some of these have since been brought under the general 2 per cent excise levy. Nevertheless, the products of the non-industrial sector and the decentralised sector are still, by and large, outside the scope of excise. It would, therefore, be roughly correct to say that nearly Rs. 500 crores of sales tax are being currently collected on goods such as agricultural products and output of small manufacturers, including those producing some high value articles like jewellery, which for administrative reasons, Central excises do not reach.

TABLE 1 - ESTIMATED YIELD OF SALES TAX (1974-75) FROM COMMODITIES NOT SUBJECT TO EXCISE

	Name of Commodity	Estimated yield of sales tax in crores of Rs.	Remarks
1.	Foodgrains, atta and other products	117.78	
2.	Liquors and spirits, etc.	42.25	
3.	Cattle-feed and poultry feed	2.05	

	Name of Commodity	Estimated yield of sales tax in crores of Rs.	Remarks
4.	Other food items other than confectionary, prepared and preserved food etc.	49.90	
5.	Coal and coke	4.41	
6.	Firewood/charcoal	1.97	
7.	Groundnuts, copra, oil-seeds, oil-cakes, etc.	64.96	
8.	Non-edible oils	3.10	Only the organised sector is liable to Central excise duty at 2% but the industry is mostly in the non-organised sector.
9.	Others like butter (other than pasteurised), ghee, etc.	1.79	(10% excise on butter from 1977)
10.	Bullion (gold and silver)	0.69	
11,	Ornaments etc. (pearls and jewellery)	10.29	Factory-made ornaments are now excisable but the industry is mostly in the non-factory sector.
12.	Mica and other minerals	1.33	
13.	Readymade garments and hosiery goods	9.13	These were taxable under Central excise in 1974-75 but now they are exempted.
14.	Cotton	22.02	
15.	Silk fabrics etc.	4.74	
16.	Wooden furniture	4.59	Factory sector now excisable at 2% but the industry is mostly in the non-factory sector.

Name of Commodity	Estimated yield of sales tax in crores of Rs.	Remarks
17. Bricks, bardana and other building material	18.18	Bricks taxable to excise at 2% but the industry is mostly in the non-factory sector.
18. Timber	25.47	
19. Metalware	25.79	2% excise only on certain metalwares and these too only if they are in the organised sector.
20. Watches and clocks	4.03	Liable to Central excise duty at 10% from 1977.
21. Arms, ammunition, etc.	1.4	Now liable to Central excise duty at 2%
22. Bicycles and parts	14.54	Liable to 2% Central excise from 1975 except tyres, freewheels and rims.
23. Bones and Bristles	0.19	
24. Hides and skins	5.55	
25. Other items not separately listed	104.56	

13.5 Excise is a tax on goods which are manufactured or produced. Confining taxes to production would mean leaving untaxed the value which is added to a product between the point at which it leaves the factory and the point when it is sold to the consumer. This would not only mean discrimination between the manufacturer and the trader but would also mean discrimination as between different products depending on what proportion of the consumer price is due to value added after manufacture. Since durable consumer goods are sold along with certain services in order to attract and please the consumers, they normally have a substantial proportion of value added at later stages. If tax is levied only at the manufacturing stage, there would be an incentive to lower the ex-factory price and correspondingly increase the wholesale or retain outlets. Since only the larger producers would be able to establish countrywide outlets, this system would discriminate in their favour. There would also be an attempt to increase the proportion of value added at later stages.

13.6 A further point to be noted when considering the distinctive role of the sales tax is that excise duties have an all-India character. They cannot take into account the differences in the

levels of incomes and patterns of consumption which vary so considerably from region to region and State to State. The different rates of sales taxation in different States, while they undoubtedly create some problems which we deal with later, permit regional and State level variations which could not be provided for under the excise tax system.

13.7 Prima facie, there is a strong case for preserving sales taxes in addition to excise duties on the ground that they play distinct roles. Excise is an all-India tax on goods which are manufactured or produced. Regardless of where the production takes place, the tax burden falls on the entire country. The revenues too accrue not only to the Centre but to all the States on the basis of the Finance Commission's recommendations without any bias in favour of States which have more excisable units located in them. The sales tax on the other hand is essentially a local tax on consumption. It is expected to fall on the goods consumed in the State which levies the tax regardless of the place of production of the goods.

13.8 Against this background, when considering the future role of the sales tax system, a choice has to be made between two alternatives:

(a) Through a Constitutional amendment, the levy of sales tax can be made a Central subject and thereafter a rationalised system of indirect taxation on domestic production and consumption can be administered by the Centre such as a comprehensive VAT;

(b) An attempt can be made to reform the existing State sales tax systems so that they are freed from most of their weaknesses.

13.9 In making a choice between the two alternatives, the final judgment will necessarily have to be political. Without going into the Constitutional and political issues that are inherent in any discussion of this question, we seek to examine in the following paragraphs the fiscal and economic considerations involved and to dwell upon both the advantages and the drawbacks of sales taxation.

13.10 One major problem with the existing sales tax systems arises from the fact that the distinction between excises and sales taxes that we have referred to earlier has become blurred in practice and in some respects destroyed. The sales taxation has got enmeshed into the production cycle. It has also become an instrument of taxation of consumers outside the State. These deficiencies, the magnitude of which should not be minimised, come about through (a) the impact of sales tax on inputs and (b) the system of taxation of inter-State sales.

SALES TAX ON INPUTS

13.11 Through the inter-action of sales taxes and excise duties, and the consequent increase in costs and profits, the total burden on the consumer of the final product often does not reflect the kind of progression to which both the Centre and the States individually attach importance in fixing nominal rates on final products. The result is a cumulative and uncontrolled incidence leading to,

a) higher prices to the final consumer than is warranted by the amount of revenue accruing to the Government;

b) difficulties in the adjustment of tax burden on particular commodities to subserve Government policy objectives;

c) difficulties in freeing exports completely of internal commodity taxation; and

d) a general escalation of the costs of production in the economy.

13.12 Sales taxes on inputs, for which no credit is given at later stages of production, produce some other undesirable consequences of a serious nature which are generally overlooked. The following deserve special notice:-

(i) There is a trend to promote vertical integration because manufacturers who buy their products from other producers, usually small scale and ancillary industries, pay a sales tax on them, while no sales tax is payable on these items if they are produced within the factory.

(ii) The competitiveness of Indian products in international markets is reduced. While procedures exist for the refund of excise duties on a product when it is exported outside the country, the sales tax paid on inputs is not refunded except in Maharashtra. Sales taxes on inputs levied earlier in the chain of production are of course not known and not rebated at all.

(iii) When the goods are sold within the country but outside the State in which they are produced, the burden of the sales tax on inputs is passed on to consumers in other States. Even in respect of items which are supposed to be free from sales taxation by States and subjected to an Additional Excise duty in lieu of it, the taxation of their inputs gives an additional revenue to the producing State which often falls on consumers in other States. We have referred in Chapter 4 to the existing procedures for giving relief from sales taxation on inputs which shows that the concessional treatment accorded to inputs is often not extended to sales of input outside the State. Also, in some States the relief is made conditional on some tax (local or inter-State) being collected on the final product.

13.13 In effect, the levy of sales tax on inputs without appropriate procedures for relief through drawback or refund, deflects from the distinctive role of sales tax as a levy on consumers within the State and turns it, like excise, into a tax on production. In consequence, the more developed States, which have attained high levels of agricultural or industrial production, are able to derive additional resources by taxing consumers in other States. On the other hand, the resource mobilisation capacity of the less developed States, which have to depend on most of their needs being met from imports from other States, is generally weakened, because they cannot impose sales tax at a high rate on products whose prices have already been enhanced by transport costs and taxation of inputs by the producing State.

13.14 In the light of the considerations set out above, we feel that the sales tax system in all the States should be suitably modified to ensure that the taxation of inputs does not impinge in the way that it does today on the price of the final product regardless of whether the production and/or consumption of the product is within the State or outside.

13.15 For such a reform to be really effective, it would be necessary to consider the role of the inter-State sales tax which is levied under the Central Sales Tax (CST) Act. In so far as it applies to inputs it has the same kind of impact as the sales tax on internal sales of inputs. In the case of

final products or consumer goods, its impact is clearly extra-territorial. At the same time, it is not an insignificant source of revenue. The State-wise breakdown of the revenues from CST is given in the Table 2 below:-

TABLE 2 - STATE-WISE BREAK-DOWN OF REVENUES FROM CST

Name of State		1973-74 (Actuals)	1974-75 (R E)	1975-76 (B E)	1976-77 (B E)
		(in rupees lakhs)			
Andhra Pradesh	...	957	900	954	2264
Assam	...	170	196	198	553
Bihar	...	674	1481	1676	2376
Gujarat	...	1865	2124	2336	3867
Haryana	...	1245	1300	1428	2225
Himachal Pradesh	...	14	12	17	21
Kerala	...	501	675	775	889
Madhya Pradesh	...	1614	1900	2100	3093
Maharashtra	...	5591	7700	6900	11718
Karnataka	...	1285	1600	1800	2500
Orissa	...	582	606	890	1382
Punjab	...	1017	1350	1553	2466
Rajasthan	...	587	655	725	1350
Tamil Nadu	...	2082	2594	2994	4173
Uttar Pradesh	...	527	1000	1050	1700
West Bengal	...	2507	3500	3760	5500
Delhi	...	1328	1871	2697	N.A.
Total	...	22546	29464	31853	46077

Source: 1. State Budget documents for figures relating to the States.

2. Delhi Administration for figures relating to Delhi.

13.16 The table shows that on the whole the inter-State sales tax is more favourable to what might be regarded as the more developed States which have a large industrial base or have substantial agricultural surpluses which are sold to other States than to what are generally regarded as the backward States; though Bihar, Madhya Pradesh and Orissa also get good revenues out of this tax mainly because of the location of steel plants in these States whose products are largely consumed outside the State.

13.17 Apart from the question of inequity involved in the distribution of the revenues from CST, what concerns us is that the extra-territorial impact of the inter-State sales tax, particularly since it has been raised from the original one per cent to the present four per cent, goes against the basic rationale of the sales tax as some thing distinct from the excise falling mainly on the consumption within the State concerned.

13.18 In this context, it is worth remembering that the TEC, which had recommended the enactment of a law by Parliament for the levy of sales tax on inter-State transactions, had made the following observations:

> "The proposed Central legislation, for the levy of sales tax on inter-State trade, will have also to specify the rate at which the tax on sales in the course of inter-State trade and commerce should be levied. Since, in permitting the levy of sales tax on inter-State trade, the main intension is to ensure that some revenue accrues to exporting States without raising unduly the burden on consumers in the importing State, it is necessary that the rate to be specified in the Central legislation should be comparatively low. It should, in our opinion, be one per cent, on all articles except on goods of special importance in inter-State trade.* Inter-State trade comprises two types of transactions, viz., (i) transactions between registered dealers of one State and registered dealers of another and (ii) transactions between registered dealers of one State and unregistered dealers of another. The rate of one per cent, proposed above, would apply only to the transactions between the registered dealers in one State and the registered dealers in another. In regard to these transactions, while the exporting States will, under the scheme of Central taxation of such transactions, retain the tax receipts realised from the levy of one per cent, the importing States will be able to recover their own taxes on the re-sales of those goods by the registered dealers within their area."**

13.19 Thus, the main object in fixing the rate of CST at the low level of 1% was to ensure that while some revenue accrued to the producing States it did not result in raising unduly the burden on the residents of the importing States. Further, a low rate of CST would serve to plug the loopholes that would arise if the goods sold across the State borders were totally free of taxation. However, under the pressure from the States, the rate of CST has been raised from 1% to 4% in three stages; 1% to 2% in 1963, 2% to 3% in 1966, 3% to 4% in 1975. Today it has become an instrument of transferring resources from the less developed to the more developed States. In order to avoid paying the inter-State sales tax, many manufacturers consign their products to their own depots in other States so that no sale attracting CST takes place. This places the small producers at a disadvantage, since they do not have the means to set up their own depots. Further, the discrepancy between the rate of CST and the rate of local sales tax on inputs causes uneconomic diversion of trade. In States where the sales tax on inputs is higher than the inter-State sales tax, there is a growing trend on the part of industries to get their inputs from outside the State even though local supplies are available. Thus, while transformer oil is available in Tamil Nadu, producers usually buy it from outside the State paying only 4% as inter-State sales tax against 8% sales tax within the State. A factory producing a heavy chemical in Easter U.P. sells most of its production to factories in Bihar which uses it as an input, while factories in U.P. which need the same input prefer to get their supplies from a manufacturer in Gujarat because the CST of 4% is less than the local

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* In regard to the levy of a tax by the State on sales or purchase of specified goods, the TEC recommended that the Central Government should take power to impose conditions subject to which the States can levy the tax. These conditions should be that in replacement where necessary of existing systems and levies, (i) the States shall levy only a single-point tax (at the last stage of sale or purchase) on these goods, and (ii) the rate shall not exceed 1/4 anna in the rupee, i.e. the same rate at which the Central tax will be imposed on these goods in the course of inter-State trade.

** Report of the TEC, Vol. III, page 57, para 17.

sales tax on the chemical both in U. P. and Bihar. Printers in Calcutta, on the same considerations, get their supplies of paper from factories in Bihar and Orissa rather than buy them from factories in Bengal. Thus, a higher levy on basic inputs than the rate of sales tax on inter-State sales has not only been causing diversion of trade but a waste of precious transport. On all these considerations, we feel that it has been a mistake to look upon CST as primarily a source of revenue and to go on raising the tax on inter-State sales and thus the trend needs to be reversed. We have, elsewhere, made specific recommendations in this regard. Some of the industrialised States as well as those which have exportable surpluses of agricultural and mineral raw materials which they sell to other States expressed in the course of our enquiry, the concern that their revenue potential would be undermined if any reduction in the inter-State sales tax were to be made. We see no reason why there should be any decline in total revenues if taxation by one State of consumers in other States is reduced. If the products consumed within the State which come from outside it, are taxed at a lower rate by the producing State, they could be taxed at a higher rate by the consuming State without raising the burden on the consumer. If in the event, it is felt that the differential impact of a reduction in the rate of CST on the revenues of different States would be inequitable, the Central Government and the Finance Commission would have to consider whether any adjustments in the scheme of devolution would be needed. Prima facie, our judgment is that once the States have settled down to the new pattern, they will, by appropriate adjustments of internal sales tax rates, be able to safeguard their revenues. Further each State will be able to ensure better the appropriate measure of progressiveness in its own sales tax structure. As things are, some of the basic essentials of life such as foodgrains and pulses get taxed at a minimum of four per cent even in States which would have wished to spare their low income consumers this burden because the principal producing States subject them to such a tax.

13.20 Two other weaknesses of the existing system of sales taxation deserve mention:-

(a) There are many products for which the Central Government or the producers try to maintain a uniform all-India price but different rates of sales tax result in divergence of price from State to State. Some State representatives were prepared to concede that certain key commodities, such as cement, for which there is an equalised all-India price and fertilisers, could well be subjected to uniform rates of sales tax throughout the country. Likewise, drug manufacturers are required to mark the maximum retail price of the product on the package. Manufacturers of products like vanaspati also maintain a uniform all India price. The Department of Civil Supplies have pointed out that their attempt to have a number of key products marketed with their prices stamped on them in the interest of consumer protection does not fully achieve its objective because in all cases it has to be indicated that sales and other local taxes are extra. This results in the prices varying from State to State. Thus, the maximum prices fixed by Government or manufacturers lose all their sanctity and the consumer may well be charged much more than what may be justifiable on account of sales tax. The consumer cannot, therefore, be told what he should be prepared to pay as the fair price inclusive of taxes. This leaves room for malpractices by the trade.

(b) Purely from the procedural angle, each State having its own law, leads to different judicial interpretations which create variations in the manner of assessment of sales tax. Similarly, the existence of different prescribed forms in each State for complying with the tax laws of different States creates unnecessary problems for manufacturers and traders whose activities are carried on in more than one State.

13.21 The preceding discussion has brought out that while sales taxes do serve an important role, independent of the excise system, in the mobilisation of resources, they are also creating a number of complications and problems particularly by interfering with the processes of production. As stated earlier, one way of getting rid of these problems is to have one integrated system of indirect taxation covering the stages of production, distribution and trade. However, our recommendation is that sales taxes should continue to have a separate existence provided necessary reforms can be introduced to make them more efficient and less cumbersome and in particular to deal with the following issues:-

(i) The problem of cascading and distortions in factor prices;

(ii) Ways in which sales taxes imposed by one State affect other States; and

(iii) Legal, administrative and procedural complexities which afflict trade and industry.

13.22 In any attempt to reform the sales tax system, the first priority has to be given to making it an efficient instrument of revenue mobilisation for the States themselves. At present, States have multi-point, double-point and single-point levies and even in respect of single-point levies the stage at which it is levied varies from State to State. A number of expert committees appointed by different State Governments have gone into the efficacy of the systems prevailing in different States. The Committee on Commodity Taxation set up by the Government of Kerala under the Chairmanship of Prof. I.S. Gulati, observed thus:

CASE FOR SINGLE-POINT LEVY

> "While the merit of the multipoint system lay chiefly in the minimisation of chances of evasion, as the incentive for evasion will be weak due to the low rate of tax, the system had certain disadvantages.
>
> Firstly, a multipoint tax involved realisation of the tax from dealers at all levels and thus the number of tax payers was naturally larger. Secondly, the incidence of multipoint levy was uncertain. It was anywhere between 3 to 4 times the normal rate. Thirdly, the scope for varying rates from commodity to commodity with a view to introducing progression or to subserving any other policy objective, was extremely limited. The tax incidence on the consumer differed from commodity to commodity and this might in cases turn out to be highly regressive. Fourthly, the multipoint tax interfered with the channels of distribution as it favoured integration and put the small dealers at a disadvantage.
>
> Under single-point taxation, on the other hand, the incidence could be kept at the declared level. The rates could easily be varied from commodity to commodity with a much greater certainty about their incidence on consumers. The system was also neutral among the distribution channels. Assessment and collection were easier and more efficient for single-point levies, because then the point or stage at which the tax became leviable could be decided upon, taking into account both the channels of trade peculiar to each and every commodity and the efficiency with which the administration could enforce the tax laws."*

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* Report of the Committee on Commodity Taxation, May, 1976, page 32, para

13.23 The Sales Tax Enquiry Committee appointed by the Maharashtra Government (Yardi Committee) noted that:

> "the States, where the multipoint system was first introduced, found out that though the system of multipoint was easy to understand and administer, the articles sold from the first stage of sale to the last could not be traced and fraudulent suppression of sales at the middle or the last stage of sales became common for obvious reasons. The other defect of such a system was that the turnover limits for registration had to be fixed at a comparatively low figure and so a large number of small traders were brought within the ambit of taxation under this system. Apart from the cascading effect such a system had on the sales in the course of inter-State trade or commerce or in export, the intermediate links like commission agents between manufacturers and wholesalers or semi-wholesalers tended to be eliminated under this system. While, on the one hand, the tax rates had to be increased to meet the growing revenue needs of the State, on the other, it became necessary to provide relief to manufacturers and commission agents. Further the States found it necessary to levy a single-point tax at the first stage on the sales of certain items which were consumed by the affluent sections of the society. All this led to complications in the tax law!"*

The Committee also noted that in regard to the two point system generally the items selected were those which could be identified without much difficulty. However, the claim that it plugged evasion was not borne out by evidence. On the contrary, evidence indicated that evasion took place in respect of the last stage of sale. Thus, the system had no superior value over other systems. The Lakdawala Committee (referred to earlier) noted

> "the single-point tax had a distinct administrative advantage where trade channels were well known and easily identifiable, so that the incidence of tax could be focussed at a known point. Considerations of economic welfare would demand that the tax should be levied at the last stage. A single-point tax imposed on the first stage might, unintended, mean some departure from the neutrality principle of taxing expenditure in all directions equally. It had, however, predominant administrative advantage of being collected from manufacturers and big dealers who could keep proper accounts and would find large evasion difficult."**

13.24 Essentially, as the views expressed by the Committees referred to above bring out. there are two sets of considerations. There is a preference for a shift towards single-point levy as being much more rational. On the other hand, there is the consideration that a single-point levy might give much wider scope for evasion and evasion at one point would mean that the product remains wholly untaxed. Although there seems to be a trend towards a single-point levy in many States, the views which we have received from State Governments on the subject show considerable variations.

13.25 Some States have stated that the point at which sales tax should be levied should be left to them to be decided in the light of their local trade and industrial structures. They apprehend that

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* Report of the Sales Tax Enquiry Committee, Maharashtra, (1975-76) - page 8, para

** Report of the Uttar Pradesh Taxation Enquiry Committee, 1974, page 210.

a single point levy at the last point of sale is likely to cause administrative problems because of the large number of dealers who set up bogus firms for dodging taxes. One of the States has said that experience has shown that the single-point tax at the last stage results in dealers accumulating large liabilities which eventually become non-realisable. Further, the verification of the claims of dealers that they are not liable to tax is time consuming. One of the Union Territories has, however, said that a combination of first point and last point taxes is always better than a single-point system although the former should be selective.

13.26 On a balance of all considerations, we favour a single-point tax at the last stage. This would eliminate cascading effects and make it easy for State Governments and State legislatures to consider and determine the kind of burden that should be imposed upon consumers of different products.

13.27 At the same time, we recognise the importance of the administrative factors. If the last point levy is to be paid by a very large number of relatively small dealers, many problems would arise. There would be a danger of loss of revenue. The possibility of some bogus firms getting themselves registered as dealers and getting their supplies without tax being paid and then vanishing into thin air cannot, in the light of past experience, be ruled out. In addition, it may be vexatious for small traders who may find it difficult to comply with the formalities of accounting and form-filling required under the law. The Yardi Committee had also pointed out that a large number of chambers and associations had advocated the abolition of retail sales tax as it caused great inconvenience to small dealers. The argument adduced was that the cost involved for these dealers in the submission of returns and the appearance for assessment with the help of sales tax practitioners, far exceeded the amount of tax payable by them. For all these reasons, we feel that it would be desirable to raise the limit for compulsory registration to a reasonably high level. Under section 44 AA(2) of the Income-tax Act, every person having a turnover of or above Rs. 2, 50, 000/- in any one of the three years immediately preceding the accounting year, has to maintain such books of accounts and other documents as are prescribed. We feel that the limit prescribed by the Income-tax Act for compulsory maintenance of accounts could be taken as a line of demarcation for compulsory registration of dealers for sales tax purposes. This change would also reduce the number of establishments which have to pay sales tax lessening both administrative costs and charges of harassment of small dealers.

13.28 Some State Governments to whom we had put this suggestion have expressed the apprehension that the imposition of a high limit is likely to reduce the revenues or promote evasion. We have considered this point. If only dealers with a turnover of Rs. $2\frac{1}{2}$ lakhs or more were to be compulsorily registered, it could well happen that manufacturers might canalise their sales through dealers with a small turnover. Similarly, imports from other States could be affected by relatively small dealers who would not come under the sales tax net work. We would, therefore, recommend that in addition to the dealers with a turnover of Rs. $2\frac{1}{2}$ lakhs or more, the law should also provide voluntary registration of dealers whose turnover is less than Rs. 2.5 lakhs. This would enable them to purchase inputs free of tax and supply them to manufacturers. Besides, all manufacturers within the State and all those who import goods from other States should be subjected to compulsory registration. In that event, the manufacturer of a product or its importer would either himself have to pay the sales tax or produce evidence of having sold it to a registered dealer who would be a party known to sales tax and income tax authorities alike. We recognise that local conditions may make it difficult straightaway to switch over to such a system. In the intermediate stage, a double-point system in respect of some commodities where the risk of evasion appears to be great could, as has been done by Maharashtra, be adopted.

13.29 Such a system would, in our view, ensure adequacy of revenues to State Governments, whose freedom to levy such taxes as they think fit from the revenue angle and on other considerations would remain unimpaired. It would also help eliminate some of the defects to which we have drawn attention earlier. Since all manufacturers will be registered dealers, the purchase of inputs by them could be exempted from sales tax through the issue of the needed declaration. This in fact is the major advantage that would be derived from the last point system. Cascading effects and overflow of sales tax from the levying State to consumers in other States as well as the difficulties in the way of exports would be eliminated. Sales tax, in other words, would become a consumption tax. The harassment to small traders will also be removed. The supplies which the small registered dealers will get will already have been taxed unless they have been bought from petty traders or very small producers. What will escape taxation would be the value added by them which would represent mainly the profits which they make. This would not mean a large sacrifice and would give welcome relief to small traders.

CASE FOR UNIFORMITY OF RATES

13.30 The next point which needs consideration is whether we should also move in the direction of uniformity of rates. Substantial differences in the rates of taxation in neighbouring States tend to result in artificial and, therefore, uneconomic diversion of trade. While a large number of products can be taxed at different rates, there are some on which rate differentials encourage uneconomic diversion of trade in a manner which also results in a loss of revenue to the State with a higher rate of taxation. Thus, for the more expensive consumer goods, cars, refrigerators, tyres and the like, it often pays the consumer if the difference between the sales tax rates is large enough to make purchase in other States than his own. Some of the State representatives seemed conscious of this danger. Some States have been inclined to favour uniformity of rates, at least on a regional basis, for products of this kind. But a regional solution would not be a complete answer, since each region adjoins another. The logical conclusion of such an approach would be to aim at country-wide uniformity or at least mitigation of difference in sales tax rates in respect of such items.

13.31 A valid point that has been made to us and referred to by us earlier is that by virtue of varying rates of sales tax in different States on goods in respect of which Government would like to maintain uniformity of prices, are goods are sold at different prices in different States. The consumer cannot, therefore, be told what he should be prepared to pay as the fair price inclusive of taxes. To obviate this, a case exists for introducing uniformity in sales tax rates in the case of such selected goods.

13.32 There are two ways in which uniformity can be achieved. Firstly, there can be voluntary agreement by States; and secondly, the device of an Additional Excise duty in lieu of sales tax can be extended to more items.

13.33 Machinery to promote agreement between States on a regional basis already exists. Four Regional Councils have been set up under Article 263 of the Constitution to discuss matters relating to sales tax and Medicinal and Toilet Preparations (Duties of Excise) Act. Adjoining States have been grouped in one region. Each Council meets twice in a year. It has representatives from each State and the Union. Problems relating to uniformity, diversion of trade due to differential tax rates, remedial action with reference to the impact of judgments on the tax powers of the States, steps to arrest evasion and avoidance, improvement in procedures, etc., are discussed in these Councils. The decisions taken by the Council have to be implemented by the States within the region.

If the decisions are not implemented, the matter can be referred to a meeting of a Council of State Ministers presided over by the Union Minister in charge of sales tax for a final decision. One of the State Governments has expressed the opinion that the Regional Councils are playing an important role in ensuring harmonisation of the sales tax system and they could meet more often to solve the various problems. It has also suggested (i) the setting up of an inter-State secretariat so that such problems relating to sales tax can be attended to more closely and (ii) more periodical meetings at all-India level to discuss sales tax problems.

13.34 We would recommend that the institution of Regional Councils should be made to play a more active role in investigating and discussing matters relating to sales tax and coordinate policy and action in the light of the decisions which Government take on the basis of our Report. Further, we feel that periodic meetings at all-India level should also be organised.

ADDITIONAL EXCISE DUTY IN LIEU OF SALES TAX

13.35 As regards the possibility of widening the list of items covered by the Additional Excise duty, the points we have made about the disadvantages of a general merger of the sales tax with excise duties do not lose their validity when applied to individual items. Though bringing them under the Additional Excise duty will have the advantage of minimising the cost of collection and risks of evasion, the value added at later stages escapes taxation. State Governments seem to have major reservations on the extension of the list of goods to be subjected to Additional Excise duty. This is partly because while sales taxes accrue to the States which levy them, the sharing of the revenue derived from the Additional Excise duty is subject to a formula which is somewhat more favourable to States whose revenue position is weak. But other reasons also have been advanced.

13.36 One State Government has argued that the excise in lieu of sales tax on a commodity has to be levied at a much higher rate than the latter if the same amount of revenue is to be obtained. The non-taxation of the value added to the goods subsequent to the manufacturing stage makes it easy for the distribution channels to appropriate large profits depending on the elasticity of demand and supply of particular goods. Another State Government has argued that the inclusion of more goods with corresponding exemption of the small scale sector both from Basic and the Additional Excise duties would cut into the revenues of the State Governments. However, one State Government has indicated its willingness to accept the inclusion of coal, petroleum products and iron and steel in the scheme of Additional Excise duties provided it is allowed to impose a turnover tax on these items. Yet another State Government has suggested the exclusion of tobacco from the existing scheme on the ground that the conditions relating to the processing and trading of tobacco products make out a strong case for taking tobacco out of the list.

13.37 Another and a more serious objection which the State representatives have voiced to an extension of Additional Excise duties is that their yield tends to be frozen at a particular level while sales taxes levied by State Governments on their own have a much greater measure of elasticity. This view is based largely on the experience that the rate of growth of revenue from Additional Excise duties has been much less than that of the yield from sales taxes levied by the State Governments. If uniformity in all-India rates is achieved for a range of products then, whether such uniformity is achieved through parallel action taken by each State Government individually or through Central action, any further increase in revenues would result only if the production of these items goes up or if their prices rise, unless the agreed upon rates are revised upwards.

13.38 The grievance which State Governments may legitimately have about the way in which the Additional Excise duties have worked in the past is that there has been a tendency for the Central Government to keep their rates unchanged at the original levels, even when the rates of Basic Central excise duties on these products have been revised upwards. We would suggest that when Additional Excise duty in lieu of sales tax is levied by the Centre, its rate should move proportionately to changes in the Central levy. That is to say, if an increase in the excise duty on such a product is contemplated, the proposed increase should be proportionately apportioned to the Basic duty and the Additional Excise duty. This kind of sharing could be in both directions. Just as the two duties would move up together as suggested above, if conditions emerge in which the tax burden on a particular product needs to be lowered, States should be prepared to accept a reduction in the revenue from this source. Such an attitude of partnership would facilitate the extension of the system of Additional Excise duties in appropriate cases.

13.39 One of the concerns of State Governments was taken note of by the National Development Council in 1970. It decided that the yield from Additional Excise duty in respect of the three commodities, sugar, textiles and tobacco should roughly correspond to 10.8% of the assessable value and the Additional Excise duty rate should be revised so as to give this yield within a period of two to three years. For arriving at this percentage, several calculations were made as to what would have been the yield from sales tax on these commodities, had not these been subject to the levy of Additional Excise duties in lieu of sales tax. In this connection, due note was also taken of the value added subsequent to the stage of manufacture.

13.40 The question for consideration is what should be the tests to be applied in selecting items to be brought under Additional Excise duties. Many States, we found, are conscious that wide variations in rates lead to undesirable consequences. However, uniformity in rates, where desired, can also be brought about through mutual agreement among the States. In case if the States do not switch over to a uniform pattern of taxation as recommended by us, it would obviously be more difficult to bring about equality of rates. More importantly, there are some products of widespread consumption which are produced by a relatively small number of large producers. In such cases, there would be considerable saving in costs of collection and elimination of trouble and expense for a large number of dealers, if Additional Excise duties were to be imposed as a means of bringing about uniformity in taxation.

13.41 It has been represented that when a product is made subject to Additional Excise duty in lieu of sales tax, its principal inputs should also be similarly treated. Otherwise, some of the advantages of the change may be lost. Thus, by taxing yarn and dye-stuffs, State Governments have been able to get revenue from the sales of these inputs casting in the result an indirect burden on textiles which is not in consonance with the spirit of the arrangement.

13.42 States are opposed to the extension of the scheme of Additional Excise duties to the taxation of inputs. They feel that the coverage would become too wide as all the inputs are not exclusively used in the manufacture of the goods covered by the scheme. For example, it is pointed out that basic inputs needed by textiles, tobacco and sugar industries, are also needed by other industries. We feel that it would be better to bring uniformity in rates in such cases through voluntary agreement. Whenever there is agreement about applying a uniform rate of sales tax to any product, it should be the endeavour to have a similar uniformity in rates in respect of the most important of its inputs which do not have any other significant alternative uses.

13.43 Much of the discussion on the impact of sales taxes proceeds on the assumption that they pose an issue of conflict of jurisdiction - and interest - only between the Centre and the States.

EXTRA-TERRITORIAL IMPACT OF SALES TAX

What tends to be overlooked is that autonomous action by each individual State is not without its repercussions on the economies of other States. Sales tax systems of individual States often have an extra-territorial impact. Attempts by one State Government to attract industries through concessions under sales tax inevitably affects other States. We have earlier, in this Chapter pointed out how through the taxation of inputs and of inter-State sales, States from which the goods originate are able to collect a tax which falls on the people in the State to which the goods are despatched. We have argued in favour of a reform of the sales tax system so as to minimise the adverse impact of taxation on inputs in such a way that the benefits of the change are not confined to producers or consumers within the State itself.

13.44 Before considering what changes would be appropriate in this sphere, it would be useful to discuss in abstract some of the points of principles which are of relevance. State Governments emphasise that there should be no curtailment of their right to levy such sales taxes as they think fit. One of the logical corollaries of the principle of autonomy on which this claim is based is that no State should levy its taxes in such a manner that it encroaches upon the capacity and, therefore, the autonomy of other States to levy similar taxes. The autonomy to which States attach importance has validity not merely with reference to any possible interference by the Centre but also in respect of any action taken by one State which may affect others. It seems to us somewhat anomalous that while States are precluded from taxing the sale of products to an overseas buyer, they can levy a tax of 4 per cent, which operates like an export duty, on sales to another State within the country.

13.45 If we may venture to reflect on the rationale which prompted those who gave shape to our Constitution to make the excise a Central levy and leave it to the States to levy sales taxes, it would seem that taxation of production was meant to be a Central responsibility so that it could fall on and also benefit the entire population without discrimination between States with a large production base and small, while States were left free to tax consumption within their States, in such manner and to such an extent as they deemed fit. If it had been possible to maintain such a line of demarcation in practice, many of the problems which we are concerned with would probably not have arisen. Sales taxes would not have affected producers. When an end-product emerged from a chain of production and was sold not to another producer for further processing but to the consumer, the State to which the consumer belonged could have levied a tax on it as it thought fit. The real check on the level of such a levy would have been the political one, namely, what the elected representatives of the people of the State concerned would have voted for and endorsed in the Legislature. But when taxes imposed by one State fall on the residents of other States, either through levies on inter-State sales or through levies on inputs, the rationale enunciated above ceases to operate.

13.46 The view has been put to us by the more industrialised States that they have to incur heavy expenditure on account of the industries located in their territories and that it is but right that the consumers of their products even outside the State should contribute their share to the expenditure which is being incurred on their account. As against this, States which are lagging behind industrially, maintain that industries contribute in a substantial way to the economy and revenue of the States where they are located and that they cannot be looked upon as a burden on their resources. Backward States have been offering tax concessions and thus sacrificing revenues, in order to attract industries because of the benefits they bring to their economy. Furthermore, they argue, their own resource position is generally far worse than that of the industrialised States and their

attempts to mobilise additional resources are gravely hampered by the fact that the prices of industrial products, for which they have to rely on imports from other States, are already on the high side, not only because of the cost of transport but also because of taxes levied by the States where they are manufactured. They are, therefore, unable to impose on their consumers, whose general level of income is low, much of an additional burden by way of sales taxes of their own.

13.47 The manner in which the revenue resources of the country are allocated between the Centre and the States or among the States inter se is a matter which receives the consideration of the Finance Commission as well as the Planning Commission. We take no position on the claims summarised in the preceding paragraph of the industrialised and the less industrialised States. We have earlier urged the adoption by States of a single-point sales tax levied at the last point. If the scheme were brought into effect by all States, the extra-territorial impact of sales tax through taxation of inputs would automatically be reduced. There, however, would remain the extra-territorial impact caused by the inter-State sales tax. We would recommend a reduction in the rate of inter-State sales tax, which should in stages be brought back to the level of one per cent. Indeed a lowering of the rate of inter-State sales tax would itself generate economic pressures in favour of a reversal in the trend for the high taxation of inputs, for, as we have pointed out earlier, if the sales tax rate on the inputs is higher than the inter-State sales tax, manufacturers begin to import the inputs from other States and thus pay a lower rate of tax.

13.48 The concept of goods of special importance, which the TEC had evolved, was meant to mitigate the impact of input taxation in so far as certain inputs of obvious importance were included in the list of declared goods. Since then not only have the rates been raised but a pertinent question has arisen, namely, whether some other inputs should not also be brought into the category of declared goods having regard to the growth and diversification of the industrial economy of the country. The TEC had spelt out the following considerations:-

(i) the commodity should be a raw material or largely in the nature of raw material;

(ii) either as raw material or as finished goods based on such material, it should be of special importance in terms of volume in inter-State trade; and

(iii) for the country as a whole, the product should also be of special importance from the point of view of the consumer or the industry.

13.49 The list of declared goods covers not only inputs but a number of products which are of major interest to the consumer. In considering whether the tax rate on them should be lowered and also whether the list should be enlarged, the following factors have to be taken into account:

(a) In the interests of progression a good case can be made out for lowering the rate of sales tax on some of the basic necessities of life such as foodgrains and pulses. However, clearly any such reduction on the rates applicable to sales within the State would mean net loss of revenue and may also be questioned on the ground that it interferes with the internal autonomy of the State to a greater extent than is warranted. Then there are other regional factors to be taken into account because consumption patterns in different States vary. Thus, in some States rice could be regarded as a basic daily need while wheat would not be considered to be so. In other States, the reverse may hold good. In general, therefore, we

feel that while there may be a good case for lowering the rate of inter-State sales tax on such products, in regard to internal consumption limitations imposed by Parliament in regard to levy of sales tax should be the minimum.

(b) Despite their distinct roles which we have sought to make out ultimately, excise and sales taxes do fall on the same products. If, on national considerations, it is regarded desirable to lower the imposition on any product it would be quite legitimate - in the context of the Centre lowering the excise duty to take measures - to ensure that the States also contribute towards the national objective or at any rate do not by raising their sales taxes prevent the benefit of any reduction in the excise from passing on to those for whom it is meant. In such conditions, recourse to the declared goods concept could be appropriately thought of.

LOCATIONAL IMPACT

13.50 While dwelling on the impact of the sales tax system of one State on another we should like to comment on the use of concessions in sales tax by different States to attract industries to their own territory or to encourage them to go to backward areas within the State. Often concessions offered by one State have to be matched by similar ones or larger ones by neighbouring States who are equally interested in getting new industries located in their territories. In the event, the effects of the concessions in influencing the location of industries get largely neutralised, while all the States stand to lose revenues. This again would seem to be an area where agreement between States to evolve an all-India pattern would be preferable to concessions being given by different States on the strength of pressures exercised by intending investors, who try to make the States compete with each other in sacrificing their revenues in the interests of development. We would suggest that the definition of backward area for this purpose should be a uniform one which all States should respect. Since such a definition already exists for purposes of identifying certain areas in which the Centre offers various incentives (vide section 80 HH and Eight Schedule of the Income Tax Act). States could well adopt it and agree upon the concessions, if any, in respect of sales taxes which need to be given in addition to other incentives that may be given. The sales tax concessions should be uniform and no concessions should be given to industries located outside the backward areas as nationally defined.

61ST REPORT OF THE LAW COMMISSION

13.51 At this stage, we would draw attention to certain possibilities of extending sales taxation which within the existing legal and constitutional frame work remain untapped. In its 61st report, the Law Commission observed that several transactions fall outside the concept of sale because of the absence of the essential requirements of sale. For example, a transaction between a hotelier and a resident customer of a hotel - if there was a consolidated charge for boarding and lodging - would be one of providing services and would not be taxable under the head 'sale of goods'. The Commission noted that the primary difference between a contract for work (of service) and a contract for sale of goods was that the service was intangible and it would be difficult to identify the service component in the final product despite the fact that a part of even the whole of the materials used by the contractor for making the final product may have been his property. In other words, this is because the distinctiveness of the two components embedded in the final product, namely, goods used and the services performed, got blurred, though the transactions relating to works contracts resembled a sale in substance. Thus, the sale of an air-conditioner is subject to sales tax but a contract to air-condition a building which does entail the supply of air-conditioning equipments escapes taxation. Similarly, sales of automobile spare parts are taxable but a contract to repair or overhaul a vehicle is not subject to sales tax. The recommendations of the Law Commission to bring the kind of transactions referred to above within the sales tax net should, we feel, be accepted.

13.52 Opportunity can also be availed of to implement the recommendations of the Law Commission in regard to taxation of hire-purchase transactions. As the law stands, it is only when the final instalment is paid that the sale becomes effective and, therefore, the tax is not leviable on earlier instalments. We would also urge the implementation of the recommendation of the Law Commission for the enactment of provisions analogous to the provisions in the Gujarat Sales Tax Act, which has been upheld by the Supreme Court, for facilitating and enforcing the recovery of any amount illegally realised as tax by a private person whether as sales tax or any other tax.

UNIFORMITY OF PROCEDURES

13.53 One of the identifiable areas of reform, which would entail no curtailment of the existing powers of State Governments in regard to sales taxation, would be to ensure uniformity, on an all-India basis, in the legal and administrative framework of sales taxation. As things are, a manufacturer in one State who gets some of his raw materials and inputs from other States or sells his products in more than one State has to comply with laws and procedures laid down by each State under its own legislation which differ from State to State. The latter create problems and difficulties. High Courts give different ruling on the same issues, merely because the State laws are differently worded. The forms to be filled for the same purposes also vary from State to State.

13.54 In this context, some of the State Governments have suggested the drafting of a model sales tax law by the Centre, which the States could conveniently adopt, with suitable modifications, taking into consideration local problems. They feel that a certain amount of diversity is inevitable because of the varying factors of production and consumption and the resources required by the States. Some State Governments have suggested uniform sales tax legislation to cover basic matters like registration, assessment, exemption etc.

13.55 The TEC had made the following recommendations in this regard:

> "Finally, we would make the concrete suggestion that the Inter-State Taxation Council should undertake the task of introducing as much uniformity as possible, between different States, in the matter of sales tax law, regulation, procedure and forms in so far as these can be distinguished from, or are not concerned with actual rates, turnover limits, exemptions, etc. At present, the definitions of terms like 'dealer', 'sale price', 'turnover', year', etc. differ widely from State to State. This leads to their interpretation and judicial construction being different in different States and creates unnecessary complications and hardships to the trade and industry, particularly in regard to inter-State transactions and for dealers who have branches in more than one State. The procedure for filing returns and payment of tax, for assessment, for appeals and revision, etc., and the regulations regarding maintenance and inspection of accounts also vary considerably between the different States. The same lack of uniformity is to be found even in the forms of returns, forms for refunds and adjustments, the type of evidence to be produced for sales outside the State, etc. Without conferring any advantage whatsoever on individual States, this diversity in regulation and procedure creates many avoidable difficulties for trade, commerce and industry. In forms and procedure, in particular, and even in regard to the structure of different Sales Tax Acts and in the definitions adopted in them - though not, as we have stated, in rates, exemptions, registration limits, etc. - it is not only possible but extremely desirable that as large a measure of uniformity as feasible should be aimed at and achieved. We consider that the inter-State Taxation Council, as soon as it is established,

should take this up as one of its very first tasks in the context of the sales tax."*

13.56 It would also be advantageous both to State Governments and to business and industry, if uniformity in sales tax legislation and procedures was achieved in all States, either through Central legislation or by the drafting of a model law by a Central Agency like the Law Commission which each State could adopt. The former could be achieved by getting the consent of the States under Article 252 of the Constitution. Alternatively, a small group of representatives from different States could be set up who could jointly evolve the draft of such a law after agreement. Such standardisation on the legal and procedural plane would be desirable and need not touch upon the rate structure which each State would be free to determine acting within its own legislative powers.

UNIFORMITY IN SALES TAX LEGISLATION MODEL LAW:

13.57 A study made by our secretariat of the problems due to lack of uniformity in registration, turnover, year, etc., is added to this Chapter as an Annexure. It would appear therefrom that without infracting in the powers of the State in the field of state taxation, uniformity or near uniformity can be achieved.

13.58 We are conscious that a question might be raised as to whether the changes suggested by us in regard to sales taxation would not result in a sizeable loss of revenues. Our approach throughout has been to ensure adequate revenues and we believe that with appropriate adjustments in rates, loss of revenue could be avoided. This will not mean imposing a greater burden on the consumer. The reduction in the rate of CST could be offset in two ways. Firstly, with the present high rate of CST, a growing volume of inter-State transactions is taking place on a consignment basis. As no inter-State sale takes place, the tax is non payable. In fact, it is only the relatively small dealers who find it difficult to circumvent the tax in this manner. If the tax rate is lower, the subterfuge will no longer be a paying one. Secondly, while the revenue derived by a State on inter-State sales would go down, its capacity to have a higher sales tax on products originating outside its boundaries would go up. It is true that for each State the loss and gain may not be quite balanced. But, in general, there may be a more equitable distribution of sales tax revenue between different States. As regards the loss that might seem to arise from a reduction in taxation of inputs, appropriate adjustments of rates on final products should make up for the shortfall without really raising the burden on the consumer. Apart from such adjustments in the rate structure of sales taxes on goods, additional revenues could also be raised through certain other sources. We discuss a few posibilities in the next Chapter.

SAFEGUARDING STATE REVENUES

13.59 We conclude this Chapter with a brief summary of the reforms suggested in the field of sales taxation. We have felt that if the sales tax were to continue as a separate tax and play a distinctive role, it should be freed of the problem of cascading and become essentially a tax on the consumption of the residents of the State Government. For this purpose, there must be a lessening of the impact of sales tax of one State on the residents of another State. The reduction in the rate of CST to the original level of 1 per cent is, in our view, the most crucial step for achieving the above objectives. There has also to be relief for inputs under sales taxation. Further, uniformity in tax rates in respect of a number of commodities through agreement between States would be desirable; if that is not feasible, a wider coverage of the scheme of Additional Excise duty in lieu of sales tax could be thought of as an alternative.

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* Report of TEC, Vol. III, Chapter V, p. 75.

ANNEXURE TO CHAPTER 13

A STUDY OF THE PROBLEMS DUE TO LACK OF UNIFORMITY IN SALES TAX LAWS

I. TURNOVER

1. The base for the levy of sales tax is "turnover". It can be turnover of sales or purchases or both. As this is an indirect tax, the assessable entity through whom the tax is collected is the dealer. The latter is obliged by law to obtain a valid certificate of regisration, if he is liable to pay the tax. Thus, turnover has a direct bearing both in regard to registration as well as liability to tax.

2. Generally, turnover is defined so as to include the aggregate of the sale prices received and receivable. Where a purchase tax is in existence, the definition of turnover will also cover the aggregate of the amounts of purchase price paid by a dealer. As the tax liability is for a year, the turnover for the year is taken into account for determining the liability to tax and liability for registration.

3. Though one approach could be to deal with the two distinctive aspects relating to "turnover", namely, its impact on registration as well as liability separately, there is a practical difficulty in treating these aspects in isolation, as there is a considerable amount of inter-connection and inter-dependence. A careful study of provisions in a few Sales Tax Acts, selected at random, relating to the definition of turnover diversely styled as "liability to tax", "incidence and levy of tax", "incidence of taxation", etc., shows that there is no uniformity in approach. The main points of divergence are :

(a) Some Acts define three concepts, namely, taxable turnover or taxable quantum, total turnover and turnover, whilst others have only a definition of turnover and taxable quantum.

(b) In Kerala, the definition of "total turnover" also includes purchases or sales in the course of inter-State trade or commerce or in the course of export of goods out of the territory of India or in the course of import of goods into the territory of India. Though no local sales tax is payable on inter-State sales or sales or purchases in the course of import into or export from India, the inclusion of the amount covered by these transactions fastens a liability on the "dealer" for purposes of registration.

(c) In U.P., the definition of turnover specifically excludes the sale by a person of agricultural or horticultural products grown by himself or grown on any land where he has interest as owner, etc., However, in Kerala, tea, coffee, rubber, cardamom and timber are specifically included in turnover. Therefore, the liability of dealers in Kerala for registration as well as tax becomes widely different from those placed, say, in U.P.

(d) It is a usual feature of Sales Tax laws to exclude in the definition of turnover itself any amount refunded in respect of articles returned by customers. Such a facility is not accorded in some State Acts with the result that the liability for registration as well as tax becomes larger. In certain States, the amount refunded is not automatically deducted unless the goods are returned within a prescribed period. The period prescribed is also not uniform.

(e) There is no uniformity in regard to the limit of turnover with reference to which the liability impinges. In some States, the classification broadly takes the pattern of an importer, manufacturer and other dealer, with different limits for each. There is no such classification in certain other States. A via media approach is followed in some States by prescribing a monetary limit for importers, whereas in Delhi, the limit for an importer is nil. There are also marked variations in regard to the taxable quantum in respect of dealers in cooked food. Such limit varies very widely with a high limit of rupees two lakhs in Kerala.

(f) Under the Delhi Sales Tax law, turnover is defined in a manner that in the case of an assessee opting to pay sales tax on the basis of sale proceeds actually received, the turnover will only include the amounts of sale prices actually received.

4. Whilst there might be differences in the stage of development between State and State which may call for differentials in the matter of limits beyond which there will be incidence of liability, it is desirable to narrow down the differences arising out of the adoption of different definitions of turnover. There is no justification for including the turnover arising on account of inter-State sales or purchases or sales as a result of import into or export out of India for determining the classes of dealers who will be liable to tax. This is because every dealer having inter-State sales is obliged to register under the CST Act. As the sales tax officer assessing the dealer under the CST Act and under the local Sales Tax Act will generally be the same person, the requirement of registration with reference to a turnover which also includes inter-State sales not liable to local sales tax does not confer any special advantage on the administration. On the other hand, it might give room for harassment on account of the dealer being required to comply with several statutory requirements. On balance, it is, therefore, fair to exclude sales not assessable to local sales tax in fixing the limit for registration.

5. When goods are returned, and the sale amount is refunded, it will not be correct to say that such proceeds still form part of the dealer's turnover. However, prescription of a time limit within which the refund of the sale proceeds should be made will tend to curb collusive practices. It is also advantageous to have uniformity in this matter. The CST Act provides for a period of six months. This period could conveniently be adopted in the State Acts also with the same phraseology.

6. An equally uniform approach is necessary in regard to the inclusion or otherwise of purely agricultural or horticultural produce arising out of one's own land or as a result of self-cultivation in the definition of turnover. Under the Income Tax Act, a distinction exists between a dealer in foodgrains and a cultivator. The performance by a cultivator, etc., of any process ordinarily employed to render the produce fit to be taken to the market is also excluded from the ambit of the Income-tax Act. Though a transaction may not result in a profit, there should at least be the carrying on of a "business" as is ordinarily understood, before such a sale is subjected to taxation. In Director of Supplies & Disposals vs. Board of Revenue (20 STC 398), it was held that in disposing of surplus war materials, the Director was not carrying on the business of selling goods. The transactions of sale were, therefore, not liable to be taxed under the Sales Tax Act. This judgment is relevant because in selling one's agricultural produce, no business is involved and as such it is not rational to levy sales tax on such sales. Further, the situations arising out of a cultivator selling his own produce or a person selling his own personal effects are almost identical. The same argument for not taxing sales of personal effects will apply with equal force to sales of agricultural produce grown in one's own land. There are other modes of taxing the income from agriculture but there is certainly no justification to include them in the turnover for the levy of sales tax.

7. The provision for exclusion from turnover sale proceeds not actually received on the basis of the exercise of an option suffers from fallacies. It may also result in abuse. Firstly, a Sales Tax Officer may not be able to correlate the sales that have taken place and the receipts which have been accounted. When the receipts are in respect of sales of different years, the task becomes more arduous i. identify the sales, which are still to be accounted. This will create problems for tracking them, eventually giving a chance to an unscrupulous dealer to omit all the receipts from outstanding bills. Secondly, when there are variations in rates, the sales which have taken place in a particular year but the proceeds of which are realised in a subsequent year may suffer a different tax altogether.

8. Under the Income-tax Act, income from property is assessed on the basis of the bonafide annual value. This is on the assumption that the rent for which the property is actually let will be received and tax is payable thereon. In order to provide for cases of hardship where the rent becomes irrecoverable, Rule 4 of the Income-tax Rules provides for a deduction in the year in which the assessee proves that the rent payable is irrecoverable. It is only proper that sales tax is levied on the receivable basis of sale proceeds with an appropriate provision for a deduction where the assessee is able to establish that the sale proceeds are lost and irrecoverable. The circumstances in which such a deduction can be allowed can also be prescribed by Sales Tax rules.

II. YEAR

9. There is no uniformity in regard to definition of the term "year". While some Acts define the year as the financial year, the Gujarat and Maharashtra Acts give an option to an assessee who maintains regular books of accounts to adopt his year of his accounts. In other words, he can adopt the Samwat year, the Ramnavami year or the calendar year depending upon how the accounts are maintained. Unlike income-tax, sales tax is payable with reference to turnover. The liability has to be quickly deduced, as otherwise, problems of collections may arise. It would, therefore, be advantageous that the necessary uniformity in this matter is achieved by adopting the financial year as the year for purposes of sales-tax assessments. As the laws prescribe filing of periodical statements, a dealer should not find difficulties even if a switch over were to be made in respect of the year of assessment.

10. It may be incidentally mentioned that a number of Sales Tax Acts do not have any provisions prescribing the period of limitation within which an assessment with reference to the return filed has to be completed. The Gujarat Sales Tax Act provides for a time limit of three years for the completion of assessment in ordinary cases and a period of eight years and four years in respect of cases where the assessment has been reopened due to under-assessment.

11. The Income Tax Act provides for a time limit of two years for the completion of the assessment from the end of the assessment year. As the assessment year follows "the previous year" which is the base for income-tax assessments, this in effect means three years from the beginning of the financial year immediately following the "previous year".

12. It is not desirable to keep the tax-payer in suspense in regard to his liability. Apart from impinging on public relations, non-stipulation of a time-limit within which as assessment should be completed may create problems for collection. The sales-tax authorities will be able to plan their work more efficiently if statutory time limits are imposed. The time limits provided by the Gujarat

Sales Tax Act and the Income Tax Act are the same. The same time limits may be considered for adoption in respect of sales tax by the State Governments.

III. REGISTRATION

13. The levy, assessment and collection of sales tax is facilitated through the medium of registered dealers. When businesses have offices in more than one State, the case for uniformity becomes more pronounced.

14. The procedures for registration vary from State to State. In some States, only those who are liable to pay the tax are entitled for registration. In Kerala, the limit for liability to pay sales tax and the limit for obligatory registration are different. The Gujarat and Punjab Sales Tax Acts have provisions for voluntary registration. In some States, the prescribed authority, for good and sufficient reasons, demands a security for the proper payment of tax or for the furnishing of a surety. Such security is linked with the demand and there is also an enabling provision for demanding additional security. In some States, appeals are also provided against the demand of security or additional security.

15. There are provisions in the State laws to enable the prosecution of a dealer who carries on business without registration. The scales of punishment vary from State to State. Some States do not provide for any imprisonment in respect of a failure by the dealer to get himself registered. The amount of fine to be imposed also varies, e.g., in U.P., the fine is Rs.500/-, or the amount of tax involved, whichever is less. In Kerala, the corresponding figure is Rs,2,000/-, or the tax plus other amounts due, whichever is less. In Kerala, the punishment is simple imprisonment for six months, or fine as prescribed above. In Delhi, it is rigorous imprisonment or fine or both. There is also difference in phraseology in the description of the offence.

16. To bring about some measure of uniformity, it is desirable to prescribe at least a few essential prerequisites. The remaining aspects could be left to the States for being dealt within their own judgment.

(a) The registration and the liability to pay tax are complementary. Whilst every dealer, liable to pay sales tax, should be statutorily obliged to apply for registration, there should also be enabling provisions for applying for voluntary registration.

(b) There should be a time limit within which the application for registration should be disposed of. A dealer will not be able to avail himself of the facilities of registration unless the application for registration is dealt with promptly.

(c) As in the CST Act, there should be provisions for demand of security for goods and sufficient reasons and for the proper realisation of the tax payable. In order to avoid the demand of a security, unrelated to the liability, the law should prescribe a ceiling, somewhat on the lines of the CST Act, namely, that the amount of security/additional security shall in no case exceed the estimated tax payable. There should be an order in writing, spelling out the reasons for the demand of security. Such order should be made appellable and a time limit should be prescribed for the disposal of the appeal.

(d) The need for uniformity in the matter of punishment was commended by the Supreme Court, in the case of Purushottam Halai vs. Collector of Bombay (28 ITR p. 891) in the context of different punishments obtaining in different States for non-payment of income-tax. The corresponding provision in the Income-tax Act dealing with the failure to file a return of income is section 276CC. This section provides for rigorous imprisonment for a term not less than six months but which may extend to seven years and with fine, where the amount of tax exceeds rupees one lakh. In other cases, it will be imprisonment not less than three months but which may extend to three years and with fine. In order to deal more effectively with recalcitrant assessee, etc. section 278A provides for a second and subsequent offences, rigorous imprisonment for a period not less than six months but which extend to seven years and with fine.

17. The situations of not filling a return under the Income-tax Act and not applying for registration under the Sales Tax Acts are analogous. For arresting evasion, more stringent provisions are necessary. As both the Income-tax and Sales Tax laws have stabilised, it is desirable that failure by a dealer to get himself registered should be visited with rigorous imprisonment. There can also be a difference in treatment as in the case of the Income-tax Act, viz., cases of tax liability of less than Rs. 1,00,000/- and over Rs. 1,00,000/- should have differential scales of imprisonment. For the second and subsequent offences, the scale of punishment should be uniform. In some States, the fine is a stipulated sum, or the amount of tax, whichever is less. In Kerala, the fine should not exceed the stipulated sum or the amount of tax and other amounts due, whichever is less. It is desirable to adopt a phraseology as obtaining in Kerala. It is also desirable to describe the offence in a manner that the Department may not be called upon by Courts to prove "mens rea". In Kerala, the words used are "Any person being a person obliged to register himself as a dealer under this Act does not get himself registered .... shall on conviction ...."etc.

18. In the Delhi Sales Tax Act, the expression used is more direct and not susceptible of imposing an obligation on the Department to establish "mens rea". The corresponding provision is "whoever carries on business as a dealer without obtaining a certificate of registration ..... shall be punishable." It would be desirable to adopt the latter phraseology.

IV. LICENCES, AUTHORISATIONS, RECOGNITIONS AND PERMITS

19. The Maharashtra and Gujarat Sales Tax Acts have provisions for issue of licences, authorisations, recognitions and permits. The broad position appears to be :—

a) A registered dealer can apply for a licence, if his sales to other registered dealers exceeds Rs. 50,000/-;

b) A registered dealer can apply for an authorisation, if the value of exports outside India or inter-State trade or sales to any authorised dealer, who either exports or dispatches in inter-State trade, exceeds Rs. 30,000/-;

c) A registered dealer can apply for a recognition, if the value of all taxable goods manufactured for sale by him exceeds Rs, 2,500/-.; and

d) A registered dealer who bonafide buys or sells for an agreed commission any goods on behalf of a principal and whose turnover exceeds Rs. 30,000/- can apply for a permit.

20. The benefit of availing of these options is broadly as below:—

I. Exclusion from the turnover of the selling dealer of :

a) Sales of declared goods to an authorised dealer or to a commission agent holding a permit ;

b) Sales of schedule C goods (these include a variety of items ranging from low rated items like betel nuts and poultry feed to high rated items like pile carpets and computers) to authorised dealers or permit holders ;

c) Sales of schedule D goods ranging from low rated items like raw wool, hosiery goods to high rated items like country liquor or foreign liquor to licensed dealers, authorised dealers or permit holders ;

d) Sales of schedule E goods which include items like foodstuffs, fountain pens, boot polish, cutlery and plastics which are mostly in the nature of household items, to licensed/authorised dealer or common agent holding a permit ;

II. Certain time limits within which the resale has to be made by the purchaser as well as certain other conditions to be observed have also been stipulated.

III. Reduced rates of tax in respect of certain sales :

a) Where any dealer sells taxable goods to :

(i) an authorised dealer, who certifies that the goods will be despatched in the same form without any processing, etc., within three months to his own place of business outside the State either for sale or for use in the manufacture of goods for sale outside the State ;

(ii) a recognised dealer, for use within the State in the manufacture of taxable goods for sale.

All the above sales will be charged at a concessional rate of 4%

It may be desirable for all other States also to provide for similar options.

21 The Kerala Sales Tax Act provides for the issue of permits for doing business at places other than the registered place or places or for employment of travelling salesman or representatives. The entire turnover under the permit should be accounted for in the total turnover of the registered dealer. There is provision for inspection and maintenance of day to day accounts in respect of transactions carried on under the permit.

22. The Sales Tax Enquiry Committee appointed by the Maharashtra Government has observed that as a large number of manufacturers, exporters and common agents are availing themselves of

the facility of authorisation, recognition and permit, these facilities should be continued. They do not, however, favour the continuance of the licence system, in pursuance of their recommendation to switch over to a first-stage, single point tax.

23. It may be desirable, if other States also provide similar concessions and adopt a grouping which can facilitate easy identification and enable the Legislature to decide whether the concessions in the stated circumstances are justified. This will also provide an in-built mechanism for cross-checking whether the conditions, interconnected with the grant of exemptions from or reduction in the rate of sales tax, are complied with. If the conditions are not satisfied, the concessions could be withdrawn. The Sales Tax Officer has also to impose additional liability in such cases. This task will become easy if separate procedures as is in vogue in Maharashtra are inscribed in the Sales Tax laws of other States. From the point of view of the dealer also, the difficulties inherent in checking as to whether the purchaser is entitled to the concession in taxes will be minimised, as the latter will have an appropriate certificate issued by his Sales Tax Officer for making such concessional purchases. In otherwords, such grouping and issue of certificates will serve a purpose, more or less analogous to the "C" form in inter-State trade. Statistical analysis will also be aided by such a grouping, as it would be possible to assess how far the incentives given have helped in achieving the objectives. Easy identification of these classes of purchasers will also enable computerisation of data as and when modern techniques to have a data bank are proposed to be extended.

CHAPTER 14

OTHER STATE AND MUNICIPAL TAXES — MEASURES OF REFORM

A. OCTROI

INTRODUCTION

14.1 Having discussed the directions of reforms of sales tax, which is by far the largest source of tax revenues in the field of State taxation, it will only be logical to deal with in detail about octroi, which is one of the important sources of revenue at the local level.

14.2 Though this was a very ancient mode of collecting tax in India and was supposed to have been in existence even during the period of the Mughals, the octroi in its present form is traceable to 1805 Regulations of the East India Company. But even in those days, the levy of octroi was found to be vexatious as it interfered with the movement of trade and commerce, and it was abolished in the provinces of Bengal and Madras as early as 1835-1842. But in other provinces like Bombay, Oudh, Punjab, North-West Provinces, octroi developed later, in successive stages, and became an important source of revenue to local bodies.

14.3 Because of its defects, octroi has often been the subject of enquiry. Almost every Committee (relevant extracts given below) that examined octroi in the past had found it to be undesirable and harmful.

VIEWS OF ENQUIRY COMMITTEES

14.4 Sir Josiah Stamp, in his evidence before the TEC said:

> "In my judgment, both theoretically and on the result of the exprience, no country can be progressive that relies to any extent upon octroi, which has nearly every vice."

14.5 The TEC doubted even the theoretical soundness of octroi :

> ".....the form in which they [octroi duties] are levied in India they offend against all canons of taxation; they are uncertain in their incidence; and their collection and system of refund, which form an essential feature of octroi put the person paying the tax to great inconvenience ..... The Committee recommend that a strenuous endeavour should be made to get rid of indirect taxation in the shape of octroi and terminal taxes and to replace it, if not by taxation of property and persons, at least by something in the nature of a tax on sales. The tax in its present form is one that is condemned by economists everywhere and there are visible tendencies to develop it into a regular tax on transit ....."

14.6 The Motor Vehicle Taxation Enquiry Committee (1950) appointed by the Ministry of Transport under the Chairmanship of Shri M.N. Dalal, remarked as follows :

> "Evidence before the present Committee indicated that in some areas the ill-effects on trade of local octroi, terminal tolls and similar taxes on goods in transit.....are

today in 1950 perhaps even greater than they were when the 1924-25 Committee commented so adversely on this form of taxation. Among the causes responsible for the present economic malaise in the body politic of some parts of India, the reversion to this form of taxation in the present aggravated form permitted by some State Governments might not be a negligible contributing factor."

14.7 The TEC's recommendations were :

"Octroi is unsatisfactory; its elimination from the tax system of local bodies should undoubtedly be aimed at, but this is inevitably a long term aim. It is impossible to conceive in the immediate future of alternative source of local taxation which will give Rs. 11 crores odd of revenue which octroi today provides. Hence, attention should be confined to eliminating the more palpable evils of the octroi system."

14.8 The State Transport Reorganisation Committee (1959) set up by the Ministry of Transport under the Chairmanship of Shri M.R. Masani, recommended that —

"Octroi, wheel taxes and other imports charged by municipalities .....should be discontinued, octroi being merged in the general sales tax or some other levy unconnected with motor transport ....."

14.9 The Committee of Local Self Government Ministers on Augmentation of Financial Resources of Urban Local Bodies, in its report submitted in 1965, quoted Sir Charles Trevelyan as having described octroi as the remains of a barbarous system of universal taxation and stated as follows

"The undesirable features of Octroi are firstly, that its incidence is regressive and falls mainly on necessaries of life like articles of food etc., secondly, the administration of the tax is very cumbersome and vexatious, as numerous barriers have to be erected for collecting the tax at the points of entry and a very complicated procedure of refunds has also to be followed; thirdly, the octroi system gives wide discretionary powers to low paid staff which leads to corrupt practices; and fourthly, it is expensive to collect and hence wasteful. It also constitutes a restriction on through trade. The national economy should be safeguarded as an entity by facilitating the smooth flow of trade and commerce among States and also among different parts of the same State and preventing the raising of bottlenecks through local government regulations. Octroi is certainly an undesirable tax from this point of view .....

We are, however, of the view that octroi in its present form should be gradually replaced either by a turnover tax or by a surcharge on sales tax or by some other method which may cover the sphere of taxation which is being exploited for the purpose of levying octroi, but would be free from the evils of octroi system."

14.10 The Committee on Transport Policy and Coordination, appointed by the Planning Commission, recorded in its report in 1966.

"Octroi duties should be abolished. There has been general agreement on the vexatious and inhibitory nature of octroi duties and the abuses to which they are prone, but action leading to their abolition has proceeded very slowly."

14.11 The Rural Urban Relationship Committee, appointed by the Ministry of Health, (1966) under the Chairmanship of Shri A.P. Jain, observed :

> "Octroi constitutes a major hindrance to the free flow of traffic and trade and hence it retards the growth of commercial and industrial activities. It is in the national interest that octroi and terminal taxes should go."

14.12 The Report of the Road Transport Enquiry Committee, appointed by the Ministry of Transport and Shipping, (1967) (Keskar Committee), stated :

> "The Committee strongly feel that octroi is one of the greatest hindrances in the way of commerce and economic development of the country. Advanced countries realised it long ago and abolished octroi. While we would leave to the State Government to choose the alternative that suits them best, we would emphasise that octroi should be abolished as quickly as possible."

14.13 The Report of the Study Group on Octroi (1971) set up by the Government of Maharashtra under the Chairmanship of Shri Wankhode, observed :

> "Octroi is an inhibiting factor to the growth of local economy in general and industrialisation and road transport in particular, besides being a major source of delay and needless harassment. Its deleterious effects on rural economy are far too obvious to be emphasised. It taxes the already limited capacity of cultivators who live at subsistence level and whose main incomes from sale of agricultural produce either in regulated markets or in the adjoining areas where they expect to get a fair price for their produce or to traders. Levy of octroi on movement of agricultural produce by more than one local body takes a large slice of the income of the cultivators, leaving them poorer. The effects of Octroi on industry are equally harmful. It is not uncommon to see large numbers of vehicles stranded at Octroi Nakas waiting patiently for verification of their goods or refund of the amount of tax paid. Such a hold-up, apart from being vexatious and leading to general traffic dislocation, invariably leads to a general delay in movement of commercial goods and commodities in a developing economy and lowers industrial as well as other efficiency. The ultimate gain, therefore, far outweighs the dubious advantage of local bodies derived at present from the existence of octroi. Viewed in this perspective, the entire abolition of octroi has long been overdue. In fact such a tax which is a survival from a more primitive economy has no place in an expanding economy such as ours whose hallmarks are speed and efficiency.
>
> Having considered all these incontrovertible facts we can only come to the conclusion that the levy of octroi needs to be eliminated and this is our earnest recommendation.

14.14 The Taxation Enquiry Committee, set up by the Government of Uttar Pradesh under the Chairmanship of Shri Lakdawal , favoured in its report, submitted in 1974, the total abolition of octroi in stages, but suggested, as an immediate step, a partial abolition in the local bodies deriving less revenues from that source.

14.15 DEFECTS OF OCTROI

Apart from the harmful effects, pointed out by different committees mentioned above, the following striking features have made it clearly undesirable and in some respects obnoxious.

(i) As the levy is often collected as a specific duty, in terms of weight, the incidence of the tax is regressive. Thus watches which are more costly get taxed at lower rates ad valorem than cloth.

(ii) Its administration is cumbersome and vexatious. Where octroi is based on unit or weighment, it takes time for the goods to be unloaded and checked. There are no warehousing facilities in all places. It is only with experianced personnel that it would be possible to check the values when duties are ad valorem. When even corporations and bigger municipalities are not able to man the administration of checkposts with qualified and experienced personnel, who could perform their job with speed and quick efficiency, the position in smaller local bodies is really pathetic. Any hold-up at the check-post also results in a national loss, in that it immobilises a large number of transport vehicles for unconscionably long periods of time. Further, discretionary powers vested in low paid staff often lead to corrupt practices.

(iii) The numerous barriers set for collecting the tax at the points of entry as well as the very complicated procedure involved in getting refunds affect the smooth flow of trade. Refunds are allowed in cases where octroi has been levied but goods are re-exported and also in cases of excess collection on goods subject to octroi. As the amounts to be refunded can only be determined after detailed investigations of the claims, there is delay as well as degree of uncertainty. There is also scope for manipulation by preferment of false claims.

(iv) The cost of collection of the tax is disproportionately high in relation to the revenues derived therefrom. For example, the Wankhode Study Group's report for Maharashtra shows that the cost of collection, as a percentage of gross octroi income was about 23.4 for 1968-69 in respect of 897 village panchayats and 22.6 for 210 municipal councils. The Lakdawala Committee report for Uttar Pradesh shows that for 1972-73, the cost of collection was 7.2 per cent of yield in respect of KAVAL cities, namely, Kanpur, Allahabad, Varanasi, Agra and Lucknow. Even this must be considered to be on the high side.

(v) Its economic impact, in addition to some of the adverse cascading effects as in sales tax, is undesirable in another respect; it encourages the concentration of industries in metropolitan areas, particularly, Bombay and Calcutta. Factories located within these areas can reach a large mass of consumers free of octroi levies. Even ancillary industries get located near the larger factories to escape this levy so that the components they sell do not pay any octroi.

14.16 In the discussions we have had with the State Governments, a point that has been urged is that urban communities must themselves pay for the higher cost of the amenities and services which they enjoy. It is argued that if octroi is to be abolished, compensation thereof through the levy of sales

tax would mean taxing the rural areas for the benfit of urban communities. This argument overlooks the fact that some of the metropolitan cities serve the entire country. In the very way in which sales tax imposed by one State spills over to other States, octroi duties, particularly those in major metropolitan cities — where there is a heavy concentration of industries — do affect consumers in all parts of the country. Further, the octroi operates like an import duty and, therefore, encourages the setting up of new industries within the octroi limits of cities having large internal markets. It will thus strengthen the trend for the concentration of more industries in metropolitan cities which will be contrary to the policy of deurbanisation and spread of industries to the rural areas.

ABOLITION OF OCTROI IN STAGES

14.17 While everyone seems to be in agreement about the need to do away with otroi, its actual abolition is deferred on the ground of inability to locate an alternative source of revenue. We are firmly convinced that a decision to abolish octroi should not be linked up with the finding of alternative sources of revenue. In our view, there is adequate scope available in the field of direct taxes, like taxes on land and property, agricultural income-tax, etc. which should be exploited to bridge the revenue gap arising out of the abolition of octroi. We also consider that abolition of octroi can be staggered. As a first stage, octroi could be abolished in respect of (a) small localities which could be more easily compensated because the amount involved may not be very large, and (b) towns and cities situated on national highways, collection of octroi by whom retards the free flow of inter-State traffic. At the second stage, an alternative source of revenue could be found by the States for the benefit of the larger cities which now depend on octroi as their predominant source of revenue.

ALTERNATIVES — PROS AND CONS

14.18 Coming to the question of alternatives, one that is suggested is the levy of a surcharge on the excise duty on high speed diesel oil. Various reasons can be advanced as to why this proposal is not feasible.

(i) The proposed surcharge would raise the cost of road transport in the case of goods and passengers, resulting in upward pressure on prices.

(ii) Such a pressure on price level is not likely to be neutralised by the abolition of octroi.

(iii) The enhanced price of diesel oil will adversely affect State road transport corporations and the Railways. The rural sector will suffer more than the urban sector.

(iv) As compensation will be payable only to States which are levying octroi, the proposal would discriminate against States which do not levy octroi but nevertheless have to bear the burden of the higher excise duty.

(v) Even among the octroi-levying States, those, like Maharashtra, who happen to resort to a greater extent to such taxation would get more compensation than other octroi-levying States.

(vi) The surcharge would also bring the problem of adulteration of diesel with kerosene.

(vii) The proposal would amount to acceptance of the principle of compensation by the Centre where in fact no such obligation exists.

14.19. While the larger road transport fleet owners may well prefer this alternative, because they may reap economies of scale with the larger turn around of vehicles, there is, from the national point of view, a good deal to be said against this course or any other, which would mean Central compensation to States levying octroi, the burden of which will also fall on States whose municipal bodies do not levy an octroi and have had recourse to other measures, such as higher property taxes. For all the reasons given above, we do not favour an increase in the levy of diesel to compensate the loss of revenue that will arise on account of the abolition of octroi.

SELF-ASSESSMENT BY TRANSPORT OPERATORS

14.20 Another alternative considered was to devise a method of assessment and payment of octroi without having recourse to check-posts. In this scheme, the road transporters would undertake the responsibility for collection of octroi due to local bodies at the time of booking the goods. The transport operators would prepare a way bill showing clearly the value or weight of goods destined to areas falling within the jurisdiction of a local body and collect duty thereon. To facilitate calculations, octroi rates were to be standardised for the local bodies and operators would deposit in the Treasury at intervals (say a fortnight or a month) the amounts collected. To prevent evasion, the proposal envisaged a system of surprise inspections. In other words, this was a system of self-assessment by transport operators. As there will be a large number of small operators who do not generally maintain accounts, and as the accounts, even where maintained, may not be up to the mark, the scope for suppression exists in a very large measure. Unless there are contemporaneous checks, it will be difficult to detect the suppression later, as a number of parties are involved. Thus, the procedure will become cumbersome and : cannot be considered as possessing the characteristics of a better substitute.

ENTRY TAX —MERITS AND DEMERITS

14.21 We have also looked into the alternatives that have been Experimented with by the Government of Madhya Pradesh in lieu of octroi. Two measures have been adopted, namely, an additional turnover tax and an entry tax. The entry tax has certain implications. It is intended to be levied on the entry of goods into a defined local area for consumption, use or sale therein. Goods have been graded into three categories; Schedule I lists goods which are exempted from entry tax on the lines of exemptions provided in the State's sales tax law. Schedule II covers goods which fall under the category of declared goods and those covered by the scheme of Additional Excise duty in lieu of sales tax.. Schedule III covers all goods not included in Schedule I or Schedule II. Entry tax was to be levied at 1.25% on the taxable turnover of goods liable to such a tax. Under the scheme, (i) check-posts will be eliminated; (ii) the tax will be levied on goods consumed in urban areas just as the octroi was; and (iii) there will be no obligation on the part of the Centre to give any compensation.

14.22 One important criticism that could be levelled against the entry tax is that it is a device to continue octroi in another form on declared goods as well as goods subject to Additional Excise duty. The basic objective of designating certain goods as "declared goods" under the Central Sales Tax Act, 1956 was to ensure controlled incidence of indirect taxation of such goods by the States and also to ensure an element of uniformity. Similarly, the scheme of Additional Excise duty in lieu of sales tax was evolved to ensure that incidence of indirect taxation on certain mass consumption goods was kept uniform and to avoid harassment to trade and industry. As we have pointed out in the previous Chapter, the policy with regard to taxation of declared goods and goods subject to Additional Excise duties has been evolved keeping in view the overall requirements of the economy of the country. If approval were given to such a tax, it would indirectly amount to the levy of sales tax even on some items where some amount of control and regulation were considered

necessary. We would not, therefore, commend the entry tax as a substitute for octroi. It is understood that entry tax has since been withdrawn in Madhya Pradesh.

IMPACT OF ALTERNATIVE LEVIES — PROS AND CONS ON WHOM THEY SHOULD FALL

14.23 In considering other alternative levies to take the place of octroi duties, the question arises on whom the burden should fall. The less industrialised States have taken the line that the levy should fall on the people of the municipal areas who enjoy the municipal services. This view ignores the fact that octroi, although it is nominally levied on goods which enter municipal limits, does cast a burden on the surrounding rural community who often draw most of their supplies of industrial products from shops within the municipal area. Further, octroi could also affect the prices which farmers get for their produce which they sell within the octroi limits, while seemingly octroi falls on the consumer through higher prices.

14.24 The other view which has been put forward is that metropolitan cities and particularly the port towns serve the entire country through their industrial output and port facilities. Therefore, it would be legitimate for the entire country to contribute towards the cost of their maintenance. In our view, while it is legitimate and proper that for the development of the infrastructure for international ports and the industrial complex around them there should be, as there is, provision for Central assistance under our Plans, the cost of maintaining and running municipal services should appropriately fall in the people who earn salaries, wages and profits in those areas and not be passed on materially to the consumers outside except in the form of the costs of the products or services which these areas provide to the hinterland.

14.25 On the whole, therefore, we feel that resources for the upkeep of municipal areas consequent on the abolition of octroi should be found by taxation by the local authorities or by the State Government but not passed on to the Centre, that is, to the country as a whole. To the extent that this can be done by purely local levies, e.g., increased property and water taxes or a tax on professions, as has been done in States where octroi is not levied, the local authorities would be in the best position to determine the rates of levy.

EXAMINATION OF FEASIBLE ALTERNATIVES

14.26 Various suggestions have been made from time to time for replacing of octroi. The Keskar Committes made the following suggestions:-

(i) Surcharge on sales tax or additional sales tax;

(ii) (a) Muncipal sales-tax;

(b) Municipal surcharge on sales tax;

(iii) Municipal turnover tax;

(iv) Other complementary levies.

These alternatives are discussed below:

SURCHARGE ON SALES TAX OR ADDITIONAL SALES TAX

14.27 A surcharge on sales tax or additional sales tax has distinctively an edge over others. The advantages are:

(a) Sales tax and octroi are indirect taxes with more or less the same tax base and almost the same economic implications. Both are passed on to the consumer and will be reflected in the price. If the abolition of octroi is not followed up by a commensurate downward revision of the prices of goods - as may well be the case — it will result in an unintended benefit to the trade and industry. A levy of sales tax would obviate such a possibility.

(b) The surcharge will have the same progression as the basic tax. Further, the cost of collection can also be kept low.

However, a surcharge on sales tax would lead to a sharp increase in the tax on items which may already be heavily taxed.

14.28 As against a levy of the kind of surcharge the various forms in which a separate sales tax could be levied are.

(1) municipal sales tax;

(2) municipal surcharge on sales tax;

(3) municipal turnover tax;

(4) a plain and simpliciter "turnover tax".

14.29 Levy of this tax is not a satisfactory solution. It will make the State tax system more complex. It will have an impact on the overall structure of indirect taxation.

MUNICIPAL SALES TAX/ MUNICIPAL TURNOVER TAX

Further disadvantages are :

(a) Local bodies may prescribe varying rates.

(b) The levy will be practicable only in the case of bigger municipalities and corporations. Smaller municipalities may not be able to raise significant funds through this levy.

(c) Trade and industry will have to keep two sets of accounts and file separate returns for essessment.

(d) Cost of collection is likely to be high.

(e) The levy will add up to the cascading effect when different municipal taxes are in vogue in the same State; relieving "input" taxation will become more complicated.

14.30 MUNICIPAL SURCHARGE ON SLAES TAX

A municipal surcharge on sales tax will not be a suitable alternative in States where sales tax is at the first point on manufacturers and importers. The levy will then benefit only those areas which are predominantly raw material producing and/or industrialised. The other disadvantages discussed in the above paragraph will also be present to a large extent.

14.31 OTHER COMPLEMENTARY LEVIES

The Kaskar Committee had in view a fuel tax, motor vehicle tax or a goods tax. Elsewhere, it has been shown that a fuel tax is not feasible. No precise information is available as to the additional revenue that will accrue if the rates of tax on public transport were revised and how it will get divided between various States. Due to differences in levels of development, there are wide variations in the number of public transport carriers as between States. From a chart of estimated vehicles in India as on 31.3.1966 (appended to the Kaskar Committee report), it is seen that whilst the number of goods vehicles is above 40,000 in Maharashtra and West Bengal, it is below 10,000 in serveral States like Assam, Jammu & Kashmir, Kerala and Orissa. The form of transport operation is also dictated by several considerations, such as, the availability of repair facilities, workshops, spare parts, etc. Inter-State corporations having a coverage over more than one State are also formed to facilitate inter-State movement. With the various facilities afforded by Railways for faster movement of goods with extended out agency services, the exact impact of a revision of rates cannot be assessed. Much will also depend on the haulage within each State.

14.32 The tax on goods will mostly be in the shape of a tax on railway freight. The Fifth Finance Commission commented that the freight structure should be consistant with the requirements of economic development as a whole and it should conform to the objectives of the economic policies of Government. Having regard to the position of Railway finances that Commission felt that the levy of a tax on railway freights was not desirable, as a large portion of the traffic, like foodgrains, coal, coke and ores, might, for policy reasons, have to be exempted. Further, such a tax would increase cost of transport which was not desirable in the interests of general economic policy. It would also necessitate a corresponding tax on road freights. For these reasons, they did not recommend a tax on freights. We are inagreement with this view.

14.33 In these circumstances, we have to find a viable alternative which will not have these drawbacks and still administratively be capable of smooth and efficient implemantation. A flat turnover tax has been suggested in more than one study by the Committees appointed by State Governments. In Maharashtra, the Wankhede Study Group suggested such a tax, limited in its operation to turnover of dealers covered under the Bombay Sales Tax Act. According to the Study Group, the turnover should exclude (i) exports, (ii) declared goods, and (iii) commodities covered by the scheme of Additional Excise duty in lieu of sales tax, but however, include even those items which are exempt under the General Sales Tax Act. The Group had recommended the levy of a flat rate and estimated that a rate of about 0.7 per cent would yield enough revenue to compensate local bodies for the loss on account of abolition of octroi. The Lakdawala Committee has also likewise recommended that the octroi should be abolished and replaced by a one per cent tax levied on turnover which would compensate the loss on account of octroi.

14.34 A PLAIN AND SIMPLICITER "TURNOVER TAX"

We are inclined to support a small turnover tax for various reasons including the fact that at least two competent Committees looking at the problem from the States' point of view have recommended it. This is superior to a simple surcharge on sales tax, because the latter would mean differential increases on the taxes on commodities taxed at different rates. A turnover tax at a flat rate,

on the other hand, would mean only a uniform addition of say, ½ per cent on turnover to the basic taxes on different commodities. This scheme does not, therefore, suffer the infirmity of the Madhya Pradesh Entry Tax. We would favour limiting the rate of turnover tax to less than one per cent and if any additional resources are needed, they should be found by the local bodies without getting into the field of commodity taxation.

14.35 While we have discussed various alternatives to octroi, our main emphasis is on getting it abolished rather than on any particular alternative to replace it. Though the suggestions made above are not free from defects, the weaknesses and adverse effects of the octroi system outweigh them. We would urge that so long as State Governments agree to the abolition of octroi they may be given reasonable latitude in the matter of devising alternatives.

TRANSITION - SUGGESTIONS

14.36 It may well be that the octroi revenues in certian areas is so large that State Governments may hesitate to do away with them, however strong the case may be for such action. As stated earlier, the operation can be carried out in two stages. In any case, octroi should be abolished in the municipal areas through which trunk road transport services operate in transit, while for the present, they could be allowed to function only in places like Bombay and Calcutta which are largely terminal points. However, this can be but a temporary expedient.

STANDING COMMITTEE

14.37 Each State Government could constitute a body somewhat like the Finance Commission which could determine the basis on which the receipts would get allocated to different local bodies. At the beginning of the exercise, the distribution could well be in proportion to octroi revenue of each recipient. Every five years, taking into account any other relevent factors, a re-allocation could be made.

B. TAXATION OF SERVICES

14.38 An important suggestion that has been made to us is that sales taxation should be extended to the sale of services. At present, there is sales taxation of goods but not of services. In many advanced countries, services rendered by lawyers, architects, accountants, consultants, etc. are taxed. The following arguments could be advanced in support of taxation of services :

(a) The pattern of economic activity is so developing that sooner or later the value added, represented by the value of services, would become large. Then it would become necessary to devise a tax which would embrace all transactions which are regarded as adding value.

(b) Such a tax would plug the loophole in the existing sales tax system and provide for taxation of "works contracts", etc., which escape taxation at present.

(c) Such a measure would, to some extent, offset the likely revenue loss if the CST rate is, by stages, reduced to 1 per cent.

(d) It could make the tax system more broadbased and more progressive because the upper income groups spend more on services while the lower income groups spend more on goods.

(e) Such a tax exist in other countries, for example, in Europe and Latin America.

14.39 At the same time, under Indian conditons, the introduction of such a tax has to be on a very selective basis. Otherwise, all types of self-employed persons even with low net incomes, and certain desirable kinds of economic activities may be adversely affected.

14.40 There are no data from which reliable estimates of the likely yield from this tax could be made. S/Shri Lakdawala and K.V. Nambiar, in their Commodity Taxation in India, have attempted an estimate.* According to the National Sample Survey, the value of total gross earnings from services in the urban sector for the year 1963-64 amounted to Rs. 226 crores, details of which are as given below :

Community Services	...	Rs. 97.68 corores
Business Services	...	Rs. 42.09 crores
Recreation Services	...	Rs. 15.24 crores
Personal Services	...	Rs. 69.83 crores
Other Services	...	Rs. 0.88 crores
	TOTAL	Rs.225.72 crores

The authors have deduced on the basis of certain growth rates that the urban expenditure on services would amount to Rs. 300.75 crores for 1968-69. This quantum again, according to the authors, is on the low side as expenditure on certain important services, independently derived from other sources would give a different picture. For example, the output value under motor vehicles repairs was of the order of Rs. 46.37 crores according to Annual Survey of Industries data for 1966. In the case of general insurance, the value of annual premium in 1966 amounted to Rs. 79 crores. Certain financial and investment services also would offer a good potential.

14.41 In the absence of adequate data, we are unable to make an estimate of potential revenue from a service tax. We suggest that if the Government consider it desirable to tax services, the revenue potential as well as practical problems of such taxation should be thoroughly examined. We are inclined to the view that if such a tax were to be introduced, it should be under Central legislation and administration, even if the proceeds from the tax go to the States. One reason for this is that the sales of services often have an inter-State character. Further, any such taxation will have to take into account its effect on the national economy as a whole. In particular, it should be important to ensure that services sold to producers are not made subject to taxation because they are in the nature of inputs. Otherwise, the same problems of cascading and distortions that have arisen now in respec of taxation of sales of goods will arise in respect of taxation of services.

* Published by Sardar Patel Institute of Economic and Social Resoarch, Ahmedabad (1972) (first edition) PP. 89-96

C. TAX ON PROFESSIONS, TRADES AND CALLINGS

14.42 When one considers the revenue position of the States, it is not necessary or proper to confine attention to the role of sales taxes. In this connection, two suggestions have been made to us. One is that ceiling of Rs. 250 fixed by Article 276 of the Constitution in respect of taxes on professions, trades, callings and employment could be raised on the ground that there is a considerable fall in the real value of the rupee since the existing ceiling was fixed. In the absence of supporting statistics, which some State Governments have said it will be difficult to furnish, it is not possible to make any recommendation as to whether a case exists for increasing the ceiling. Any action in this regard has necessarily to be preceded by incidence studies as well as a clear appraisal of the cost of collection, extent of evasion and existence of a proper machinery of enforcement. Profession tax is not strictly an indirect tax. However, a study analysing the various issues which have to be kept in view before a decision to increase the ceiling is taken as well as the uniformity that can be brought about within the existing framework included in Appendix 18.

NEED FOR A MORE COMPREHENSIVE STUDY

14.43 Another area to which attention needs to be given is the ways in which States can streamline their sales tax systems so as to eliminate evasion and leakage. This would also be one of the means of enlarging their resources. The ways in which the systems could be improved need to be studied by competent bodies which could draw attention to any harmful effects caused by the sales tax structure. A number of States have had such studies carried out. Some of these studies, looking at the problem from the point of view of the individual State Governments themselves, have urged simplification of the sales tax structure including reduction in the number of rates. Another reform that some of them have urged is a move towards a single-point tax. The studies also draw attention to problems of evasion and weaknesses in administration. We feel that this is a healthy trend. The economy of each State has its own peculiarities. Levels and sources of income differ from State to State. Therefore, studies of all connected problems in each State would be most helpful.

14.44 It would be advantageous to make the studies comprehensive enough to take into account all the resource possibilities of the State rather than one single source of revenue. Further, for a proper perspective on some of the more fundamental issues which arise on account of the ways in which Central Excises and State sales taxes overlap over a large field and to assess the revenue potential of each State, it is necessary to have a much wider view instead of confining attention to indirect taxes alone. It would be even better if the same body or agency undertook such a study for all the States and if in addition a representative of the Planning Commission was associated with the studies. We make this suggestion because a body which can review the performance of different States can enable each State to get the advantage of the experience of other States and benefit from it. Furthermore, such a study would enable some national yardsticks to be evolved by which the performance of different States in the matter of resource mobilisation can be measured, after making due allowances for the differences which exist in the tax potential of different States on account of differences in the level of their incomes as well as the nature of their economies.

D. ELECTRICITY DUTY

14.45 The levy of a duty on the sale of electricity has to be viewed from a number of angles. First of all, there is the contribution which the duty makes to the revenues of different States. In our review of the electricity duty levied by State Governments, in Chapter 4, we have had occasion to point out

that the revenue earned is not particularly significant, except for the States of Bihar, Gujarat, Maharashtra and West Bengal. A more important factor to be taken into account is that with relatively few exceptions the agencies selling electric power are State-owned. This means that the bulk of the revenue arising out of this duty could be made to accrue to the State Governments by making appropriate changes in the tariff — except for that portion which may be attributable to levies made on privately-owned electricity undertakings. The device of having a duty over and above the tariff fixed by the electricity undertakings could be justified on certain considerations, such as, that if the electricity undertakings raise their tariffs they could be accused of profiteering and that there are good reasons why the revenue should accrue directly to the State Exchequer rather than through the electricity undertakings. A further point which might influence State Governments to levy a duty which in fact reduces the profits of a company or a corporation wholly owned by them could be the consideration that corporate profits would be taxed by the Centre while, if the profit was siphoned off by the State Government through indirect taxation, it would remain with the State. Any consideration of the rationale of the levy and its rate structure cannot therefore be complete without some look at the rate structure and profitability of electricity undertakings. While we have not ourselves undertaken any such study we draw upon studies made by other authorities.

PROBLEMS OF ELECTRICITY UNDERTAKINGS

14.46 There are 18 State Electricity Boards. Some of the Union Territories/State Governments are also executing power projects departmentally. Damodar Valley Corporation supplies energy at concessional rates to certain areas in Bihar and West Bengal. Certain places like Ahmedabad, Bombay and Calcutta are covered by licensees.

14.47 Investment in power projects as at the end of 1973-74 is estimated at well over Rs.5,000 crores, Loans advanced by State Governments to Electricity Boards, at the end of 1973-74, was about Rs. 3,225 crores. The question of prescribing a certain minimum return on investments in power projects had been engaging the attention of the Planning Commission and the State Governments for quite some time. The Vankataraman Committee which made a review of the working results of State Electricity Boards urged that a phased programme should be drawn up for attaining a minimum return of 11 per cent on capital invested after meeting all working expenses and depreciation. During negotiations with the International Bank for Reconstruction and Development for loans for certain transmission projects in the middle sixties, the issue of prescribing a norm of 11 per cent return on capital invested according to a phased programme came up and the State Electricity Boards gave an undertaking that they would achieve a return of 11 per cent by the stipulated dates.

14.48 In actual fact State electricity undertakings have not found it possible to meet the interest charges on the loans advanced to them. The Fourth Finance Commission suggested that the State Governments should realise their interest dues excluding interest on fresh loans to be issued in the Fourth Plan period. The Fifth Finance Commission assumed that the State Governments should be able to realise the full interest charges on loans advanced by them to the State Electricity Boards except in the case of Assam and Rajasthan. In this connection, the Fifth Finance Commission noted that the rates for electricity varied widely according to the purposes for which it was used. Electricity for domestic use attracted higher rates. Often the charge varied according to whether it was used for lighting or heating. Large industrial users and agriculturists were charged lower rates. In the case of some Electricity Boards making losses, the rates were lower. The Commission suggested that these rates could prima facie be increased and that efforts should be made to reduce the disparity of rates in particular States by consultations between States on a regional basis.

14.49 The Sixth Finance Commission noted that despite the all round awareness of the need to achieve certain minimum rates of return on investments made in power projects, the working results of State Electricity Boards had suffered a further set back. The reasons were identified to be the following factors:

(i) increase in cost of raw materials, fuels and replacement; and increase in expenditure on account of wage awards ;

(ii) increased constraints on thermal stations for using lower grades of coal, the higher grades with lower ash content having to be reserved for production of steel ;

(iii) need for extension of rural electrification with the growing use of electricity for lift irrigation despite the wide gap between the cost of power at the point of delivery to the consumers and the actual rate charge from them ;

(iv) transmission losses ranging from 20 to 27 per cent as against the normal percentage of about 15. A saving of even 1 per cent in transmission losses would mean an additional revenue of the order of Rs. 8.5 crores per annum at the present level of generation of power.

14.50 The Sixth Finance Commission suggested a number of steps in this connection, some of which are summarised below :

(a) Unless some minimum returns are laid down in respect of investments made in power projects and are strictly enforced, the present drift would continue with serious consequences to the health of the economy.

(b) The return of 11 per cent suggested by the Venkataraman Committee and agreed to by the States when negotiating for loans from the World Bank is unattainable for the present.

Action should be taken immediately to raise the levels of tariff and improve the operational efficiency so as to secure a minimum return of at least 6 per cent.

(c) In the light of the general financial picture of the State Electricity Boards it would be highly unrealistic to recover arrears of interest to any appreciable extent.

(d) The cost of generation of thermal power was undoubtedly higher than that of hydel power. The rates of interest charged by the State Governments on the loans advanced to the State Electricity Boards also varied. Some States charged concessional rates on certain types of loads, such as, rural electrifiation. In the interests of uniform treatment it would be desirable to reassess the interest due to the State Governments on an identical basis: 5 per cent in respect of loans allocable to thermal capacity and 6 per cent in respect of hydel.

(e) The levy of electricity duty/tax on sale or consumption of electricity has limited the scope of revision of tariffs by Electricity Boards and to that extent also reduced the

operating surplus out of which interest is payable. There was also no uniform approach in the matter of the levy. It is only proper that the revenues realised as electricity duty should be set off against the interest due according to the norms prescribed so that revenue from electricity duty and interest from Electricity Board might together make up the interest stipulated as the minimum to be recovered from Electricity Boards.

(f) Though energy intensive industries might call for specially negotiated rates and under certain circumstances it may be advantageous to State Governments and their Electricity Boards to concede special rates to large projects sponsored by the Central Government as there are likely to be benefits in the form of inter-State sales tax, additional employment, etc., it would be inequitable to expect the States where such projects are located to bear the full burden for supply of power. In all cases involving supply of concessional power by State Government to Central industrial projects, the larger aspects of securing a reasonable return from power projects should not be lost sight of.

ROLE OF ELECTRICITY DUTY VIS-A-VIS TARIFF

14.51 What has been stated in (c) of the preceding paragraph makes it clear that the electricity duty is not really serving the proper function of an indirect tax but in fact falling on the agency generating electricity. Further, the Finance Commission felt that the duty collected, instead of being regarded as an addition to the revenue, should be set off against the interest payments due from the electricity undertakings. Thus, in the main, the elelctricity duty is not a source of additional revenue, its contribution being offset by a corresponding and even larger reduction elsewhere. On the other hand, the duty as levied by different States, which in turn is related to a very complex tariff structure, results in very wide variations in incidence, as the following table shows :

TABLE

A COMPARATIVE STUDY OF ELECTRICITY TARIFF AND ELECTRICITY DUTY IN SOME STATES

Type of use	Electricity tariff per kwh	Average duty per kwh	Duty as % of tariff
l) Domestic lights and fans (30 kwh/ month	24.50 (Haryana) 45 (Assam)	10.25 (Haryana 3 (Assam)	42% 6%

Type of use	Electricity tariff per kwh		Average duty per kwh		Duty as % of tariff
2) Commercial lights & fans (50 kwh/month)	32.98	(Gujarat)	8.40	(Gujarat)	27%
	75	(Andhra Pradesh)	Nil	(Andhra Pradesh)	nil
3) Agriculture 10 HP)	9	(Himachal pradesh)	8	(Himachal Pradesh)	11%
	32	(West Bengal)	6	(West Bengal)	24%
4) Small industry (10 kwh)	15	(Kerala)	1.50	(Kerala)	10%
	32	(Andhra Pradesh)	nil	(Andhra Pradesh	nil
5) Large industry (1000 kwh)	4.54	(Jammu & Kashmir)	1.68	(Jammu & Kashmir)	15%
	26.25	(Tamil Nadu)	2.89	(Tamil Nadu)	11%

14.52 Looking at the totality of the picture and having regard to the importance of electricity in the economic development of the country and also because it is a major input in almost all production, a good case could be made out for the abolition of the electricity duty. It would result in no net loss of revenue except in a few very narrow sectors. In Maharashtra and Gujarat there are major private electricity undertakings and in so far as the levy falls on them there is a net addition to revenues. In West Bengal and Bihar, the levy falls on the sale of electricity by the Damodar Valley Corporation and thus augments the revenues of these two States. If some State-owned electricity undertakings make profits, any tax revenues derived from them could be considered to be a real addition to the State's resources and also an instrument for saving on income tax which accrues to the Centre. If, on these considerations, some States or all States insist on retaining the electricity duty we would very much hope that the present system which results in such wide variations in the incidence of the duty on different classes of consumers in different States would be simplified to achieve, at least, near uniformity of treatment.

14.53 Whilst pricing is a matter in respect of which uniformity could not be achieved as it is strictly related to costs, etc., and the mode of power generation, at least no justification exists for lack of uniformity in the matter of rates of duty. The systems of levy also are not uniform. Some States have the slab system. For unmetered supplies, the pricing as well as the duty is calculated with reference to the wattage of the lamp used. There are possibilities of misuse of electricity and loss of revenue as well as duty, in such cases. In some States the duty is on an ad valorem basis, which adds upto the differential in the matter of incidence.

14.54 The Lakdawala Committee, appointed by the Uttar Pradesh Government, had noted in its report that electricity duty was being levied at differential rates. The electricity tariff is also a result of complex commercial, social, economic and other considerations. Fabrication of the tariff was rendered somewhat negatory by the addition of a differential tax which bore no relation to the tariff schedule. It, therefore, recommended that no cognizence of any consideration demanding a differential treatment of different categories of consumers should be taken note of and the levy should be at the rate of 1 paisa per unit, as all relevant considerations are taken care of in the formulation of tariff rates.

14.55 We see considerable merit in this recommendation. Such a change in the system of levy will lead to (i) simplicity in administration; and (ii) elimination of a large number of calculations and paper work. The only weakness in having a flat specific rate would be that in so far as the tariff is geared to be progressive by charging higher prices for domestic consumption than for agricultural use, the progressiveness would be somewhat eroded. A possible alternative may be to have a flat ad valorem rate. However, quite a number of States might be well advised to do away with the duty altogether. In fact State revenues from electricity as a whole can be greatly increased by paying greater attention to maintenance — which suffers because of the inadequacy of resources at the disposal of the electricity undertakings-to recoveries of dues, to reduction of losses in transmission, and a rationalisation of the tariff to make the undertakings break even.

ALLOCATION OF DIRECT TAXES FROM ELECTRICITY UNDERTAKINGS

14.56 The above discussion on electricity duty gives us an opportunity to make a point which we would commend to the Central Government. There seems to be a genuine concern among State Governments about the profits earned by State-owned undertakings being subject to income tax which means that part of what might have come to them as revenues gets transferred to the Centre. In consequence; there is a tendency to run State-owned undertakings departmentally rather than in the form of corporations which would ensure better commercial accounting and a greater attention to costs and profits. Alternatively — and there are cases where to our knowledge this is happening — certain devices, such as, indirect taxation, are resorted to in order to keep the profits of a State-owned corporation at a very low level. While there can be no question of exempting from income-tax a State-owned undertaking which may at times be operating in competition with privately owned undertakings of a similar nature, we would suggest that the Central Government may seriously consider, in consultation with the Finance Commission, whether it would not be a good thing to provide that the income tax paid by any undertaking, which is wholly State-owned, would in its totality be given to the State Government which owns the undertaking.

CONCLUSION

14.57 Our main emphasis in this Report is on getting octroi abolished because of its harmful and undesirable effects. So long as the State Governments agree to do so, they should have reasonable latitude in the matter of devising alternatives to compensate the revenue loss. In this context we have suggested certain alternatives as well as stressed the need for comprehensive studies to take into account all the resource possibilities of the State. In regard to electricity duty, we are of the view that a good case exists for its abolition. Greater attention should be paid to better maintenance of machinery and other equipment, effective realisation of dues rationalisation of tariff and reduction of losses in transmission. If the duty is to stay, it would be preferable to narrow down the variation by having a flat ad valorem rate.

CHAPTER 15

PROCEDURAL REFORMS

15.1 Among the desirable features which a sound tax system should possess, operational efficiency in the matter of assessment, collection and enforcement of the various taxes is of great importance. In an ideal system, the law and procedure for the levy and collection of taxes must be simple and capable of easy understanding. While ensuring fair, just and speedy disposal, they should result in the minimum of cost, harassment, disputes and occasions for litigation. Although several Committees and the Working Group of the Administrative Reforms Commission (on Customs and Central Excise Administration) have made many suggestions on procedural issues, a large number of which have also been implementedwe have felt it necessary to suggest reforms in some areas since we strongly believe that any shortcomings in tax laws and procedures would seriously distort the impact of the tax system as a whole.

15.2 In identifying the areas which call for immediate reform, we have had the benefit of the views and suggestions from the leading Chambers of Commerce and Industry, like FICCI and ASSOCHAM, who undertook special studies at our behest. We also held discussions with senior officers of the Customs and Central Excise administration. Arising out of these discussions, we have picked out some of the more important issues which have been repeatedly brought to our notice and which, in our view, deserve special consideration.

15.3 The most serious problem confronting trade and industry in respect of excise and customs procedures is that of in the finalisation of assessments. Fixation of drawback rates and payment of rebate claims or refunds are also matters of concern. What needs special emphasis is that, unlike in the case of direct taxes, delays and uncertainties about the amount of excise duty payable can cause serious hardship and entail financial losses. Pending a decision about duty liability, the produc: cannot be sold and it causes real hardship to the producer to be forced to keep adding to his stocks without any funds flowing in through sales. Again, if the levy is increased on revision or appeal after sales have taken place, the producer has to pay the higher duty without being able to recover it from the consumers. If there is a lowering of the duty, he gets a windfall profit, without the consumer getting the benefit of it. The possibilities of fortuitous losses and gains abound in delays. And so do opportunities for corrupt practices.

DELAYS

15.4 From time to time instructions have been issued to reduce delays. But, as far as we have been able to judge, the delays have by no means disappeared. Part of the reason for this is that the very ways in which the tax liability is defined in the law, the rules and the tariff, leave considerable room for doubt about what the precise tax liability on a particular product is. They also provide opportunities for dodges and devices to avoid and reduce the liability or to question it in a Court of law. This is a problem we shall be examining later in this Chapter. However, one question which needs to be considered right at the beginning is whether having regard to the apparent ineffectiveness of departmental instructions in eliminating delays, some statutory time limits should not be provided. The point has been made to us by departmental officers that statutory time limits may lead to hasty and not fully considered decisions, which could jeopardise the interests of revenue or of the assessees. However, the basic point is whether, when there are any doubts arising out

of any ambiguities in the legal position for which the assessee is not to blame, he should be called upon to suffer such financial losses as may accrue on account of the delay in taking a decision. In the matter of income tax, where the assessee does not suffer quite so much on account of delays in assessment, as in the case of indirect taxes, statutory time limits for completion of assessments have continued in operation for years without any undesirable consequences. Even these time limits were further drastically cut down through the Finance Act, 1968. We feel that the time has come when statutory limits should be fixed in the excise and customs laws in respect of the following:-

(i) approval of classification and valuation;

(ii) sanction of refunds, rebates and drawbacks of excise and customs duties;

(iii) finalisation of provisional assessments and assessment documents; and

(iv) decisions on short assessment demands.

For each one of the above, different time limits could be stipulated after careful assessment of the reasonable time that may be required. Such time limits could exclude the time taken by the assessee to furnish the requisite documents/particulars. It may also be necessary in cases of unavoidable delays to make a discretionary provision for grant of an extension of the time limit by the concerned Collector of Excise/Customs, but only once and after recording his reasons in writing.

15.5 With the switch-over to Self Removal Procedure under excise and the gradual shifts to ad-valorem duties, the prior approval of classification and price lists has been made a pre-requisite for effecting clearances. In other words, the assessee indicates the classification for the products and his pricing of them on which his duty liability depends, but he cannot act on them till they have been approved. Thus any delay in getting the approval would adversely affect the assessee. It has been brought to our notice that this approval continues to take an extremely long time, keeping the manufacturer in suspense about his final tax liability. The Venkatappiah Committee had recommended the fixation of statutory time limits in the matter. Though Government some time ago issued administrative instructions to ensure approval of all cases within a period of three months, the situation does not appear to have materially changed.

CLASSIFICATION AND PRICE LISTS APPROVAL

15.6 We feel that these two matters need to be treated separately. The prior approval of classification is something that cannot be dispensed with. However, the obtaining of prior approval for the price lists presents serious problems where a manufacturer is marketing a new product or selling his output for the first time. Even otherwise, we feel that this requirement is not warranted. We would suggest that in cases where a manufacturer does not generally sell to, or through, a related person, the submission and approval of the price lists prior to the removal of the goods may be altogether dispensed with. If, however, Government does not find it possible to accept our recommendation in this regard, a definite time limit for approval of both the classification and the price lists should be fixed. In most cases this should not take more than a fortnight. There may, however, be some cases where approval might be delayed owing to circumstances beyond the control of the excise department. In any event, approval should not take more than 3 months. Where this time limit

is exceeded, the classification and value claimed by the assessee should be deemed to be final. Any revision in these lists thereafter should only be prospective in operation. There would thus be no long term loss, and the only consequence in cases where the assessee's own valuation is on the low side would be to benefit the consumer — but not the assessee — for some sacrifice of revenue. Actually we feel that as with income tax, the officers concerned will take good care to ensure that there are no delays as in the event of any proceeding becoming time-barred, action can be initiated against the officers and they would become personally answerable for any losses which ensue. Similar provisions should be made in regard to finalisation of assessments — both excise and customs — made on a provisional basis.

15.7 Another important complaint of the assessee is the time taken for settling claims for refund, rebates and drawbacks. We feel that no refund or rebate or drawback claim should take more than three months to settle and this time limit too should be fixed statutorily. We understand that in U.K., 95 per cent of the claims in the Customs and Excise Department are paid within a period of 15 days. A time limit of 3 months for the grant of rebates/refunds/drawbacks would, we feel, be liberal enough. In respect of refunds, the period should count from the date on which full information relevant to the claim has been furnished by the claimant. For claims for rebate/drawback of duty in respect of goods exported, the period should start from the date of shipment of the goods. Where the statutory time limits are exceeded, on the analogy of provisions relating to grant of interest on delayed refunds obtaining under the Income-tax Act, Central Excise and Customs laws should provide for payment of interest at appropriate rates from the date of expiry of the time limit. We find that the Venkatappiah Committee had made recommendations to this effect.

GRANT OF REFUNDS/ REBATES/DRAWBACKS

15.8 Another issue on which we have heard considerable criticism is in regard to the scope and interpretation of the provisions relating to valuation for purposes of levy of Central excise duty. The new Section 4 of the Act provides that as far as practicable, the value for assessment of duty on excisable goods, where the buyer is not a related person and the price is the sole consideration for the sale, is the price at which such goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade for delivery at the time and place of removal. However, when the assessee sells his goods to, or through, a "related person", the price at which such related person sells the goods would form the basis of assessable value.

VALUATION PROBLEMS

15.9 A related person has been defined as a person who is so associated with the assessee that they have interest, directly or indirectly, in the business of each other and includes a holding company, a subsidiary company, a relative — a term which has the same meaning as in the Companies Act — and a distributor of the assessee and any sub-distributor of such a distributor. Now, it is sound principle to stipulate that the value for excise purposes should be the price that a manufacturer gets for his product at the point of his first sale except when the sale is not to a genuinely independent buyer. Thus, whenever an assessee transfers his product to another agency at an artificially low price, so as to lower his tax liability, and gets a flow-back of the advantage of the higher price at which the product is ultimately sold, it would be justifiable to adopt a price other than the one charged by the assessee as value for assessment. Even in the sphere of direct taxation and international sales, the accepted principle is that when there are "arms length" transactions, i.e.,

when the first sale is to a genuinely different party and not to one in which the seller himself has the kind of interest which would enable him to get the benefit of the higher price which the buyer may get, the original sale price is used as the basis for taxation. On the other hand, where the seller has an interest in the agency to which the first sale is made, it is the selling price which the latter gets which becomes the basis of taxation.

15.10 The concept of "related person" under excise law is primarily based on this principle. The criticism voiced before us is that in supplying this principle, the excise authorities are interpreting the concept of "related person" too widely and have, at times, taken the view that since the manufacturer anyhow has an interest in seeing the business of his agents expand, the selling price of the agent should be the basis for taxation, even if there is no other link or tie between the manufacturer and his agent.

15.11 The terms upon which a manufacturer sells to his distributors differ from case to case and commodity to commodity, depending on whether the distributor has to provide after-sales service facilities and to what extent he has to incur expenditure in pushing up sales. The profits or the commission allowed to the distributor by the manufacturer is a recompense for the services which the distributor renders and some of the expenses which he incurs. We see no justification for a presumption in law that a portion of the agent's or distributor's profits or commission is passed back to the manufacturer. The real test to apply should be whether the kind of terms on which goods are being sold to such distributors and agents, etc., would be available to any independent buyer, or whether any preferential treatment is being given to any special class of people in the expectation of what is known as a "kick-back". Applying this concept, transactions between holding and subsidiary companies and companies under the same management can clearly be treated as transactions between related persons and accordingly the price charged by the related person to independent buyers could be the basis for assessment.

15.12 We have, however, some reservations about holding an assessee's relative, distributor or sub-distributor of such a distributor, as a "related person" by definition, as it were. In the case of 'a relative', the corresponding definition in the Companies Act has been imported. The purposes served by the Central Excise Act and the Companies Act are different. Prima facie, transactions between relatives who are either lineal ascendents or descendents could be regarded as transactions between related persons, but not all relatives in the widest sense can be treated alike for excise purposes. There is much less reason for treating all agents and distributors as related persons. Even for products which are not subject to excise, agents and distributors are in existence. The standards followed for direct taxation should apply to indirect taxation also.

15.13 The relevance of the inclusive definition (in the general definition), namely, that a "related person" means a person who "is so associated with the assessee that they have interest, directly or indirectly, in the business of each other" is to free the taxing authority from the burden that is imposed by the general definition. We feel that in so far as other 'relatives' and a distributor or sub-distributor of the assessee are concerned, the onus should still be on the excise department to establish the kind of interest, whether direct or indirect, which would affect the price charged by the assessee. For this purpose, the law on the subject should be made clear to avoid future disputes.

15.14 In some cases, there is difference between the ex-factory price and the re-sale price of wholesale dealer/distributor. This difference may be due to the transport cost, or due to the

cost of any special packaging needed to facilitate the transport, or due to other elements of costs which the distributor may have to incur, e.g., in marketing or in servicing machinery items which are sold. Clearly, these elements should not be treated as part of the assessable value. Even when the transaction is with a related person, to the extent that the party concerned does incur expenditure on transport, marketing and the like, the full price realised by him cannot be said to be the price at which the assessee could have sold the product to some one who was not a related person. Therefore, it would be appropriate for the law and the rules to make allowances for it.

15.15 Similarly, there are cases where a manufacturer sells his goods at one uniform price at all destinations including even the place of removal. At present, the law does not clearly provide for abatement of the equalised freight element included in the uniform price. It has been brought to our notice that deduction on account of such equalised freight element is denied primarily on the ground that it does not represent the actual transportation cost. In principle, there is no reason to treat actual transportation cost and the equalised freight element differently. The mere fact that in the latter case it is an average expenditure does not alter the basic position that it represents the cost of transport. We, therefore, recommend that where the manufacturer establishes his average transport cost, he could be allowed to claim a deduction from the all-India price while determining the assessable value.

15.16 Another problem area relates to the type of deductions which may be allowed on account of cost of packaging. At present, a distinction is made between inner and outer packaging of goods. Further, in the case of durable containers which are returnable by buyers, the value of such containers is allowed as deduction from the sale price, but it is not done so when they are supplied by the buyer and are returnable by the assessee. Some of the departmental officers feel that it is only in respect of selected commodities, like medicines and paints, that the cost of packaging may be included while determining assessable value. Others are of the view that packaging cost should be included in the value only if goods are incapable of being sold in an unpacked condition. There is also another view that packaging cost should form part of assessable value in all such cases where goods are marketed in a packed condition. We are of the view that the cost of the packaging, without which the product cannot be sold even to a customer at the factory gate, should be a part of the assessable value. But the cost on account of special packaging and outer packaging, required for transport or to meet the special needs of any class of customers, should not form part of the assessable value.

15.17 The validity of the valuation provisions now in force, we learn, has been challanged in a number of writ petitions filed in different High Courts. It is possible that different views may be taken in different High Courts on the points at issue. A Supreme Court verdict alone could finally settle the issue. The whole process may well take years. Since there will be sales in the interregnum based on certain assumptions, it may so happen that if the decision of the Supreme Court goes in the assessee's favour they may, as a class, reap a windfall profit. There may also be the converse situation. The need for arriving at a finality as early as possible is, therefore, imperative and hence we would urge that the question of amending the law should be examined urgently. Side by side, Government could also consider requesting the Attorney-General to move the Supreme Court under Article 139-A of the Constitution to transfer the cases pending in High Courts to itself so as to enable a speedy determination of the issues involved.

15.18 The classification problems which are a major source of delays and disputes arise out of the ambiguities of the existing tariff. The present excise tariff had only a few simple entries to begin with when the Central Excises and Salt Act was enacted in 1944. During the course of its evolution, the coverage was extended gradually and most goods were brought under the excise net by creating new tariff entries, or adopting sub-entries in the existing items or sub-items, or modifying and re-wording the existing items. In the process, the tariff has become very complex and has been the subject of considerable criticism in the past. The Working Group of the Administrative Reforms Commission (on Customs and Central Excise Administration) had also remarked:

CLASSIFICATION PROBLEMS

> "We are constrained to observe that the Central excise tariff is a maze, overlaid with complexities and distorted by factors which are not germane to sound principles of taxation. Consequently, the administration bristles with difficulties for the tax-payer as well as the excise official and opportunities abound for differential treatment and exercise of individual discretion, which could generate even into discrimination, abuse of power, and corruption." *

15.19 A large number of representations. have been received by us urging that the tariff should have detailed and comprehensive classification in which the entries are precise and unambiguous in the matter of interpretation. The general view of the industry seems to be in favour of adoption of the Customs Co-operation Council Nomenclature (also known as Brussels Tariff Nomenclature — BTN) for Central excise purposes as in the case of Customs tariff schedule. The officers in the Department, whom we consulted, agree that there is an urgent need for rationalisation and simplification of the excise tariff schedule. Some have suggested restructuring of the excise tariff entirely on BTN pattern pointing out that even at present, BTN Explanatory Notes are being relied upon whenever there are classification disputes. Others have argued that we are still not as advanced as the highly developed western countries who have adopted the BTN and have recommended selective adoption of BTN entries. Suggestions have also been made that wherever the BTN tariff entries have been adopted, or are adopted in the future, they should be taken in their entirety, as partial adoption, which has been done in certain cases (like plastics and bolts and nuts) considerably reduces the scope for the use of, and reliance on, the clarifications in the Explanatory Notes to the BTN.

15.20 On a careful study of the tariff, and the views expressed before us, we feel that the time is now opportune for a total restructuring of the existing tariff schedule. The techniques of industrial production presently adopted in the country are fairly advanced; the range of manufactured goods is now much more varied and extensive than in the past and there is bound to be further sophistication and expansion in the future. Therefore, it will not be quite correct to assert that we are not yet ready for a switch-over to a detailed classification on the lines of the BTN. Excise levies already extend to most manufactured products. Further, our recommendations, if accepted, would entail appropriate classification of the various goods at present classified under the residuary tariff Item No. 68. The rationalisation of the rate structure may also require a re-wording

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*Report of the Working Group of the Administrative Reforms Commission (on Customs and Central Excise Administration) October, 1968, p. 4.

of various other tariff items. We feel that while making changes in the existing rate structure, attempt should simultaneously be made to rationalise the various tariff entries so as to evolve a tariff based upon a scientific system of classification which is not only comprehensive in scope but also more precise and unambiguous.

15.21 Adopting BTN even for excise tariff purposes, would have a number of advantages. Apart from the fact that we would have a scientific and internationally accepted comprehensive system of classification, it would minimise the classification disputes and bring about considerable uniformity in the tariff rulings on customs and excise. Furthermore, it would align the Excise and Customs tariff schedules and thereby greatly facilitate the levy of countervailing duty on imported products, which is now a subject matter of frequent classification disputes. As we have had occasion to point out, imported goods* are often subject to high countervailing duties even if the items concerned are not indigenously produced because excise tariff classification is not comprehensive.

15.22 The Tariff Revision Committee, which had gone into this problem in depth, had felt it necessary to revise the Central excise tariff on a scientific basis and align it with the customs tariff. However, that Committee felt that complete alignment of the two tariffs may not be feasible in areas where it would seriously affect the compactness of the then existing Central excise headings, or in a few other instances (like textiles), where the accepted terminology differs considerably from the nomenclature of a few imported goods. It cannot be ignored that there is some difference in the matter of administration of customs and excise levies. In many industries, there is a large number of small producers who may find it difficult to understand all the nuances of the international terminology. Judicial pronouncements have also laid greater emphasis on the commercial identity of the trade name of a commodity as a determining factor for its classification. In certain spheres, goods marketed by the indigenous producers may be better known by commercial names which are not used in BTN. On the whole, while it would be desirable to extend the application of BTN for excise purposes, it would be preferable to use the Indian commercial or trade identity for describing a range of products where the latter is considered more appropriate. We endorse the recommendations of the Tariff Revision Committee for adoption of BTN to the extent practicable, though it should now be possible to have the BTN terminology in respect of a greater number of products on account of the present universal coverage of excises. As for the timing of this revision, we feel that it needs urgent consideration and could be synchronised with the process of rationalisation of rate structure. We also feel that to facilitate correlation between the customs and excise tariff schedules for the purpose of levying countervailing duty, it might be useful if the customs schedule gives a cross reference to the excise schedule for each tariff entry.

15.23 Sometimes, the excise department revises the classification of a product with retrospective effect as a result of which the manufacturer is called upon to pay a higher duty even for past clearances. Once the manufacturer has marketed his product, he cannot recover from his customers the higher duty. We are of the considered view that unless forgery, fraud or collusion is involved, a change in the classification of a product should have only prospective effect and the authorities should not demand a higher duty for the past period. There are also cases where due to a revision in classification the duty liability gets reduced and the manufacturer may get a fortuitous benefit which cannot be passed on to his customer. It would,

CHANGES IN CLASSIFICATION

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* For examples, see para 8.70

therefore, be legitimate to hold that no refund in respect of past clearances should be permissible to the manufacturer. A provision of this kind already exists in the sales tax law of Gujarat, the validity of which has been recently upheld by the Supreme Court. A similar provision should be made in the Central excise law.

EXCISE BONDS

15.24 At present Central excise licensees have to execute different types of bonds for various purposes. Thus, a bond has to be executed for manufacturing an excisable commodity. This entails execution of a separate bond for each different commodity produced by a manufacturer if they fall under different tariff items. There is a bond for receiving certain goods under Chapter X procedure of the Central Excise Rules, and yet another for provisional assessments. Then, there are bonds for exports, for warehousing of goods, and for availing of special facilities. While these bonds are prescribed under the Central Excise Rules, several other bonds have been prescribed by executive instructions. Most bonds have to be executed either with security or surety.

15.25 It has been argued before us that these bonds do not serve much useful purpose and cause considerable inconvenience to industry and even hardship to smaller producers. Suggestions have been made for a drastic reduction in the number of bonds required to be executed at present, if they cannot be given up altogether. Though some departmental officers support their retention, as they feel that bonds exercise a moral check on the licensees, in general they are in favour of substantially reducing the number of bonds to be executed. They have pointed out that there are very few cases where the bonds have been enforced but that considerable time and energy is spent by the officers every year in verifying the solvency of sureties, payment of interest in cases of securities, etc.

15.26 The Chanda Committee had also expressed itself against these bonds, when it observed:

> "Excise bonds are at best a formality both in their form and effect, specially as in most cases they are executed for amounts much smaller than those which must be involved in any large scale frauds or defaults.....their execution, custody and drawal and disbursement of interest on securities deposited and annual verification of the solvency of sureties for all personal surey bonds involve, however, a volume of work which is not inconsiderable but which does not, in our view, yield commensurate revenue gains.*"

There is thus a strong body of opinion, which we share and endorse, in favour of streamlining the provisions relating to the taking of bonds and we would recommend that either a single bond be devised to cover all operations, or in the alternative, a drastic reduction should be made in their number.

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*Report of the Central Excise Reorganisation Committee, 1963
Chapter 4, p.51.

15.27 Normally, before any manufactured goods can be cleared from a factory, the excise duty leviable thereon has to be paid. There are, however, provisions in the Central Excise Rules for removal under bond without payment of duty and warehousing, of any specified class of excisable goods, outside the factory premises. Where this facility is permitted under the Rules, the duty is required to be paid by the licensee of the warehouse to which the goods are removed and deposited, as and when they are cleared for consumption. Only a very restricted use of this provision is being made at present, as the facility is limited to unmanufactured tobacco and petroleum products. We have received a good number of representations suggesting liberal extension of the warehousing facility and allowing movement under bond to more manufactured commodities, especially in view of the present stringent credit availability, high interest rates, etc.

WAREHOUSING OF NON-DUTY PAID EXCISABLE GOODS OUTSIDE FACTORY PREMISES AT IMPORTANT MARKETING CENTRES

15.28 The view of the officers of the department generally is against any further extension of the warehousing provisions to other excisable commodities as they fear it may lead to malpractices, apart from the administrative burden on account of checks that have to be enforced on movements and control over a large number of distributors and sales depots. Some of the officers have, however, favoured extension, though on a very selective basis, to more commodities.

15.29 We appreciate that excise being basically a tax on production or manufacture should normally be paid by a licensee at the time of removal from the licensed premises. However, Government have recognised that there may be circumstances when postponement of the collection of duty to the point from where it gets sold is justified. Having regard to the wide coverage of excise and present-day marketing conditions, we feel that in cases where the goods are generally not sold (or the sales are very few) at the factory gate, but have to be stored at a number of centres before they are marketed, and where in addition the amount of duty involved is heavy, the extension of the warehousing facility, with appropriate safeguards, may be given favourable consideration

15.30 Under rule 173-E of Central Excise Rules, a provision exists for establishing norms of production and calling upon an assessee to explain any short-fall in his production as compared to the norm. This can be a valuable check in preventing evasion. However, we gather that in practice this rule has not been made much use of. We understand that on the income tax side norms are already being applied for various industries in regard to turnover, wastages, etc. We feel that in excise matters also norms should be gradually evolved particularly to cover industries which have a large number of producers. For this purpose, there should be a closer liaison between the two departments - income tax and excise. Where the former have already got some norms established, they should be accepted without question. In other cases, some outside agencies which can be regarded as impartial and having the necessary expertise could be associated so that the norms developed are accepted without reservation.

PRODUCTION NORMS

15.31 Restrictions on removal of certain excisable products before the Budget are sometimes imposed under rule 224 of the Central Excise Rules. These lead to scarcity and to a consequential pre-Budget price-rise, whether the Budget in fact raises the rates of duty or not, as with the reduced pressure of supplies from manufacturers, retailers can hold back stocks in anticipation of a price rise. In some cases, there is also an adverse impact on production because, both physically and financially, it may be difficult

PRE-BUDGET RESTRICTIONS

for an industry to keep on producing while stocks keep on accumulating. Most of the officers of the department — especially those in the field — have expressed themselves against such restrictions being imposed, as they also cause considerable administrative inconvenience. We too are of the view that the balance of advantage will lie in not imposing any pre-Budget restrictions on clearances.

NEW CENTRAL EXCISE ACT

15.32 The Central Excise Act came into force with effect from 1944. Apart from the almost universal extension in coverage, the system of collection of the levy has undergone a radical transformation. The Chanda Committee (1963) had made several observations relating to the various anomalies and deficiencies in the Act as well as in the Schedule, and recommended that the Act should be made comprehensive, incorporating all substantive provisions of law, leaving only procedural matters to be covered by subordinate legislation. Efforts to bring into effect a new Act did not, however, go beyond a reference of the Bill to a Select Committee of Parliament.

15.33 We had specifically invited the view of the departmental officers on the need for having a new Central Excise Act. Most Collectors of Central Excise and other officers at different lower levels have favoured a comprehensive, new, Central Excise Act. Many of them have suggested that the new Act should be a self-contained, more precise and less ambiguous, piece of legislation. It should empower the officers of the excise department to discharge their various functions (instead of their making use of powers conferred under other Acts as at present). The law should also reflect Government's intentions, keeping in view the pronouncements of Courts on important issues, like definition of factory, manufacture, the power to levy duty at the time of clearance, valuation, etc. Such clarifications will also enable the conflicts in respect of certain matters to be set at rest. In regard to penal provisions, it has been felt that they are grossly inadequate in the case of commodities subject to physical control.

15.34 A self-contained and comprehensive Act replacing the existing Central Excise Act with adequate provisions to deter evasion, would make excise procedures and administration smooth, efficient and objective-oriented. We are sure that the Government would take care of the views of the trade and industry while drafting the new Bill.

ACCEPTANCE OF BILLS OF ENTRY PRIOR TO MANIFEST

15.35 We now turn to some issues of specific relevance to customs. One of the points represented to us is that the benefits envisaged under the prior entry system have been negated by the delay in the announcement of the rotation number of the vessel. As a result, the importer is not in a position to file the bills of entry and get all formalities completed within the "demurrage-free" time available for clearance of goods off-loaded from the vessel. Under section 46(3) of the Customs Act, a bill of entry normally is to be presented after the delivery of manifest except in certain special circumstances. We note that the Customs Study Team had recommended that bills of entry may be taken up for processing without waiting for the manifest, with certain procedural adjustments in regard to the 'noting' of the bill of entry at a subsequent stage, and we fully endorse the suggestion.

15.36 We have heard complaints that the processing of bills of entry is delayed at different stages in the Custom House. Consequently, the importers have frequently to pay demurrage. We note that as a result of the recommendations made earlier by the Customs Re-organisation Committee and the Customs Study Team, some changes have been effected in procedures which have generally expedited the clearance of goods. We also understand that the Central Board of Excise and Customs has prescribed specific time limits for disposal of bills of entry by various departments of the Custom Houses. In spite of these, delays continue to occur. It is reported that much time is lost in resolving import licence matters and in carrying out chemical tests required to determine classification or to resolve points of differences. Besides, it is learnt that assessing officers call for information piecemeal before making a final assessment of the bills of entry, merely to make it appear that they are not pending with the assessing officer and the delay is due to lack of complete information. We feel that there is need for far more effective supervision and control in the Custom Houses to ensure that instructions are scrupulously followed by all concerned. In this context, a suggestion has been made that a previous bill of entry showing evidence of classification and assessment of identical goods should normally be accepted without calling for literature/drawings for the subsequent imports, etc. We are inclined to share this view and recommend it for acceptance.

DELAY IN ASSESSMENT AND CLEARANCE OF GOODS

15.37 Congestion at port premises as a result of non-clearance of goods causes hardship to the importer and creates several serious problems. We feel that pending customs clearance, facility for temporary warehousing of goods, even outside the port premises, could be granted on a liberal basis under section 49 of the Customs Act. Section 61 of the Customs Act provides for warehousing the imported goods for a period of three years. It has been suggested that the period of three years is too long and may well be cut short by a year or even two. The need for such curtailment is all the more when one considers the blocking up of goods in warehouses, on the import of which foreign exchange has been expended. On the contrary, some have argued for the extension of the period of warehousing in the case of such goods as may have to be stored because of uncertainty of future supplies or which, because of specially favourable prices at the time of import, create conditions conducive for stock-piling to meet future requirements. We consider that the latter grounds are somewhat exceptional and therefore endorse the suggestion to reduce the warehousing period. A period of one year with a provision for extension by another year may be adequate in this regard.

WAREHOUSING

15.38 It has also been brought to our notice, both by Government departments as well as by the trade, that after the introduction of the new classification, duties on a number of products have gone up considerably though it was not the intention of the legislation that the mere process of re-classification under the new Customs Tariff Schedule (introduced in August, 1976) should result in significant changes in the rates of duty. Perhaps one of the reasons for the anomalies of this kind is that there has been a large scale merger of adjacent headings of the CCCN while framing the new customs tariff. Out of 99 Chapters of the CCC, nomenclature, some headings have been so drastically condensed that as many as 47 Chapters consist only of a single nomenclature heading. We understand that the main consideration behind this course was Government's anxiety to minimise

IMPORT CLASSIFICATION

the number of tariff headings in the First Schedule to the Customs Tariff Act and to eliminate entries in respect of items which are not likely to feature in our international trade. Some of the items on which the rates reportedly had gone up because of re-classification are listed below:

1. Dodecyl/Alkyl benzene
2. Cocoa beans
3. Titanium dioxide
4. Recorded tape
5. Film, positive and negative
6. Recording blank
7. Sound recording equipment and spares
8. Stereoflongs
9. Cinema laboratory equipment
10. Component parts of internal combustion piston engines
11. Component parts of hearing-aid appliances.

We understand that some corrective action has been taken in respect of some of them through the issue of notifications.

15.39 From what has been said in the preceding paragraph, it would seem that the contraction of the CCCN has not been without its impact on items which do feature in our present list of imports. Further, the fact that certain items today are not being imported does not mean that in a fast developing economy the need to import them would not arise in the foreseeable future. Much more important is the consideration that in the matter of international trade the adoption of internally-accepted standards offers many advantages. In any differences or disputes which arise, often not only the importer and the importing country but also the exporter and the exporting country, would be involved. If there is an occasion for international arbitration, the adoption of different standards by the two parties can create unnecessary difficulties and complications. In trade negotiations and in seeking tariff concessions or preferential tariff treatment for our products, whether under the GATT or outside, the use of common nomenclature has obvious advantages.

15.40 One other very important consideration of recent origin which is heavily weighted now in favour of the Customs tariff being based wholly on CCCN without any condensation is the adoption by the import control authorities of a statutory schedule which is a verbatim reproduction of the classifications in the CCCN tariff without any contraction. Therefore, in the interests of operational efficiency, specially in matters relating to import trade control, as also to ensure comparability between the Customs Schedule and the Import Trade Control Schedule, it is imperative that the Customs Schedule also is wholly CCCN-based without any contraction or adaptations.

15.41 The adoption of the more detailed classification will also help in applying the same standards and nomenclature in import trade control as well as for purposes of international trade statistics. In all these matters, if both the importing and the exporting countries follow the same system, it also becomes easier to compare statistics. The Customs Co-operation Council has already, in collaboration with the United Nations Statistical Officer, established a key co-relating each heading or sub-heading of the CCCN with a corresponding item of the Standard International Trade Classification (SITC, revised) to facilitate simple and rapid transposition of national data into SITC, revised.

We further gather that if we accept the CCCN in toto, the way would be open for India to accede to the Nomenclature Convention in due course and to become a full-fledged member of the Nomenclature Committee so as to have a voice in its functioning and decisions. Indeed, this particular advantage has influenced several countries to fall in line with a classification which was originally devised for members of the European Economic Community. By adopting the CCCN classification in toto our Customs administration would derive an immediate and continuing benefit from the stream of explanatory notes and classification opinions arising out of the deliberations of the Nomenclature Committee.

15.42 Another point, partly of procedure and partly of substance, relates to the drawback of duties borne by products exported out of the country. At present drawbacks granted on exports do not cover State and Local indirect taxes like sales tax, octroi, etc. and also any taxes on fast-waring component parts of machinery and stores consumed in the manufacturing process. The drawback rates are fixed by the Central Government on the basis of either the average duty incidence on the materials used in the manufacture of finished goods for export, or the actual duties paid by the manufacturers.

DRAWBACK OF DUTIES ON EXPORT

15.43 Various Chambers of Commerce and Trade Associations have represented that the drawback allowed is often inadequate. The basis adopted in fixing the drawback rates is the weighted average of the total Central duties (customs and Central excise) borne in the course of the production of a particular commodity. This method of computation results in inadequate drawback being given where imported materials are allowed for export production, because the import duty is much higher than the excise duty on most materials. Further, due to fluctuations in prices and the rates of duties, it becomes difficult to ascertain the average duty incidence in a reasonably precise manner, and as the approach is one of applying rules of strictness of proof of actual payment of duty in respect of the product which is exported, the exporter gets only a part of the actual duties paid as drawback. As a result of the inadequacy, Government have had to introduce schemes of cash assistance or other forms of incentives to enable exporters to compete in overseas markets.

15.44 All the earlier Committees, which examined the drawback issue, were almost unanimous in the view that the search for an exact duty content in the export product for fixing the drawback rate should be given up in favour of a more liberal approach. The Customs Study Team, in their report, * observed that —

> "keeping in view the purpose of these drawback and excise rebate schemes, viz., to give relief to our exports in the matter of indirect taxes with a view to increasing our exports, a meticulous calculation of the exact duty content is neither necessary nor desirable."

The Drawback Enquiry Committee, in their report, ** recommended —

> " the present emphasis of meticulousness and exactitude in trying to equate drawbacks due with the amounts of duty actually recovered needs to be substantially modified."

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*Report of the Study Team on the Customs Department, Part I, p. 98

**Report of the Drawback Enquiry Committee (November, 1967) p. 24,

Shri S. Bhoothalingam, in his report, * observed:

> 'The procedures governing drawback, however, still suffer from a hangover of the past when it was seriously thought that a real drawback required exact identification of when and how the import duty was originally paid. Considerable progress has already been made in standardising drawback but not neatly enough. It should be frankly recognised that strict identification is just not possible and all the shackles of the past must be altogether shaken off. The drawback admissible on various kinds of commodities should be determined by Government with the help of technical committees on a judgment of the best information available and announced as valid for a specified period."

The practice in other countries too is to be generous in allowing drawbacks. In the U.K., for example, if a particular input is being produced locally and imported as well, the exporter of the finished product used to get the rebate of the import duty payable on the input without being asked for any proof that it was the imported input and not the domestic input which was physically used in the manufacture of the product which was exported. The rationale behind this approach was broadly the consideration that since anyhow indigenous products and imported products would sell at the same price in the domestic market, the duty on the imported product which has affected the cost of manufacture of the exported product should be refunded. More important was the consideration of pushing exports by every means short of subsidisation which could attract countervailing or anti-dumping duties in importing countries. Developed countries have since moved over to a system of 'inward processing relief'. Under this system duties payable on the inputs used in the manufacture of an export product are waived ab initio so that it is ensured that the finished product is totally relieved of the tax burden and is consequently better placed to compete with products of other exporting countries.

15.45 While we may not be ready to go so far, it would be worth considering whether the manner of computation of drawback amount could be liberalised by suitable changes in the provisions relating to the fixation of drawback rates under the Customs Act, 1962, so as to obviate the precise determination of the exact quantum of duty burden on the components/ingredients of the product exported. In cases where both indigenous and imported raw materials are used in the export products, specific provisions may be made by amendment of the law to deem the entire raw materials content to be of imported origin and drawback allowed accordingly, subject, of course, to the limitations that materials of the kind used in such export products are actually imported at least to the extent of such use in the export products. This should not only make the drawback rate fuller but also obviate the need for calculating the duty incidence on the weighted average basis as is done now. Even with this liberalisation the drawback will not cover the elements of other duties/taxes, such as, sales tax and octroi on the materials used in the production of the export product.

15.46 The States have been generally reluctant to extend relief from sales tax in regard to export products because they feel they do not derive any direct benefits from the country's earnings of foreign exchange. The restrictive view in this matter is somewhat shortsighted. Exports have now been made free from sales taxation at the last two stages. But sales or purchase taxes fall at earlier stages also. Apart from this, sales taxes at present fall on most inputs which enter into the

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*Final Report on Rationalisation and Simplification of the Tax Structure (December 1967) pp. 15.16

cost of production of export products. In view of this situation, we feel that the coverage of drawback may be made more comprehensive so as to authorise refund of an amount equivalent to the element of sales tax and terminal taxes. That the amount should really come out of State revenues rather than Central revenues seems to us to be a matter of academic rather than practical significance, since all States receive sizeable subventions from the Centre.

15.47 At present, no drawback is allowed where drawback due in respect of any goods is less than Rs. 5/. The stautory provision regarding this minimum qualifying amount of drawback has been continuing for a very long time though the value of the rupee has gone down considerably. We, therefore, recommend that the present minimum qualifying amount of drawback may be raised to Rs. 25/- in respect of exports by post-parcels and Rs. 100/- for other exports.

15.48 It is obvious to the extent that due relief in respect of input taxation under the Central excise and exemption of inputs from sales taxation are introduced or extended, the burden of internal indirect taxation on exports is automatically reduced. In dealing with reforms of Central taxes as well as sales taxation, we have laid considerable emphasis on providing, wherever possible, a set-off for duty paid on inputs. If our recommendations regarding the reform of sales taxation relating to the treatment of inputs are accepted, the problem of granting drawback in respect of sales tax will not arise. Such an advantage would also accrue from the adoption of Value Added Tax at manufacturer's stage. However, under the existing circumstances, there is clearly a case for adopting a more liberal procedure suggested above.

15.49 Even after the simplification of the law and the rationalisation of the tariff, occasions will arise when assessees who feel aggrieved by a levy would challange it in a Court of law. They will naturally argue that they have been called upon to pay more than what the law provides for or permits. The tax authorities will challange this contention. Finally, the Court will give a verdict based on an interpretation of the law as it stands. Thereafter, it is open to the party who feels aggrieved about the decision to go in appeal. We are inclined to the view that so far as Government are concerned, they should consider very carefully whether, when the verdict goes against them, they should or should not accept it. If they find it unsatisfactory, they should further consider whether the better answer would not be to seek to amend the law rather than to attempt to get a higher judicial authority to reverse the legal view already taken. Whenever Government go in appeal against an adverse decision, the assessment of the pending and subsequent cases of a similar nature become difficult. The judgment given is binding until and unless it is reversed. Assessments made on the basis of the judgment would, however, have to be re-opened and higher levies made if eventually the department gets a verdict in its favour. If the assessees concerned have collected excise from their customers at the lower rate, they may suffer a severe loss if the verdict goes against them. On the other hand, if the assessees eventually win and meanwhile they have been charging to their customers the higher rate of duty claimed by the tax authorities which they are challenging, then the consumers will have borne the tax which will accrue not to the exchequer but benefit the assessees concerned. Since it is well known that for a variety of reasons it may sometimes take several years to get a final Supreme Court verdict which alone can settle the issue beyond legal challenge, the shadow of uncertainty which will fall on all assessments may, in the interim, result in fortuitous gains and losses.

REDUCING THE SCOPE FOR LITIGATION

One way to obviate it would be to ensure that whenever a verdict goes against Government, instead of filing an appeal against it as a matter of routine, there is an examination of the case on merits. If the view is taken that it is particularly desirable that the basis on which the assessment was made should be upheld, fullest consideration should be given to the possibility of making such amendments in the law as will place the matter beyond doubt. This would be a much speedier method of achieving the desired objective and eliminating the harmful effects of the uncertainties to which we have just referred. Such a course of action, besides reducing the volume of litigation, would minimise the need for making retrospective changes in law in order to eliminate fortuitous gains to assessees who have charged higher duties than are ultimately upheld under the law.

MEDICINAL AND TOILET PREPARATIONS ACT

15.50 We have also a few recommendations to make on procedural issues relating to the Medicinal and Toilet Preparations Act. At present exemptions from levy under rule 7 of this Act are subject to restrictions in regard to the mode of purchase or the person who makes the purchase. Thus, only purchases made by State owned/certified hospitals/dispensaries directly from bonded factories/warehouses get exemption from duty. This means that the exemption is not available in respect of market purchases, etc. Besides, the exemption is applicable only to alcoholic medicinal preparations and not to preparations containing narcotic drug or narcotic. Further, no distinction is made as between life saving or essential preparations and others. As these restrictions unduly dilute the benefit of the exemptions, in our view, the correct approach would be to identify the medicinal preparations containing not only alcohol but narcotic drug or narcotic which are life-saving or essential from the point of view of the health of the community, and then issue exemption notifications under the Rules, without any restriction.

15.51 The present tariff classifies the medicinal preparations (allopathic and ayurvedic) containing alcohol into two broad categories, namely, those which are capable of being consumed as ordinary alcoholic beverages (also known as restricted preparations) and those which are not (i.e., unrestricted)— the former attracting a higher rate of duty. When the question of classifying a particular medicinal preparation arises, a time-consuming procedure is required to be followed involving a reference to the Central Government, submission of samples and scrutiny by a Standing Committee. Ultimately, the Central Government, on the basis of the advice tendered by the Standing Committee, declares the category in which the preparation should be placed and the item or sub-item, or both, in the Schedule to the Act under which the preparation falls. We feel that the better course would be to provide in the law itself appropriate criteria for classifying medicinal preparations into restricted and unrestricted categories. This would eliminate subjective judgment in the matter of categorisation and reduce disputes. Besides, since the assessing officers would then be able to categorise the products straightaway after a chemical test, this would minimise considerably the delay involved in classification.

15.52 A related question is whether a medicinal and toilet preparation which in its final form does not contain alcohol but for the manufacture of which alcohol has been issued, is covered under the Act. The States have generally taken the view that where alcohol has been issued, the end product should be deemed to contain alcohol and if this view is contested, the States do not issue alcohol for the manufacture of such preparations. We are of the view that if the end product in its final form does not contain alcohol, no duty should be levied under the Medicinal and Toilet Preparations Act. To put the matter beyond the pale of controversy, it would be desirable to write the correct position in the law itself. Sometimes jurisdiction is asserted by more than one

State in respect of the same product. This particularly happens when the ingredients of the medicinal and toilet preparations are manufactured in one State but they are bottled or capsuled in another. In such cases, multiple levies on the same product should be avoided and each State should levy duty only on that part of the final value of the product which is added within its territory.

ADOPTION OF METRIC SYSTEM

15.53 Yet another point requiring consideration is the continuance of the practice of determining duty in some cases at a specific rate per litre of the strength of London-proof spirit. This stipulation entails finding of the specific gravity at a particular temperature and conversion thereof to the specific gravity at 60 degrees fahrenheit. Thereafter further calculations have to be made. The whole exercise is time-consuming besides being antiquated. We feel that the metric system may be adopted, thus severing the linkage with the London-proof spirit. If this is done the rate of duty would require suitable upward revisions.

CHAPTER 16

ADMINISTRATIVE FRAMEWORK

16.1 The reforms we have suggested earlier on procedural issues and the restructuring of the tax rates that we have recommended, would, we hope, give considerable relief and freedom from irksomeness. However, it is necessary simultaneously to ensure that the administration of the tax laws while being objective and much more sympathetic and human in its approach, does also enable taking of expeditious decisions. Towards this end, apart from the changes in tax laws and procedures, we would like to emphasise the desirability of bringing about appropriate improvement in the administrative framework so as to take adequate care of the human machine whose role in making the system work smoothly and efficiently is pivotal.

16.2 We would not like to concern ourselves with details on such issues as recruitment, staffing and promotion, but would like to make some observations which would be relevant for the streamlining of the administration. The first and foremost task should be to enable the general public, more particularly the assessees themselves who have to pay the indirect taxes, to understand clearly the tax laws including their tax liability, obligations and rights. At present, even the tax collectors, are often unable to give clear interpretations on these matters, and it is not surprising that the assessee feels confused. Even after the laws have been streamlined and procedures simplified, it would be necessary to make the public and particularly the assessees aware of these in a language which they can comprehend. Since every one cannot read an official notification and get its true import, to explain each law, notification or procedure in the language of the layman should be one of the objectives of a reformed administration. We note that there are public relations officials attached to the tax administration. We do agree that a public relations approach has to be built into the tax machinery so that people of small means, particularly the small producers who cannot get expert legal advice are fully aware of their rights and, of course, also their obligations. In this context, we would also recommend that it would considerably aid efficiency and public relations alround, if publications like working schedule, tariff guides, and a digest of important rulings by the courts and by Government are brought out and regularly updated.

16.3 It is quite possible that a detailed investigation which we ourselves have not been able to undertake will bring out that inadequacy of staff, either quantitative or qualitative, is at the root of much of the delay that takes place. We shall be happy if pursuant to the implementation of the recommendations we have made, the workload goes down resulting in the existing staff itself being adequate to meet the commitments arising out of the revised laws and procedures. But in so far as this does not happen, we would certainly hope that Government would not grudge the extra staff needed for the smooth collection of revenues without the present delays and other difficulties. However, an aspect that would call for special mention is the need for providing adequate training for customs and excise staff. During the course of evidence, almost all the departmental officers felt that the existing facilities should be improved both in terms of coverage and quality. At present, it is learnt that an officer of the department is put through formal training probably once or twice in a career of about 30 years. The course contents also mostly relate to customs and excise laws. In the context of the growing complexity of customs and excise administration and with the switch over to more account based controls under excise, we are of the view that there is an immediate need to reorient the training of the officers of this department to meet the professionalised needs of administration. Besides, periodic refresher courses should be conducted for middle-level and senior

officers to bring them up-to-date with regard to developments in the overall tax system and in the economy in general.

STRENGTHENING OF THE BOARD

16.4 The Central Board of Excise and Customs is the Chief Executive Authority, administering the Customs and Central Excise Acts. This Board, along with the Central Board of Direct Taxes was, constituted with effect from 1.1.1964 in place of the Central Board of Revenue, by virtue of the powers conferred by the Central Boards of Revenue Act, 1963. Section 3(2) of the Act provided that the membership of each Board should not exceed five. Under the Central Board of Excise and Customs (Regulation of Transaction of Business) Rules, 1964, the Central Government is empowered by notification to appoint one of the Members to be its Chairman.

16.5 Since 1964, a large number of tax laws have been enacted. The tariff has become more complex. There are complaints that the administration is not yet adequately geared or oriented to meet the challenges arising on account of the phenomenal increase in its responsibilities. One of the major factors which has contributed to the difficulties in ensuring a smooth and efficient functioning of the two Boards is the limit on the number of Members placed by the Central Boards of Revenue Act, 1963.

16.6 We, therefore, recommend that the restraint stipulated by the Act, limiting the number of Members should be removed.*

RE-ORGANISATION OF COLLECTORATES

16.7 With the progressive increase in excise coverage and the growing complexity in the tariff and valuation provisions, the work in some of the Collectorates has become unwieldy. This has resulted in the Collector not being able to concentrate upon some of the core technical problems in respect of which his personal involvement is necessary. The Collectors are also not able to concentrate on inspections of all their field units due to their other preoccupations and priority commitments. All these tell upon the efficiency and the general health of the Collectorates, calling for immediate remedial measures. The Venkatappiah Committee had recommended that ordinarily a Collectorate should not have more than four to six divisions. We endorse this recommendation.

INTERNAL AUDIT

16.8 A sound internal audit system is a basic requisite for effective control, especially where public revenues are involved. At present, arrangements exist in Custom Houses and Excise Collectorates to carry out internal audit. On the excise side, this function is shared between the divisional set up and the headquarters organisation. But the basic infirmity that this kind of arrangement suffers from is lack of independence. To be efficacious, the audit function should be performed by an independent organisation (within the control of the Central Board of Excise and Customs) manned by officers drawn from different field formations and possessing specialised knowledge or training in examining production and cost accounts. We would urge that the nature of audit should be critical and qualitative so as to bring out cases of evasion, and misdeclaration of value and classification and also to throw light on the lacunae in the law and procedure. It should also be ensured that prompt follow-up action is taken on audit objections involving revenues, after due consideration of the concerned

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* The Customs, Central Excises and Salt and Central Boards of Revenue (Amendment) Bill, 1977, introduced in Parliament on 19th December, 1977 contains a provision to raise the maximum strength of the Members of both the Boards from five to seven.

issues. Besides, major audit points should be brought to the notice of all the field formations so that suitable steps could be taken to rectify similar mistakes.

STATISTICAL BASE AND RESEARCH AGENCY

16.9 It is well recognised that an adequate information system is a prerequisite for the effective administration of broad-based or comprehensive taxes such as extended excises and general sales taxes. The information system should generate data not only on the yield of taxes from various commodities and from various regions but also the information needed to analyse the impact of taxes on the economy. The system should be so devised that there would be a two-way flow of information - basic data flowing from the field to the Central Agency (through regional offices) and processed information and analysis flowing from the Central Agency to field formations. In order to fulfil these objectives, it would be necessary to equip the tax department with necessary staff not only for the collection of data but also for its analysis. Further, the design of data collection should be formulated after carefully considering the scope and depth of information needed for purposeful analysis.

16.10 As at present, there is for Central Excise and Customs, a Directorate of Statistics and Intelligence with a separate wing called the Central Exchange for Assessment Data. The Directorate compiles data on production, clearance and tax collected in regard to excises; and on imports, exports and duty collected in regard to customs. Information on the pattern of trade and distribution or on the pattern of use of major excisable products is, however, not being collected, nor does the Directorate undertake any analysis of growth and elasticity of revenues or the impact of the tax system on various sectors of the economy. We understand that such an analysis is not being carried out in any other part of the Ministry of Finance also (except for a limited amount of work done in the Fiscal Policy Unit of the Department of Economic Affairs), with the result that no proper analysis of empirical data is at all provided for the formulation of tax policies in the sphere of indirect taxation. It is significant that almost all the analysis needed for the Committee's work had to be carried out on an ad hoc basis by the Secretariat or had to be specially commissioned. While certain studies could only be undertaken at intervals or on an ad hoc basis several others needed for policy formulation would have to be carried out on a continuing basis. We would recommend that steps should be taken -

(a) to enlarge the coverage of data collection;

(b) to strengthen the data collection wing; and

(c) to strengthen the Research Wing so as to equip it for carrying out more comprehensive studies on a continuing basis, if necessary in collaboration with Research Institutes.

16.11 The process of data collection as well as analysis would be considerably facilitated through computerisation. Regional Computer Centres should be linked to a Central Data Processing Unit.

16.12 At the level of States, the information system relating to taxes is even more inadequate. We found that the States could not furnish even commodity-wise yield of sales taxation on a firm basis for more than a year or two. Analysis of the impact of State taxes is also not being carried out except on an ad hoc basis from time to time. Research Wings are either non-existent or very

inadequately staffed. In regard to certain other State taxes, information is not generally available even in respect of the number of tax payers in different areas or the total value of the bases. In the spheres of State taxation, as in the sphere of Central taxation, improvement in the information system is one of the major ways in which formulation of tax policy could be made on a more rational basis. Empirical analysis would also enable a better coordination between the policies of the Centre and the States.

16.13 Suggestions have also been made that in order to ensure uniformity and safeguard revenue, a central valuation unit should be set up on the pattern obtaining in the U.K. to advise the Collectors on valuation under the central excise as well as Customs laws. The Unit could concentrate on the study of trading relations and terms of agreement between the importers and suppliers of goods, and the relationship of manufacturers with wholesalers, distributors, etc. It should keep detailed records of pattern of import, export, indigenous production and distribution of goods, and provide relevant and useful information to the field officers.

16.14 In the last few years, the volume of imports has gone up considerably and even the pattern of imports has shown significant changes. In the field of excise, the tariff has become much more complex and excise duties now extend to all commodities as against their selective coverage till recently. It has been brought to our notice that in comparison to the increased load of work in recent years, the test facilities and the number of test laboratories in the customs and excise departments are totally inadequate. This causes considerable delays in the receipt of test reports, often holding up clearance of goods and resulting in uncertainty in the determination of the final duty liability. It has also been represented that the technical literature available with the test laboratories under the Board's control and the departmental libraries is not always up-to-date. The lack of modern testing equipment also leads to frequent differences of opinion between the department and the assessees, as the latter base their contentions on the latest available technical literature and the tests conducted by better equipped testing laboratories run by other agencies. We have also received suggestions from a number of departmental officers for modernising and strengthening the existing laboratories as also opening new ones. Many have suggested that each Central excise collectorate should have one such laboratory.

TEST LABORATORIES AND TECHNICAL LITERATURE

16.15 While we would prefer the tariffs to be so rationalised as to minimise the need for chemical tests and frequent technical opinions, such tests etc., cannot be altogether eliminated so long as we have a differential system of duties and a large number of exemptions and ambiguous tariff entries.

16.16 We note that matters relating to the test facilities in general as well as the reorganisation of the customs and central excise laboratories in particular have been studied in the near past by the Customs Study Team (1967) and the Venkatappiah Committee (1975). We have, therefore, not made any special studies, in regard to the adequacy or otherwise of the existing facilities. The Working Group on Customs and Central Excise Administration set up by the Administrative Reforms Commission (1968), also noted that one of the major complaints put forth by the representatives of the industry related to the delays in obtaining test results. In that connection, the group noted that the number of existing laboratories was inadequate and they were not adequately equipped. It, therefore, recommended the setting up of regional laboratories at convenient points of industrial importance. Nevertheless, from the trend of the representations, it appears deficiencies and inadequacies still continue to exist, in respect of test facilities and other ancillary matters like

promptness in the matter of tests, etc. We would, therefore, reiterate that Government should take early steps to eliminate them.

APPEALS AND REVISIONS

16.17 Presently, an appeal against a decision or order passed by an officer lower in rank than a Collector lies to the Appellate Collector of Central Excise/Customs concerned, while an appeal against a decision or order passed by a Collector lies to the Central Board of Excise and Customs (the Board). As the department itself cannot go in appeal against the orders or decisions passed by its own officers even if such orders or decisions are prejudicial to revenue, there is a certain one-sidedness about these appeals. Revision applications against the orders-in-appeal passed either by the Appellate Collectors or by the Board lie to the Central Government. Revision applications against appellate orders passed by the Appellate Collectors are decided by a Joint Secretary or two Joint Secretaries sitting as a bench depending on the nature of the case and against those passed by the Board are dealt with by a Special Secretary to the Government of India, Ministry of Finance (Department of Revenue). Important cases are decided sometimes, but not always by a bench presided over by the Special Secretary. Apart from this, the Central Government may of its own motion or otherwise call for and examine the record of any proceeding in which any decision or order has been passed for the purpose of satisfying itself as to the correctness, legality or propriety of such decision or order and may pass such orders on it as it thinks fit. The Board is, however, not empowered to exercise powers of revision against orders-in-appeal.

16.18 In essence, therefore, all the appellate and revision functions are exercised by the executive. The fact that these officers are not immune from criticism by Revenue audit, it has been argued, inhibits their independent functioning resulting sometimes in a pro-revenue bias. The view has been repeatedly put forward that there should be an independent machinery to resolve disputes under customs and central excise laws to replace the present arrangements. Such a change would be in keeping with Article 50 of the Constitution which envisages separation of the executive and judicial functions. An independent body would inspire public confidence, which the decisions of executive officers, no matter how impartial they try to be, do not.

16.19 Similar views have also been expressed by the Supreme Court in the case of Siemens Engineering and Manufacturing Company of India Limited Vs. Union of India and Others /1976 AIR SC, page 1785/. The Court observed thus:

> "In fact, it would be desirable that in cases arising under Customs and Excise laws, an independent quasi-judicial tribunal, like the Income-tax Appellate Tribunal or the Foreign Exchange Regulation Appellate Board is set up which would finally dispose of appeals and revision applications under these laws instead of leaving the determination of such appeals and revision applications to the Government of India. An independent quasi-judicial tribunal would definitely inspire greater confidence in the public mind".

16.20 Almost all the Commissions, Committees and other similar bodies who have considered this matter in the past, starting with the TEC (1953-54) have recommended the setting up of an independent machinery for this purpose. For facility of reference, the observations of the various Commissions and Committees are reproduced in the Annexure to this Chapter.

16.21 The main argument we have heard in support of continuing the present procedure under which final decisions are taken at the level of the Central Government is that in the matter of indirect taxation quick decisions are necessary, whereas, because of procedures a judicial tribunal would follow, its decisions are prone to delays. We recognise that delays in settling issues pertaining to indirect taxation must be avoided. But there is no reason to assume that the replacement of an executive agency by a quasi-judicial one must necessarily mean the adoption of dilatory procedures.

16.22 After carefully considering all aspects of the matter, we are of the view that: (i) a two-tier appellate machinery with a Tribunal Independent of the Board for hearing appeals both on facts and law from the first court of appeal should be established. While appeals which lie to the Appellate Collectors could continue to be disposed of by them, the second appeal arising therefrom should be heard by the proposed Tribunal; (ii) where the original order of adjudication is passed by an Additional Collector/Collector, the first appeal should itself be to the Tribunal. All relevant procedural provisions in the Income-tax Act can, with suitable adaptations, be incorporated into the Central Excise and Customs Acts, with this variation, namely, that the procedure in vogue under the Income-tax Act whereby an assessee/department has to move the Tribunal for drawing up a statement of the case to the High Court be dispensed with. This would help in minimising delays. The Tribunal's decisions on facts should be final. A reference could be taken to the High Court only on points of law with a further appeal to the Supreme Court. Where on account of the conflict of decisions of different High Courts in respect of any particular question of law, it is necessary to get the final opinion quickly, the Tribunal should be empowered to refer such cases directly to the Supreme Court. Since in the revised set up, the Board will not be hearing any appeals and instead the Tribunal will be deciding the appeals against orders of the senior Collectors of customs and central excise also, the members of the Tribunal should have a status at least equal to that of Members of the Central Board of Excise and Customs with a higher status for the Chairman. The Tribunal will regulate its own procedure so as to facilitate the disposal of appeals. For the present, the Tribunal should have six members. To inspire the necessary confidence, the membership should have an equal sprinkling of professional experts and judicial officers besides departmental officers.

CONSTITUTION OF INDEPENDENT TRIBUNAL

16.23 For the officers to be drawn from the department it could be laid down that they should have served at least 4 years as Collectors of Central excise/customs in Level I of the Customs and Central Excise Service. The professional Members could be selected from the Chartered Accountancy and Cost Accountancy professions as well as from organisations like the Bureau of Industrial Costs and Prices so that the persons selected would have experience in fields like Costing, Import and Export trade, etc. For judicial members, it could be laid down that they should have served at least as District and Sessions Judges or in equivalent posts in the judicial service for a minimum period of seven years.

16.24 The question as to whether the Tribunal will need further strengthening and whether it should constitute Benches at the headquarters of different Collectorates, could be examined, on an appropriate future occasion, after the initial transitional period, and by the end of which the Tribunal would have been well established.

16.25 The present practice of suo moto revision may continue except that it should be exercised by the Collector if the original order or decision was passed by an officer lower in rank than a Collector and by the Board in respect of an order or decision of the Collector.

16.26 In order to maintain the independence of the Appellate Collector, a provision should be inserted in the Customs and Central Excise Acts to the effect that the orders, instructions or directions of the Board shall not either interfere with the discretion of the Appellate Collector in the exercise of his appellate functions or require the Appellate Collector to dispose of a particular case in a particular manner.

16.27 A question that arises for consideration is whether Appellate Tribunals as envisaged above, could be left to deal finally with classification disputes and to bring about uniformity of practice on classification matters. The present practice is that a measure of uniformity in classification matters is sought to be brought about through executive instructions and tariff conferences with Collectors presided over by a Member of the Board. This arrangement has not been found to be quite satisfactory as such decisions are neither binding on appellate authorities nor even on the assessing officer. This is because, in the Orient Paper Mills case (CAS 659-664 of 1968) the Supreme Court held:

> "If the power exercised by the Collector was a quasi-judicial power - as we hold it to be - that power cannot be controlled by the directions issued by the Board. No authority, however, high placed can control the decision of a judicial or a quasi-judicial authority. That is the essence of our judicial system. There is no provision in the Act empowering the Board to issue directions to the assessing authorities or the appellate authorities in the matter of deciding disputes between the persons who are called upon to pay duty and the Department. It is true that assessing authorities as well as the appellate authorities are judges in their own cause; yet when they are called upon to decide disputes arising under the Act they must act independently and impartially. They cannot be said to act independently if their judgment is controlled by the directions given by others. Then it is misnomer to call their orders as their judgment; they would essentially be judgments of the authority that gave the directions and which authority had given those judgments without hearing the aggrieved party. The only provision under which the Board can issue directions is r.233 of the rules framed under the Act. That rule says that the Board and the Collectors may issue written instructions providing for any supplemental matters arising out of these rules. Under this rule the only instructions that the Board can issue are that relating to administrative matters; otherwise that rule will have to be considered as ultra vires s.35 of the Act."

16.28 Uniformity and an early final ruling on classification are of utmost importance for the healthy growth of trade and industry and for normal interplay of commercial competition. By the very nature of its work, the contemplated Appellate Tribunal will be dealing with several matters of which classification will be one. Consequently, the required priority for disposal of classification appeals cannot always be ensured. There may also be lack of uniformity when different benches of the Tribunal dispose of appeals in classification matters. The desired objectives of uniformity and an early final ruling which is needed in respect of classification disputes cannot be achieved through the normal appellate machinery. The balance of advantage would, therefore, lie in a single body being vested with the necessary authority to dispose of disputes relating to classification, such decisions being made binding on all concerned including the Appellate Tribunal.

16.29 We, therefore, feel that an All India Classification Tribunal should be set up, with the members having appropriate status and qualifications keeping in view that not only will its decisions

be binding on the assessees, assessing officers, appellate authorities including the Appellate Tribunal but, it will also hear matters referred to it by the Board. As the work of this Tribunal will be highly technical, it will be necessary to confine the selection of its membership to persons who by virtue of their training and experience can give sound decisions which will be respected by all. The Chairman and other Members of the Classification Tribunal should be appointed by the Central Government from amongst persons of integrity and outstanding ability having special knowledge of and experience in problems relating to customs and central excise. If a Member or Chairman of the Board is appointed to the Classification Tribunal, he should cease to be a Member or Chairman of the Board. An appeal should be allowed to the Supreme Court against the decision of this Tribunal only on points of law.

16.30 In order that the proposed Classification Tribunal is not unduly saddled with all types of references, the procedure for reference to the All India Classification Tribunal should be carefully defined. In the light of the experience gained on the working of the proposed All India Classification Tribunal for, say, five years, the position could be further reviewed if need be and the span of coverage modified appropriately.

16.31 We also recommend that in the interest of uniformity, every State should have also a uniform pattern of appellate procedure, providing for first appeal to an Appellate Assistant Commissioner of Sales Tax, further appeal by the department/assessee to a Sales Tax Appellate Tribunal and references on points of law to the High Court/Supreme Court. Such a procedure obtains in several States. We recommend that the remaining States should also fall in line.

ANNEXURE TO CHAPTER 16

APPELLATE TRIBUNAL - OBSERVATIONS OF COMMISSIONS AND COMMITTEES

Taxation Enquiry Commission (1953):

"Having examined the matter from the point of view of the need for moderating the claims of abstract justice by practical consideration of administrative efficiency, we think that it is not expedient to introduce in the customs administration exactly the same type of appellate machinery as exists in income-tax. We would leave the appellate powers of the Central Board of Revenue as they are, but suggest that revision petitions against the orders of the Central Board of Revenue or the Collector of Customs should be disposed of by a Tribunal which should be independent of the Ministry of Finance and should consist of at least one judicial member who should be either a serving or a retired High Court judge, and one member who has had experience of Customs administration."

Tobacco Expert Committee (1956-57):

"Taxation Enquiry Commission's recommendations for setting up a Tribunal to decide revision petitions against the Collectors and the Central Board of Revenue and the appellate orders should be implemented".

Customs Re-organisation Committee (1958):

"We agree with the (Taxation Enquiry) Commission's views except to the extent that we consider that the association of a suitable representative of the import-export trade as an additional or third member of the tribunal would be an improvement and would help to secure more informed, and therefore, objective decision".

Estimates Committee (1959):

"Revision petitions are, however, again considered by the Chairman, C.B.R., even though as Additional Secretary to the Government and assisted by a Joint Secretary of Ministry of Law. The Committee feel that as a result the purpose of the law is not fulfilled. They, therefore, recommend that the feasibility of setting up a separate Tribunal to deal with revision petitions independently of the Central Board of Revenue as suggested by the Taxation Enquiry Commission might be reconsidered".

Central Excise Re-organisation Committee (1963):

"While the present appellate channels may continue, the final stage of the revision application should be abandoned; instead an Appellate Tribunal which would go both into the facts of the case as well as point of law should be set up. The Tribunal should have one Member of status and experience comparable to that of a serving or retired High Court Judge and one or two members with working experience of technical excise work. The Tribunal should not be subordinate to the Chief Excise Authority but there is no objection to its being within the Ministry of Finance".

Tariff Revision Committee (1966):

"We have considered the above arguments very carefully and we feel on balance that a tribunal structure should be available in respect of tariff cases. The present system, whatever may be the advantages claimed for it, is due for change, particularly since it has been unfavourably commented upon by several bodies, and to date seems to have failed to satisfy the Commercial public. We agree with the consensus of the opinion expressed before us, namely, that the first appeal may lie to the departmental authorities as at present. A second appeal or revision petition may lie to the tribunal whose decision should be final, but with a provision for reference to the High Courts on points of law.

We do not propose here to go into details like the constitution of the tribunal, its location and so on. Obviously, however, the members of the tribunal should be persons of high status, wide administrative experience and knowledge of commercial practices and above all imbued with public spirit. We would not like to make any other specific recommendations but would point out that in view of the pressing need for satisfactory and acceptable arrangements for settling disputed points in regard to the principles of classification and issuing authoritative rulings in this regard, such a body should be independent of the concerned administrative department."

Study Team on the Customs Department (1967):

"In view of all these considerations we recommend the setting up of appellate machinery somewhat on the lines of income-tax appellate tribunals with suitable modifications. They may deal with revision applications against the orders of the appellate Collectors and also appeals against the orders of the Collectors. This would mean that would be no further revision application in respect of cases originally decided by Collectors and disposed of at the appellate stage by the appellate authorities. These authorities would have to function in a quasi-judicial manner with due regard to the principles of natural justice."

Working Group of the Administrative Reforms Commission on Customs and Central Excise Administration (1968):

"There is considerable public opinion in favour of establishment of independent appellate tribunals. These may be set up and the objections of cost, delay and uncertainty met by the undermentioned measures:

(a) A fee sufficient to deter frivalous appeals could be prescribed and refunded if the appeal succeeds. An alternative of departmental review of original decisions by a hierarchy of superior officers for cases involving small amounts may also be provided.

(b) The appellate tribunals may only deal with cases at the second stage of revision applications.

(c) It should be provided that the Board's general rulings will be binding on the appellate tribunal also except that the appellate tribunal could refer any such ruling which is not acceptable to it, to Supreme Court for a final decision, the Supreme Court's final decision, holding the field prospectively."

Central Excise (SRP) Review Committee (1975):

"A Tribunal should be set up to deal with cases at the revision stage, i.e., those in which orders in appeal have been passed by the appellate Collector or the Board. The Tribunal should be competent to look into the question both of law and of fact. It should not be administratively attached either to the Central Board or to the Department of Revenue and Insurance. Preferably, it should be attached to the Ministry of Law.

The Tribunal should consist of a Chairman and a minimum of two members. This number may be added to depending on the volume of work. The Chairman of the Tribunal though he need not necessarily be drawn from the judiciary, should have the status of a High Court Judge."

General Agreement on Tariff and Trade, 1948
(to which India is a signatory):

"Each contracting party shall maintain, or institute as soon as practicable, judicial, arbitral or administrative tribunals or procedures for the purpose, inter alia, of the prompt review and correction of administrative action relating to customs matters. Such tribunals or procedures shall be independent of the agencies entrusted with administrative enforcement and their decisions shall be implemented, by and shall govern the practice of, such agencies....."

/Art. 10, para 3(b)/

"The provisions of sub-paragraph (b) of this paragraph shall not require the elimination or substitution of procedures in force in the territory of a contracting party on the date of this Agreement which in fact provide for an objective and impartial review of administrative action even though such procedures are not fully or formally independent of the agencies entrusted with administrative enforcement. Any contracting party employing such procedures shall, upon request, furnish the CONTRACTING PARTIES with full information thereon in order that they may determine whether such procedures conform to the requirements of this sub-paragraph".

/Art. 10, para (c)/

Law Commission (1959):

The Commission has not made any specific recommendations about customs adjudications, but among its recommendations in the matter of reviews of administrative decisions in general, the following are relevant to customs adjudications:

"(a) In the judicial and quasi-judicial decisions an appeal on facts should lie to an independent tribunal presided over by a person qualified to be a judge of a High Court. He may be assisted by a person or persons with administrative or technical knowledge. The tribunal must function with openness, fairness and impartiality as laid down by the Franks Committee.

(b) In the case of judicial or quasi-judicial decisions, an appeal or a revision on a question of law should lie to the High Court. Special machinery can, if necessary, be provided to assist the High Court Judge. The suggestions made by the Spens Committee may be adopted in this connection."

The Committee on Administrative Tribunals and Enquiries set up by the Command of Her Majesty of England, presided over by the Right Hon'ble Sir Oliver Franks, G.C.M.G., K.C.B. (1957).

"104: The existence of a right of appeal is solutary and makes for right adjudication. Provision for appeal is also important if decisions are to be of reasonable consistency. Finally, the system of adjudication can hardly fail to appear fair to the applicant if he knows that he will normally be allowed two attempts to convince independent bodies of the soundness of his case.

105: The first question is the extent to which appeals should lie to the courts or to further appellate tribunals. An appeal to the courts on matters of fact would not, we think, be desirable since it would constitute an appeal from a body expert in the particular subject to a relatively inexpert body. In the absence of special considerations we consider that the ideal appeal structure for tribunals should take the form of a general appeal from a tribunal of the first instance to a second or appellate tribunal. By a general appeal we mean an appeal on fact, law or merits. We do not think that it is necessary for appeals to the second or appellate tribunal always to be heard orally. As a matter of general principle we consider that appeal should not lie from a tribunal to a Minister.

xx xx xx xx xx xx

107: We are firmly of the opinion that all decisions of tribunal should be subject to review by the courts on points of law. This review could be obtained either by proceedings for certiorari or by appeal. If, as we recommend, tribunal are compelled to give full reasons for their decisions by error of law in such a decision would subject the decision to quashing of order of certiorari in England, and it is now clear that the fact that the decision of the Tribunal may be expressed in the statute as "final" does not oust this jurisdication."

CHAPTER 17

VALUE ADDED TAX — BASIC FEATURES

17.1 One of our terms of reference requires us —

> "To examine the feasibility of adopting some form of Value Added Tax in the field of indirect taxation where appropriate and, if found feasible, to suggest the appropriate stage to which it should be extended, having regard to the Indian conditions, i.e., whether the stage of coverage should be manufacturers, wholesalers or retailers."

17.2 The system of value added taxation has attracted considerable attention after the recommendation of the Neumark Committee in 1962 that all countries of the European Common Market should adopt a Value Added Tax (VAT) and its subsequent adoption by the Council of the European Economic Community (EEC) as the common form of sales taxation for its member States. It is a popular topic of discussion whenever the question of reform of a country's indirect tax system is considered. The growth in world trade and international competition has particularly led many countries to study the feasibility of adopting some form of VAT to avoid the adverse impact of their tax system on export prices and the competitiveness of their industries. Apart from the EEC countries, VAT in some form have also been adopted by several countries in Africa and Latin America.

17.3 Although there has been an extensive discussion of the system of VAT in the public finance literature in recent years, it is still an unfamiliar form of taxation in this part of the world. Sufficient material is also not easily available for those interested in understanding its basic features as well as their operation in actual practice — most of the existing literature has been written by the experts on taxation for their fellow experts and a good part of it is not in the English language. As a background to our discussion of the applicability of VAT to Indian conditions, we shall, in this Chapter, give a theoretical exposition of the characteristics of VAT as also a description of the main features of its operation in a selected number of developed and developing countries. We deal with the desirability and feasibility of its adoption in India (including the complex problems that would have to be tackled) in the next Chapter.

17.4 In the course of production and distribution, goods usually pass through a number of stages before reaching the final consumer. Primary materials go through successive stages of processing or manufacture before they are converted into goods for final use — either consumer or capital goods. After manufacture the good again pass through the wholesale and retail stages before they ultimately reach the final users. At each stage, in the chain of production and distribution, an element of value is added, which is represented by the outlay of the manufacturer on wages, rent, interest, etc., together with profits, i.e., all costs other than costs of materials bought from other firms plus profits. VAT is levied on the value added to the product at each stage in the chain of transactions. Hence VAT, in its comprehensive form, may be simply defined as a tax to be paid by all sellers of goods and services, other than those specifically exempted, on the basis of value added by their respective firms. By contrast, a cascading type turnover tax, which may also be comprehensive, falls on the total value at each stage.

WHAT VAT MEANS

17.5 Since the value added at each stage is subject to VAT, in the end the total value of the product as it reaches the consumer is covered by it. A retail sales tax also covers the total value of products; but the difference between the two is that while the retail tax is collected at one stage, VAT is collected in instalments at successive stages of production and distribution.

17.6 The total receipts of a firm from the sale of its output during a given period are equal to, and are collected among, the cost of inputs, wages, interest, rent, depreciation and profits. Therefore, if the cost of inputs is subtracted from total receipts, the remainder will be equal to the sum of factor incomes paid plus depreciation. The base of the value added tax can be alternatively looked at as (a) the value of output minus the value of inputs (O-I), or (b) the sum of factor incomes generated in a firm, i.e., the sum of labour income, property income and depreciation (W + P + D). In the first case, we subtract the value of inputs from the value of output and in the second case we add different types of incomes generated. Correspondingly, one could think of the subtraction method and the additive method of levying the VAT. The use of the additive method has not been seriously contemplated anywhere.

METHODS OF COMPUTATION OF VAT

17.7 Taking the subtraction method, since value added is equal to (O-I), the VAT at a given rate, say 't', can be computed either as t. (O-I), or t.O-t. I. The first is called the 'sales less purchases' or 'accounts' method, and the second is called the 'tax credit' or 'invoice' method. The second method, which is used by all the European countries as well as a few developing countries like Brazil, requires each tax-payer to invoice VAT separately on every sale. The tax due to the Government from a particular business concern is equal to the VAT arising from its total sales less a credit for the tax invoiced to it on its purchases.

17.8 Under this system, every VAT payer will be able to charge full tax on his sales from his customers, even though he pays to the Government only the difference between that and the tax on his inputs. (The latter would have already accrued to the Government in instalments). Since the value of a product increases as it goes through successive stages of processing or production, the tax passed on to the successive buyers keeps increasing. The final buyer, e.g., the consumer, cannot pass the tax; nor can he claim tax credit, since he is not a taxable person under VAT. The intention is that the full tax on the product, though collected in instalments from producers at different stages, should be borne by the final buyer. (In practice, full shifting may not be possible in all cases, at least in the short run.)

17.9 It may be noted that the VAT required to be shown on any given invoice is not the seller's VAT liability with respect to that sale but which he can collect from the buyer. In fact, the VAT liability is determined only at the end of the taxable period when he takes into account all of his purchases from other tax-payers.

17.10 The working of VAT may be illustrated by the following example based on the various stages invloved in the production and sale of, say 1000, containers produced out of one tonne of steel.

(Figures in rupees)

	Purchase price of input including VAT	Sale price	10 per cent VAT		
			Gross tax	Credit for tax paid on purchase	Net tax payable
(1)	(2)	(3)	(4)	(5)	(6)
Steel Plant	800*	1000	100	-	100
Steel container manufacturer	1100	1400	140	100	40
Wholesaler	1540	2000	200	140	60
Retailer	2200	2500	250	200	50
				Total	250

*no tax is assumed to be paid on inputs at this stage

(In this example, no account has been taken of the VAT on purchase of other supplies and services).

It can to seen that a 10 per cent tax is assessed at each stage of the process on the amount of sale, excluding the VAT, but that credit is taken for tax paid on purchases, leaving a net amount of tax chargeable on the value added at each stage. The cumulative tax of Rs. 250/- collected at 4 points is equal to the tax at a rate of 10 per cent on the final retail sale value of the products to the consumer.

17.11 It is obvious that if a single rate of tax is applied, the computation of the tax amount under the subtraction method or the invoice/tax credit method will result in the same tax liability. However, if more than one rate is introduced, the tax liability under the two methods may become different for a given tax-payer. This and other implications for using the two alternative methods are indicated more fully later.

17.12 It must be pointed out that the term 'value added' refers rather to the method of levy or collection than to the conceptual base of the tax. The aggregate base of the VAT is not what the economists understand by the term 'value added' and the objective is not to reach the total value added in the national accounting sense. For one thing, value added in the Government sector (which is taken to equal wages

and salaries paid to Government servants) is excluded from the base. Second, exports out of the country are completely freed of VAT, while imports are subjected to it, in order not to discriminate between imports and domestically produced goods. Additionally, the cost of some forms of investment, e.g., that of capital goods, is also often excluded from the base. Thus, any impression that VAT covers the total value added in the economy is not correct.

VARIANTS OF VAT

17.13 It has been indicated earlier that the base of VAT can be arrived at by subtracting the cost of inputs from the value of output. Though capital goods are treated as fianl goods in national income accounting, from the point of view of a firm they also represent inputs whose cost has to be recovered in due course. For the purpose of VAT, one has to decide on the treatment of the cost of capital goods or of investment by the firm during the concerned accounting period. One possibility is to exclude the cost of investment from the tax base. In this case, the purchase of capital goods is relieved of taxes and the entire burden of the tax falls on consumer, they alone not getting any credit for the tax they pay. The investor is freed of tax on the capital goods he buys, and only the use of capital goods over time gets taxed when the consumer goods produced are subjected to VAT. This is called the consumption variant of the tax. Since imports are taxed but exports are not, this variant becomes a tax on domestic consumption in the private sector of the economy. This tax is equivalent to a retail sales tax on consumer goods and services.

17.14 The second variant is called the income variant. Under this, depreciation on capital goods employed, and not the cost of new investments, is to be excluded from the base. Since depreciation is excluded, there is an approximation to the concept of net output not related to exports. Both types of final buyers, the consumers and the investors, bear the tax.

17.15 If neither the cost of capital goods bought during the period nor depreciation is excluded from the taxable base, then it (the base) becomes something akin to gross value of output (W + P + D, in terms of the notations used in paragraph 17.6). Hence this form of VAT is called the gross product variant. Under this, capital goods are first taxed when bought and their use is later taxed through the tax on the goods they produce.

17.16 Under the tax credit method that is generally employed, it is difficult to relieve depreciation of the right amount of tax, because the taxes to be so rebated over the life of different assets would be those paid in the past. In fact, the income variant of VAT has not been adopted anywhere. The real choice lies between the consumption and the gross product variants. The former involves taxation of capital goods only once and is, therefore, considered to be neutral between labour-intensive and capital-intensive methods of production. The latter, as mentioned earlier, involves the taxation of capital goods when purchased and once again through the taxation of their products whose value includes depreciation. The EEC model is the consumption variant.

17.17 Allowing full offset of VAT on a capital good against the current VAT liability of a firm, under the consumption variant, has the merit of simplicity. It also enables a country to maintain its competitiveness in the export markets despite the taxation of capital goods. However, it would mean that substantial capital purchases could create claims for tax credit in excess of current VAT liability leading to actual refund of tax. Alternatively, the excess tax credit could be carried forward until cancelled by tax liabilities, or the refund could be deferred for a set period. Instant refund would, of course, give maximum stimulus to capital creation.

17.18 MAIN CHARACTERISTICS OF VAT

From what has been stated above, the main characteristics of VAT may be easily deduced. First, it is a multi-stage tax rather than a single stage one like the retail sales tax, and, in its ideal form, is to be levied on all stages of production and distribution. Second, it is, in principle, comprehensive unlike selective excises. Third, it is collected in bits at each stage of production and distribution which, when added, equal a tax on the retail sale of the final product at the same rate as the VAT. A 10 per cent retail sales tax will have the same yield as a 10 per cent VAT. Thus, VAT is a method of taxing by instalments final spending in the domestic economy. Finally, the VAT falls on each input into final products once and once only. This is in contrast to the gross turnover tax under which the same element of value added is taxed repeatedly as goods pass along the production chain.

17.19 It is sometimes suggested that the most notable feature of the VAT is its neutrality. It is true that one of the basic attractions of VAT is that it tends to be neutral as between different types of business organisations, methods of production, industries and occupations. The more comprehensive the VAT is made the more neutral it would tend to be. However, neutrality is not an inherent and necessary attribute of VAT. For example, it could be made non-neutral as between different final products by the introduction of multiple rates. Many countries which are operating VAT have more than one rate. By the same token, it could be made progressive or regressive with respect to consumer expenditure. Again, by excluding some products or some stages of distribution, it could be used as an instrument of discrimination. Thus, in a developing country where capital is scarce but labour is surplus, a mild bias against capital-intensive methods could be built into the system. The essential feature of VAT is not neutrality but rather the fact that it avoids cumulative taxation of inputs.

17.20 MAIN ADVANTAGES AND DISADVANTAGES OF VAT

The chief merits of VAT may be briefly recapitulated. As has been indicated earlier, the VAT ensures that an input is taxed only once and hence not only is cascading avoided, but the incidence on any final product can be controlled. Thus, the VAT combines the advantages of being a general tax, without the disadvantages of extended input taxation. It is also free of other economic demerits of cascade type turnover or sales taxes. Thus, it does not promote vertical integration so long as there are no exemptions to important sectors in the middle of the chain of production.* As the proportion of tax in the final price of any particular product is the same irrespective of the number of stages through which it may have passed, it does not discriminate against products embodying a larger part of value added at the earlier stages of production. It does not change the relative prices of inputs and give wrong signals to producers regarding factor combinations. And, finally, since it does not raise costs through input taxation and since under it exports could be fully relieved of internal indirect taxation, the VAT helps a country to maintain the relative competitiveness of its industries in the world market. It has, therefore, been said that VAT lets businesses "free to select the form of organisation, combination of factors, and methods of production, on grounds of efficiency rather than with a view to minimising the impact of taxation on their costs**. It has already been pointed

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*This means that small enterprises are at no disadvantage as compared with large integrated enterprises in so far as indirect taxation is concerned.

**Michele Guerard : "The Brazilian Value Added Tax" IMF Staff Papers.

out that, if desired, the VAT could be made non-neutral with regard to consumers' choice between final products. It is also possible to favour some producers or industries as against others imposing a nil rate of tax on the former so that, like exporters, they would be entitled to a refund of tax on inputs. Again, in developing countries, a mild bias against the capital-intensive methods could also be built into the system by adopting a suitable variant of VAT. A moderate non-refundable tax on capital goods might not mean any significant escalation in costs or loss in competitive advantage so long as the essential feature of VAT, namely, avoiding cumulative taxation, is not impaired. Also, it is desired to promote economy in the use of any scarce inputs, they could be subjected to an additional non-refundable duty so that the prices would be raised to the desired extent. However, the simplicity of the VAT system would be lost if too many rates are introduced and it would be extremely difficult to administer a VAT if there are more than a limited number of rate categories.

17.21 In explaining the merits of VAT, we have been implicitly comparing it with cascade type sales taxes. A tax has necessarily to be judged against the performance of other possible forms of taxation. If the VAT is compared with a retail sales tax, it could be argued that the latter is superior in the sense that it is much simpler to understand and operate and further that it would involve a smaller number of tax-payers in any given country. (Another criticism made against the VAT in this connection is that it ties up the working capital of manufacturer of goods destined for exports, whereas no previous payment and later refund arise under a single stage retail sales tax.

17.22 If a country could succeed in raising the major part of the needed revenues through income taxation and selective excises it could be argued with some justification that such a country would be better off if it adopted as a supplementary measure, retail sales taxation rather than the VAT. On the other hand, the view has been expressed that the shifting of some burden from corporate profit taxation (if it is fairly high) to the VAT might be conducive to a better performance on the exports side and to a larger retention of profits.

17.23 It should also be pointed out that VAT is more easily adopted in a country with unitary form of government than in a federation — particularly if powers of indirect taxation are shared under the Constitution between the two levels of government. If a comprehensive form of Value Added taxation, reaching down to the retail level is to be adopted, it is obvious that the federal government will have to pre-empt the whole field of indirect taxation. We refer to this problem in the Indian context in the following Chapter.

17.24 It is also frequently contended that the introduction of VAT leads to a rise in the price level at the initial stages, as the tax-payers pass on the revised tax liability under VAT on invoices without adjusting the base sales price taking into account the relief of input taxation provided under VAT.

ADMINISTRATIVE ASPECTS OF VAT

17.25 It has been argued that, from the administrative point of view, the VAT has the advantage under the tax credit method that evasion is more difficult because the system provides a ready method for cross-checking the records of taxable persons in so far as invoices play an important role in the operation of the tax. The amounts shown on invoices are important for the calculation of the tax liability of both the seller and the buyer and they are regarded as identifiable items by both of them. Also, it is in the interest of a taxable person to insist on his suppliers collecting the tax and furnishing an invoice, as otherwise he would not be able to claim tax credit. It is also maintained that evasion of tax under a value

added system is less profitable for any single tax-payer than it is under a single stage system, since under the former each tax-payer has to pay only a fractional amount. And it follows that avasion of tax by anyone tax-payer under the VAT system would generally mean less loss of revenue than under the retail sales tax.

17.26 As against these advantages, must be set several features of the VAT which demand a strong and efficient administrative structure as well as additional efforts on the part of tax-payers. It is clear that more computations and checking are needed under the VAT than under a gross value, sales or excise tax. Correspondingly, more elaborate book-keeping is required of the tax-payers. This might involve considerable additional expenditure which the small tax-payers may not be in a position to incur. In developing countries where a considerable proportion of small traders are likely to be insufficiently educated, it would be too much to expect them to maintain adequate records of purchases of inputs which have to be matched against output. The second major administrative drawback in the introduction of a comprehansive VAT in any country where retail taxation does not exist, is that there would have to be a large increase in the number of tax administrators, because of the need to bring in a multitude of retail outlets. Third, it has been pointed out that even though, theoretically speaking, the VAT system provides for an automatic cross-checking, in practice it will be, and has been, possible for a number of tax-payers in a chain of transactions to collude and evade taxes. Evasion can also be easily practised by those who sell services directly to consumers. Since in their case value added is likely to form a major proportion of the value of services rendered, it would be profitable to indulge in evasion.

17.27 While, in its ideal form, VAT is to be made comprehensive, it has not been found practicable to bring all sectors within the tax net. Several types of financial services, such as, banking and insurance, are normally exempt under the European VAT system. It has also been found expedient to exempt farmers, giving them, however, the freedom to opt into the system if that was advantageous to them. It is also possible to have a system of VAT extending down only to the wholesale stage, either completely exempting retail sellers or subjecting them to a moderate tax on a gross value basis.

17.28 Exclusion of the retail stage from a VAT cuts down considerably the magnitude of administrative and compliance problems. At the same time, such an exemption does not also impair in any significant manner the major virtues of the system, for the reason that the retail stage comes at the end of the chain of productive process. Exemptions of other sectors, however, would normally break the chain of tax credit in respect of inputs and would thus introduce distortions. Unlike the imposition of a nil rate of tax, exemption from VAT would not mean a favour but discrimination against the exempted producers in cases in which the exempt stage is sandwiched between two taxable stages. A number of exemptions in the system, therefore, leads to administrative complications and in the process, the tax loses the claim to superiority on neutrality grounds.

17.29 The disadvantage arising from the exemption of some producers is sought to be mitigated in certain countries by providing for what is called "a global credit offset". This refers to a provision by which those who buy from exempted producers are allowed to claim tax credit at a pre-calculated rate that would enable them to recoup the tax on inputs paid by the exempted producers. The EEC model permits its member States to have recourse to this device in the case of farmers. There are also provisions in certain countries where though a producer is exempt, he can opt for VAT in order to obtain a tax credit in respect of a large amount of capital expenditure incurred by him, or else to

enable him to issue invoices for which taxable clients could claim a tax credit. However, it is generally agreed that, if a VAT is to be adopted with exemptions, these should be severely restricted.

17.30 Experience has shown that the introduction of several rates complicates the administration of VAT considerably. The complication arises from the fact that the tax-payer is forced to maintain separate records in order to match inputs and parts of outputs that may be taxed at different rates. The difficulties are said to be particularly felt by multi-product firms. The easiest form of VAT to administer would be one with a single rate. For various socio-economic reasons, however, governments which have adopted VAT have found it necessary to introduce more than one rate, but the number of rates have to be strictly limited. Under these circumstances, a desirable degree of differentiation and progression is sought to be achieved in two additional ways. One method is to impose, on a selected number of final products, an additional differential excise duty which would not come under the system of tax credit. For example, such an additional tax is imposed, in West Germany, in the form of consumption tax. The second method is to reduce the base of the tax in respect of certain commodites so that the effective rate of duty would be lowered. Such a procedure is adopted in Sweden in respect of the construction industry. In a developing country, where large inequalities of income exist, which could not be corrected by means of direct taxation alone, a set of differential excise duties might be called for in case some form of value added taxation is adopted.

IMPLICATIONS OF THE "SALES LESS PURCHASES" AND "TAX CREDIT" METHODS

17.31 As indicated earlier, the aim of the two alternative methods of computing VAT under the subtraction method is to exclude from the tax base at each stage the cost of inputs already subject to tax so that any one input would be subject to tax only once. In the simplest case where there is a uniform rate of VAT on all commodities with no exemptions and there is no other indirect tax, the two methods would result in identical tax liabilities for any given producer, as the numerical example in Table 1 below shows.

TABLE - 1

Value added tax at a uniform rate of 10 per cent — 3 stages of production

(i) Sales less purchases method

	Stage 1	Stage 2	Stage 3
		(Figures in rupees)	
Gross value	100	200	259
Cost	0	110	209
Value added	100	90	50
Tax at 10%	10	9	5
Price	110	209	264

Total tax 24 ; Final price = 240+24 = 264

Tax on final product = $\frac{24}{240}$ x 100 = 10%

(ii) Tax credit method

	Stage 1	State 2	Stage 3
		(Figures in rupees)	
Gross value	100	190	240
Cost	0	100	190
Tax at 10%	10	19	24
Tax credit	0	10	19
Tax due	10	9	5
Price	110	209	264

Total tax = 24; Final price 240 + 24 = 264

$$\text{Tax on final product} = \frac{24}{240} \times 100 = 10\%$$

(Note:- In the tax credit method the gross value represents the tax-base.)

If there is more than one rate of VAT so that the rate of VAT varies between stages, the two methods would give results as shown in Table 2 below :

TABLE — 2

Value added at 3 different rates — 10 per cent, 15 per cent and 20 per cent at successive stages of production

(i) Sales less purchases method

	Stage 1	Stage 2	Stage 3
		(Figures in rupees)	
Gross value	100	200	263.5
Cost	0	110	213.5
Value added	100	90	50.0
Tax	10(10%)	13.5(15%)	10.0 (20%)
Price	110	213.5	273.5

Total tax — 33.5; Final price = 240 + 33.5 = 273.5

$$\text{Tax rate on final product} = \frac{33.5}{240.0} \times 100 = 13.9\%$$

(ii) Tax credit method

	Stage 1	Stage 2	Stage 3
		(Figures in rupees)	
Gross value	100	190	240
Cost	0	100	190
Tax	10 (10%)	28.5(15%)	48 (20%)
Tax credit	0	10.0	28.5
Tax due	10	18.5	19.5
Price	110	218.5	288

Total tax = 48; Final price = 240 + 48 = 288

$$\text{Tax rate on final product} = \frac{48}{240} = 20\%$$

(Note:- In the tax credit method the gross value represents the tax- base.)

Thus the tax credit method will yield an average rate which is the same as the tax rate at the final stage, i.e., 20 per cent; whereas the sales-less-purchases method will yield a rate which is a weighted average of the different rates applied, the weights being the proportions of value added at the three stages. Thus, the average rate on the final product in this case works out to 13.9 per cent as against the rate of 20 per cent at the final stage.

17.32 The tax credit method makes it possible to tax a given final product at any specified rate that may be desired, without disturbing the taxes on other goods or inputs. That is, the nominal and cumulative rate on that product will be the same. On the other hand, under the sales-less-purchases method, if there are more than one rate, the nominal and cumulative rates on the final product will differ.

17.33 From various points of view, the tax credit method is easier to apply. While the sales-less-purchases method would require that taxes at all stages be ad valorem, the tax credit method can be enforced even with specific duties at some stages. Again, under the former, there could be evasion throguh exaggeration of costs; under the latter the need to submit vouchers of tax paid acts as a check on artificial increases in claimed deductions.

17.34 Under the tax credit method, if there are some exempted products occurring in the chain of production, there will be a "catching up" in the subsequent stages of production, because credit is granted only if tax has been paid on an input. Per contra, under the sales-less-purchases method, the exempted inputs will escape taxation till the end. Because of this reason, under the manufacturers' sales tax in the Phillippines embodying the value added principle, deductions were restricted to the cost of previously taxed items. If there are other indirect taxes in the country besides the VAT, the sales-less-purchases method would imply granting total or partial credit to these other taxes paid on

inputs, whether intended or not. This would create problems if, for instance, import duties are levied on certain inputs for protective reasons. Also the effect of any special excises levied deliberately to raise the price of scarce inputs would be nullified by the sales-less-purchases method.

17.35 So far we have discussed theory and the general features of the VAT. We shall now present briefly certain basic features of the tax as it operates in some of the industrialised and developing countires.

THE EVOLUTION AND SPREAD OF VAT

17.36 France is generally credited to be the first to incorporate the principles of VAT in its taxation system. It introduced the system of fractional payment in relation to the tax at the manufacturing stage, as early as in 1948.* (Some even trace back its evolution to start from 1917 when France introduced 'la taxe sur le chiffre d'affairs.) The VAT was extended to the wholesale level in 1954. Subsequently, the Council of EEC adopt d VAT as the common form of sales tax to be used by its member-states.** The rapid adoption of VAT by a number of European countries started only from 1967, after the issue of the two directives by the Council of EEC which required its member-States to replace their present system of turnover taxes by a common system on value added basis as rapidly as possible and not later than Ist January, 1970. (This date was extended by subsequent directives.) The following Preamble to the first directive of the Council, dated the 11th April, 1967, explains the object behind the adoption of VAT :

> "Considering that the primary objective of the Treaty is to establish, within the framework of an economic union, a common market providing for healthy competition and having characteristics similar to those of an internal market ;
>
> Considering that the attainment of this objective presupposes the prior application, in the Member-States, of laws relating to turnover taxes which neither distort conditions of competition nor impede the free circulation of goods and services within the Common Market ;
>
> Considering that the laws now in force do not meet the above-mentioned requirements; and that it is, therefore, in the interest of Common Market to harmonize the laws relating to turnover taxes with a view to the elimination, insofar as possible, of those factors which are capable of distorting conditions of competition both in the national and community levels, and to permitting the subsequent attainment of the objective of abolishing the levying of taxes at importation and the refunding of taxes at exportation with respect to trade between the Member-States;
>
> Considering that it is apparent from studies carried out that such harmonization must result in the abolition of the systems of cumulative cascade taxes and in the adoption by all Member-States of a common system of tax on value added ;

* This was the occasion for coining the term 'taxe sur la Valeur Adjoutee (TVA)' by Monsieur Laure

** This decision was based on the recommendations contained in the Report of the Fiscal and Financial Committee of EEC, generally known as "The Neumark Report".

Considering that a system of tax on value added will achieve the highest degree of simplicity and neutrality when the tax is levied in as general a manner as possible and when its scope of application includes all stages of production and distribution as well as the realm of the rendition of services; and that it is, accordingly, in the interest of the Common Market and of the Member-States to adopt a common system the scope of which also extends to retail trade."

17.37 The growth in world trade and international competition also induced serveral countries to examine the effect of their system of taxation on the relative competitive position of their industries and a number of countries adopted VAT after 1967. There are at present about dozen countries in Europe (9 members of EEC — Belgium, Denmark, France, Federal Republic of Germany, Ireland, Italy, Luxembourg, Netherlands and the United Kingdom; and Austria, Norway and Sweden), a few in Latin America (Argentina, Brazil, Chile, Colombia, Equador, Peru and Uruguay), as well as some in Africa (like Ivory Coast, Madagascar, Morocco and Senegal) having some form of VAT.

17.38 A questionnaire (copy given in Apendix 19) was sent by the Committee to a number of Indian Embassies abroad. From among them, comprehensive replies were received for ten countries, namely, Denamark, West Germany, Netherlands, Luxembourg, Ireland, Belgium, Italy, Austria, Chile and Argentina. Some information was also received on the tax systems in Algeria and Brazil . The various replies received have been summarised question-wise (except for Brazil and Algeria) and are given in Appendix 19. The basic features of VAT system as operating in Brazil have been separately included. In the following paragraphs, we highlight some of the more important points arising out of this study which, in our view, need special attention in applying VAT to Indian conditions.

BASIC REASONS FOR ADOPTION OF VAT

17.39 The gradual evolution of what later came to be known as TVA in France tended to give that country a certain advantage over the other members of the EEC because it was possible for that country to free its exports from internal commodity taxation than other European countries with cascade type taxes. This added an impetus to desire for the latter to switch-over to VAT. In any case, with the formation of the EEC it was necessary to bring about fiscal harmonisation through the adoption of a common form of indirect taxation. The EEC countries chose VAT for several reasons, the more important being :

(i) to eliminate the cascading effect of the turnover taxes which were in operation in most countries ;

(ii) to mitigate distortions like vertical integration caused by the earlier indirect taxes by having a neutral tax system; and

(iii) to introduce progression.

Admission to the EEC weighed in deciding on a change-over to VAT in some countries. Chile adopted it for removal of distortions of earlier purchase/sales taxes as also to minimise evasion. In Argentina, it was both a rationalisation measure and an attempt to harmonise central and jurisdictional tributary systems. Austria went on the basis of international trends and other advantages of the VAT system,

while Brazil adopted it as a measure of tax reform at the Federal and State levels as also to minimise the distortions caused by the earlier turnover and "consignment" taxes levied by the States. The automatic yield of considerable revenue without the necessity of frequent changes in tax rates, because of the comprehensive scope of VAT, also appears to have influenced some of the countries to go in for VAT.

17.40 In most countries VAT replaced purchase or sales taxes or turnover taxes which were levied at one or multiple rates either on goods alone, or both on goods and selected services. In U.K., besides purchase tax, VAT also replaced the selective employment tax. In Brazil, VAT at the State level (ICM) replaced the erstwhile State turnover and "consignment" taxes, as well as industries, professions and municipal taxes. Though there has been considerable discussion in public finance literature about VAT being used as a partial or complete substitute for corporate income tax, no country has attempted it in practice so far.

TAX SYSTEM REPLACED BY VAT

17.41 All the 9 EEC countries, Austria, Norway and Sweden in Europe, Argentina, Chile, Brazil (State VAT), Equador and Uruguay in Latin America, have VAT extending upto the retail level. Ivory Coast, Madagascar, Morocco and Senegal, formerly associated with France, have VAT similar to the earlier French version, up to the wholesale level. Mexico in Latin America and Algeria in Africa have also VAT which extends only up to the manufacturing stage. Though the Phillippines does not have VAT as normally understood, its 'sales tax' levied on producers and manufacturers does contain certain features akin to VAT, as various deductions are allowed to mitigate the cumulation of taxes. The federal tax in Brazil on industrialised products (IPI) has also the features of a VAT.

STAGE UPTO WHICH VAT INTRODUCED

17.42 Most countries cover both goods and services under VAT. Imports also are subject to this tax. In the case of goods there are very few exemptions. In EEC countries especially, the Council directives enjoin on Member-States to restrict the area of exemptions as far as possible. The taxation of services is generally not universal. Though in most European countries all services are chargeable, exemption is provided for a large number of cases. In developing countries, wherever services are charged under VAT, the taxation is usually on a selective basis.

SCOPE OF VAT

17.43 Normally under VAT, an exempted producer/supplier of services having tax liability will not be able to claim credit for the input taxes he has paid. If it is desired to fully free certain products/services, or products/services used for certain purposes, such as exports, from VAT, refund of input taxes paid in such cases would have to be specially provided for in the legislation. Such provisions sometimes take the form of zero-rating the concerned products/services. If input taxes are refunded, it could be said that the product/service is zero-rated or fully exempted; on the other hand, if only the product/service is exempted but there is no refund of input taxes, it can be called a case of partial exemption. Where, for social and economic reasons, relief is considered desirable, partial exemption is provided. Complete exemption with full repayment of credit of input taxes is also extended but this treatment is generally reserved for goods meant for exports or services related to exports. In some countries it is given in respect of some other transactions as well. In U.K. for example, food, drugs and medicines, certain categories of publications, news services and construction of buildings are zero-rated and the tax-payer can claim refund of VAT paid on inputs. Financial institutions and insurance companies are granted partial exemptions in almost all European

countries. Thus, though these activities are exempt, no credit is allowed for the taxes paid on inputs. Medical and allied services and certain cultural and social services (e.g., public educational institutions, theatres, social insurance institutions and welfare organisations) are also generally exempt without credit for input taxes. Construction is usually treated as a service activity and taxed as such — unless otherwise exempt.

17.44 In developing countries, the scope of the tax is relatively less comprehensive. Thus, in Brazil, direct sales of agricultural products by the farmers and a limited number of food-stuffs, electricity, hydro-carbon oils, unprocessed minerals, industrial machinery and equipments are exempt. In Algeria, Brazil and Equador, services are not covered by VAT but are subjected to separate taxes — though on a selected basis. Thus, in Brazil municipalities charge industrial and commercial services, such as rental of movable property and space in warehouses and hotels, to service tax up to 5 per cent. The treatment of public utilities varies, but they are generally left outside the scope of the tax or granted specific exemptions in developing countries.

17.45 All the countries which are having VAT have very few rate categories ranging generally between two and a maximum of four. To start with, West Germany, Netherlands, Luxembourg, Chile and Argentina had two rates: Ireland, France and Belgium had 4, while Denmark, U.K. and Sweden had only one rate. The standard rate varied between 8 per cent and 20 per cent. The changes effected after the introduction of VAT show that there has been a tendency to keep only very few rates, though someof them which started with one rate, like Sweden and U.K., have increased the number, whilst others having four rates have later reduced them.

RATE STRUCTURE

17.46 The rate structure reflects broadly the relative tax incidence on different commodities before the change to VAT system. All European countries, except Swedan, use tax exclusive basis for calculating tax on value added. Brazil uses a tax inclusive basis and so also most of the African countries that follow the French type of VAT. In France itself the base included tax till January, 1970.

17.47 Table 3 below outlines the rate structure in some of the European countries as well as developing countries, both at the time of introduction and as at present.

TABLE 3

RATES OF VAT IN SOME EUROPEAN AND LATIN AMERICAN COUNTRIES

Country	Date of adoption	Lowest		Intermediary		Standard		Highest		Remarks
		On the date of adoption	Present	On the date of adoption	Present	On the date of adoption	Present	On the date of adoption	Present	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
West Germany	1.1.68	5	5.5	-	-	10	11	-	-	

Country	Date of adoption	Lowest		Intermediary		Standard		Highest		Remarks
		On the date of adoption	Present	On the date of adoption	Present	On the date of adoption	Present	On the date of adoption	Present	
Netherlands	1.1.69	4	4	-	-	12	18	-	-	
Belgium	1.1.71	6	6	15	14	20	18	25	25	
Luxembourg	1.1.70	4*	10	-	-	8	15	-	-	
Ireland	1.11.72	5.26	5.26	-	-	16.37	16.37	30.26	30.26	
Denmark	3.7.67	-	-	-	-	10	15	-	-	
U.K.	4.1.73	-	-	-	-	10	8	-	12.50	
Italy	1.1.73	3	6	6	9	12	12	18	35**	
Austria	1.1.73	8	8	-	-	10	18	-	-	
Sweden	1.1.69	-	3	-	9	11.11	17.65	-	-	
Chile	N.A.	8	8	-	-	20	20	-	-	
Argentina	1.1.75	-	-	-	-	13	16	21	-	
Brazil (State VAT)	N.A.	-	-	-	-	-	14-15@			

*For certain food items 2 per cent rate is applied.

**As per Report of the FICCI Study Team. As per information received from Indian Embassy, VAT rates now vary between 6 per cent and 25 per cent.

@ 14 per cent rate applies to States located in South-east and South regions where most developed areas are located and 15 per cent to other areas. In the case of export operations except industrialised goods, the rate is 13 per cent. On inter-State transaction VAT rate is 11 per cent.

Source:- (i) Information collected by the Committee's Secretariat from Indian Embassies and that collected by Member-Secretary during his visit to U.K./Brussels.

(ii) Information collected by the Federation of Indian Chambers of Commerce and Industry (FICCI) Study Team.

17.48 Almost all countries levy some additional duties on a selected range of products, apart from the value added tax, generally called excise duties or consumption taxes. The items covered by these special additional taxes usually are spirits, alcoholic drinks, tobacco, patroleum products, sugar, aerated waters, matches, radios/TVs, perfumes, motor vehicles (generally cars) and tyres. In West Germany, even tea, coffee, salt, electric bulbs and playing cards are charged to special consumption taxes. These additional duties, it may be observed, are not eligible for deduction under VAT wherever the commodities are used further as an input by a tax-payer. The rates and scope of these duties vary considerably between different countries. In the case of EEC countries, there has, however, been a move to harmonise the scope, basis of assessment and mode of levying excise duties, in particular those which have an appreciable influence on trade. A number of Council directives have also been issued in this regard.

LEVY OF ADDITIONAL TAXES ON COMMODITIES APART FROM VAT

17.49 In most countries, the tax credit or invoice method is used for collecting the VAT and the total tax borne on purchases in any specified period is allowed to be adjusted against the total tax charged on sales in that period and the net tax is only payable to the treasury. The periodicity of tax adjustments and submission of assessment returns is not uniform, Thus, in Chile and Italy, they are monthly for all tax-payers; inWest Germany, Luxembourg and Belgium, it is monthly for comparatively bigger licensees while for others it is on quarterly basis. (In Belgium, however, even though the returns can be sumitted quarterly, the tax payments are to be made monthly.) In Denmark and Netherlands, the payments and submission of returns are on a quarterly basis. Only in Ireland this is done bi-monthly.

MANNER OF ASSESSMENT AND COLLECTION

17.50 In all countries, to claim credit of the taxes on inputs, the tax-payer must have received a proper tax invoice even though he is not obliged to have actually paid to his suppliers. It is not insisted that there should be a precise corelation between goods received and goods delivered and, therefore, it is not necessary that the tax chargeable for a taxable period should represent the value added in that period. For some periods, the tax credits on purchases may exceed the tax chargeable on sales. In most European countries an immediate repayment of any excess tax is made except where the amount is small and it is considered administratively more convenient to carry it forward for set-off against the tax for the next accounting period. Some developing countries have, however, .sions (similar to the 'Buffer Rule' of the earlier French VAT), whereby if the input tax for an accountable period exceeds the tax chargeable on sales, the excess is not repaid but is allowed to be carried forward for set-off against future tax liability. Some of the developing countries have put further limitations like the prior stage tax on inputs being restricted to the tax due on the final products.

17.51 Where an assessee has certain tax free (exempt) sales, not exports, as well as taxable sales, the share of input taxes which goes into the tax free sales is not allowed as a credit. This necessitates an apportionment of the amount of input tax for tax credit purposes. The deduction of VAT on purchases in such cases is generally made on a proportional basis. Thus, input taxes are generally creditable in the ratio which the amount of taxable supplies bears to the amount of exempt supplies.

17.52 Under the EEC model, certain goods and services which may be used for private purposes by the tax-payer or his employees, such as food, drink, accommodation, entertainment expenses, etc., are usually not allowable as a deduction.

17.53 Most European countries allow a full credit of the tax paid on investment goods in the period in which they were acquired, though certain adjustments were made for the purchases of capital goods during the transitional period. For example, the Federal Republic of Germany allowed immediate credit for VAT but charged a separate investment tax at rates decreasing gradually from 8 per cent in 1968 to 2 per cent in 1972. Belgium, France and Netherlands restricted the deductions of tax on investment goods in the initial periods of the new tax. Developing countries have, however, not followed this practice of allowing an immediate credit for investment goods. Equador, for example, does not allow credit for investment goods; Uruguay on the other hand, allows credit of tax paid on fixed assets but buildings are exempt from the charge and no tax credit is given for the tax paid on the materials used in construction. In Brazil, industrial machinery is fully exempted. In African countries, tax credit is usually allowed for buildings, plants and machinery but not for transport equipment and certain buildings and office furniture. Algeria allows deductions of taxes paid on specified investment goods.

TREATMENT OF INVESTMENT GOODS

17.54 There is no uniform practice in the matter of prescribing by law the format of invoices or specified records to be maintained by the assessee. Generally, the particulars to be given on an invoice to make it an acceptable document for allowing tax credits is specified. The particulars to be shown are those normally given in commercial practice, like name and address of the supplier and of the recepient of the goods or services, the date of issue, the date of delivery, full description of goods and services to which the invoice relates, the amount charged and factors, such as discounts or packing costs affecting that amount, and the rate and the amount of VAT. It must also give the registration number of the person issuing it. Invoices are not normally issued at the retail stage to fianl consumers but when requested they are issued by the retailer to a registered person.

17.55 It is also usually insisted that a VAT licensee must maintain a detailed record of his purchases and sales so that it can be easily ascertained from the records as to what the total tax paid is in a period on the purchases made and how much tax has been billed on the sales effected by the licensee. The intention is to maintain records in a manner that any third person should be able to get an idea of the business transactions, within a reasonable time — specially of the tax due and the deductible tax amount. The entrepreneur has to maintain his records complete and in proper order with all relevant vouchers — both copies of the outgoing bills and incoming bills — and keep these records for a number of years. (For example, in West Germany, records are preserved for 10 years and invoices for6 years.)

17.56 Returns which are submitted by the VAT assessees are generally in simple forms which contain the details of the sales and the amount charged by the tax-payer in the accounting period as well as purchases made and amount creditable as input taxes. If the firm is manufacturing (or supplying) a number of commodities which are subject to different rates, the break-up for each rate is required to be shown. Where there are some tax free sales also, its particulars have to be given separately and the credit on inputs apportioned appropriately. On the whole, the book-keeping requirements are simpler where VAT is charged at a single rate and where there are few exemptions. For small enterprises there are generally special provisions to which we briefly refer below.

TREATMENT TO SMALL SCALE SECTOR

17.57 The inability of many small producers/traders to cope up with the accounting procedures as well as the limitations of the tax officials to control effectively a very large number of VAT licensees — particularly where the tax extends up to the retail stage, have prompted special provisions

being made in regard to small enterprises. Even the Council of EEC conceded the need for simplified procedures for smaller establishments and left it to member states to devise appropriate provisions as may be more suitable in its national circumstances — the fundamental objective being to keep smaller manufacturers under surveillance so that if they expand beyond the limits for small enterprises, they may be brought fully under the VAT system.

17.58 The relief to smaller manufacturers is granted by —

(i) giving them complete exemption (especially for very small assessees);

(ii) requiring payments under a simplified procedure rather than the normal procedure under VAT;

(iii) allowing assessments at reduced rates ; and

(iv) relaxing the frequency of submission of tax returns.

17.59 The small scale sector is not necessarily exempt from VAT liability but in a number of countries if the turnover (in certain cases duty liability) does not exceed specified limits, the assessee is exempt from further tax and he has to bear only the tax borne on his purchases. Table 4 below gives an indication of the exemption limits under various European VAT systems. The criterion is usually sales, except in France, Luxembourg and Netherlands, where it is based on the amount of tax payable.

TABLE 4

EXEMPTION LIMITS UNDER EUROPEAN VAT SYSTEMS

S.No.	Name of the country	Exemption limit
1	Denmark	Annual sales of less than DKr 5000
2.	France	Annual liability not exceeding F 1350
3.	Germany, Federal Republic of	Annual taxable sales of less than DM 12000
4.	Ireland	Sales of £ 1800 a year for those engaged in providing services. Higher figures for those engaged in trading, depending on the category of business (£ 6000 and £12000 a year)
5.	Luxembourg	Annual liability of F 5000 provided that turnover is less than F 500,000

S, No.	Name of the country	Exemption limit
6.	Netherlands	Annual net tax liability not exceeding F 1300
7.	Norway	Annual taxable turnover less than NKr 6000
8.	Sweden	Annual taxable turnover less than SKr 10000
9.	United Kingdom	Annual turnover of not more than £ 5000

Source : Sales taxation Administration: Major Structural and practical issues with special reference to the needs of developing countries, United Nations, New York, 1976.

17.60 In case the turnover (or duty liability in some cases) exceeds the exemption limit, there are simplified procedures for payment of duty. Specific mention needs to be made here of the forfait system available to traders in France and Belgium and certain other countries. Brazil uses it extensively, though in a modified form. Even West Germany has a somewhat similar provision. Certain salient features of the forfait system which orginated in France are included in Appendix 19. Under this system, the small tax-payer does not have to keep full and detailed records of his business transactions as normally required under the VAT. The tax is paid not with reference to actual sales by the tax-payer in taxable period, but in a fixed sum for each period. The duty liability is fixed on a periodic basis taking into account the past performance and sometimes certain other relevant factors to have a reasonably accurate estimate of sales.

17.61 In West Germany, medium-sized units which are not exempt (because their outturn exceeds 12000 DM but does not exceed 60000 DM) are taxed at the lower rate at 4 per cent as compared to the standard rate of 11 per cent applicable to the bigger units. This tax is, however, not admissible for deduction and need not be shown in their invoices. Further, there is a provision under which these units can opt for the VAT and pay the normal rate for which tax credit is allowed. The latter is advantageous for such of the units as are exclusively or mainly effecting their sales to other undertakings using their products as inputs. This provision for option to smaller enterprises to come under VAT is available in other countries also.

17.62 In Argentina, there is a special provision under which very small retailers need not register themselves under VAT. However, for their purchases made from the registered suppliers the tax charged is increased by 40 per cent. Thus, as against the 16 per cent normal VAT charged by a registered licensee to another registered licensee, he charges 6.4 per cent additional tax when his sales are made to an unregistered buyer who is exempted from the provision of registration because of small turnover.

17.63 In Chile, there is no special provision for smaller entrepreneurs and there is no relaxation even for accounting formalities.

17.64 In France, West Germany, Luxembourg and Netherlands though normally tax declarations have to be submitted monthly together with the tax payments, for small businesses a quarterly basis is accepted. In Belgium, payments on forfait basis must be made monthly but tax declarations are quarterly. In Sweden, the taxable period is normally bi-monthly but for small enterprises four monthly and six monthly bases are acceptable - very small concerns can submit declarations and make payments even on an annual basis.

DATA COMPILATION AND CHECKS

17.65 In West Germany, Denmark, Belgium, U.K., France and Ireland, computers are used on an extensive scale for checking returns submitted by VAT assessees and to detect any discrepancies and point out assessees deviating from averages. The computers are even used for issuing reminders, advance notices and tax declaration forms. Besides the checks by computers, in most countries, there are periodical audits whereby tax declarations, account books and vouchers are examined. Over and above, in certain cases special VAT auditing is conducted by experts experienced in turnover taxation. If there are indications of fall in taxes, tax preventive services are activated.

17.66 In Netherlands, the main way to control the assessees is physical verification by tax accountants. The records of each entrepreneur are carefully scrutnised at regular intervals and no computers are used for checking the returns. In Italy, also there is a physical verification of the records and invoices by revenue officers, on a periodical basis. In Austria, the revenue officers are supposed to have a physical verification at least every three years for the big and small units. Computers are also used at certain centres.

17.67 In Ireland also there are regular audits to examine traders' records depending upon the nature and size of business and the standard of records kept. Figures from VAT returns are checked back to trader's summaries and further to daily records making a random selection of entries for detailed check (including credit notes if issued). Some invoices are cross-checked with customers' or suppliers' accounts, etc.

PUBLIC EDUCATION AND OFFICIAL GUIDANCE BEFORE INTRODUCTION OF VAT

17.68 The introduction of VAT in almost all countries was preceded by detailed public debate in chambers of commerce, industry, associations and other forums, in Parliament and educational institutions, etc. In fact, in some EEC countries though the initial discussion for moving towards a VAT system started as early as 1956 (when the "Treaty of Rome" was signed) it was years later when the actual decision to go in for VAT was taken and the intention made public. Even after this announcement of each Government's intention to switch over to VAT, it took some of the countries (e.g., Belgium, Luxembourg, Ireland, Netherlands, Italy and Austria) more than two years to actually legislate and educate their public, tax-payers and tax collectors about the implications of the new system so that the switch over could be smooth and there were not many serious distortions in the economy. Details of the scheme were brought out in simple booklets, copies of which were supplied widely to affected tax-payers; advertising campaigns through press, courses on radio and TV and public meetings throughout the country where revenue officials explained the provisions of the new tax, were organised; a special telephone service was provided at tax offices (e.g., 'Green Telephone' in Belgium) by which people could ring up for any clarification about VAT. Special training courses for revenue officers were organised. These were some of the steps taken up by the various governments to educate public/tax-payers and revenue officers. Besides this, symposia and discussions were also organised by important chembers of commerce, trade and industry organisations on their own or in conjunction with revenue officials.

17.69 PROBLEMS FACED AFTER INTRODUCTION OF VAT

Due to the detailed training imparted to revenue officials and the education of assessees by Government and trade chambers etc., the introduction of VAT in the countries under study did neither create many problems nor did it cause much distortions. Though it appears to have affected the prices in some of the countries, the increase was not much — generally 1 to 2 per centage points appear to be the increase attributed to the new system. The fact that many of these countries were already having turnover taxes/sales taxes down to retail level also greatly helped in its easy introduction. In the matter of calculation of prices and value to which VAT was to be applicable, there appears to have been some problems. Thus, in West Germany, it appears that their entrepreneurs did not reduce their ex-factory prices at the time of switch-over. It was made clear to them that VAT cannot be charged on the old prices, but at first, old gross turnover tax was to be calculated out of these prices and to this net price VAT had to be added. In Austria, the verification of taxes paid on inputs appears to have created some problems initially but they were sorted out later.

17.70 The Chairman and Member-Secretary of the Committee visited the U.K. and Brussels and had discussions with senior officials as well as representatives of trade and industry on the operation of VAT in the U.K. and other EEC countries. A summary of the report given in Appendix 20. It was learnt that the switch-over to VAT in the U.K. had created several problems which were further complicated by numerous exemptions and zero-rating. It also appears that the small traders had resented the tax because it involved considerable time and effort to maintain the required accounts and file the returns correctly in time. As no general sales tax had existed in U.K. prior to the introduction of VAT, the vast increase in the number of assessees brought about by the switch-over had also created problems regarding visits of officers. However, the general impression given was that the tax system was broadly settling down and that computers had considerably helped in the process of collection.

17.71 Discussions in Brussels revealed that the problem of small traders was generally a difficult one to solve. They have been finding it difficult to maintain the kind of accounts necessary for the workings of VAT. The administrative problem of dealing with a large number of small traders was also considerable. About the degree of tax evasion/avoidance in respect of VAT alone, it was indicated that taking into account all the taxes of the country, it may be about 5 per cent.

CHAPTER 18

LONG TERM REFORM OF THE INDIRECT TAX STRUCTURE

18.1 In the course of our analysis of the weaknesses of the prevailing system of indirect taxation in the country (vide Chapter 5), we had indicated that given the magnitude of the problems and the interaction of taxes levied by different authorities, it would not be enough to consider limited reforms within each individual tax system, but it would be necessary to think of more far-reaching changes to bring about a harmonious functioning of the various elements in this system. In Chapter 8, we have outlined the main principles that should guide the reform of the systems of excises and import duties, and in Chapter 13, we have indicated the lines of reform of the sales tax system of the State Governments, on the assumption that the sales tax would continue as a separate tax to be levied and collected by the State Governments themselves.

18.2 The reform of a complex structure of taxes such as the one we have at present would naturally take time and would have to be carried out in stages. The kinds of changes that we have indicated in the earlier Chapters should be thought of both as preliminary steps towards fundamental changes to be brought about in course of time and as measures of reform that would by themselves effect a significant improvement in the existing system. We have also taken care to ensure that the measures that we are recommending for immediate implementation are consistent with the long-term objectives that we have in view.

18.3 We have emphasised more than once that the excise tax system at the Central Government level forms the bulwark of the entire structure of indirect taxes in the country and that unless it is placed on a sound footing, it would not be possible to bring about a full rationalisation of that structure. Particularly in regard to excises, the immediate steps that we have recommended can be said to go only part of the way towards resolving the basic problems created by an extended system of taxation, covering not only consumer goods but also all kinds of inputs and capital goods. Moreover, in the longer run, we need to think also of a proper dovetailing of import duties with excises so that their combined operation, while leading to a progressive distribution of the burden of taxes among consumers, would not militate against economic efficiency. Finally, we have to consider whether in due course of time we should work towards the creation of one integrated tax system which would replace most of the present indirect taxes on internal transactions including, in particular, excises and sales taxes.

GENERALISED SET OFF AND TAX ON VALUE ADDED

18.4 The lines of evolution of the system of internal indirect taxation in India are by no means unique. Several developed and other developing countries had also started with a simple system of selective excises. Over time, but owing to increasing need for revenue, they gradually extended the system of excises, often adding a general sales tax to their fiscal armoury. In the end, they found themselves with complicated, cascade-type of sales taxes with or without extended excises. As such a system produced several harmful economic effects and seriously militated against the pursuit of rational economic objectives, a thorough reform of the system had to be brought about sooner or later. In examining the lines of reform, it was realised that in order to avoid distortions, promote exports and to make

intervention beneficent, selective and purposeful, it was necessary to think of a different system embodying a principle which would eliminate the above-mentioned problems, even under an extended commodity tax system. This is the principle of generalised set off for taxation of inputs. The main reason why this principle becomes an essential requisite under an extended system of indirect taxation is that, as we have indicated in Chapter 8, a simple reduction in the rates of duties on raw materials and other inputs could only proceed up to a point; beyond that it not only involves huge losses in revenue but also relieves certain types of consumption and products from taxation. The system of tax credit does not suffer from these disadvantages.

18.5 From the economic point of view and for easily achieving a determinate degree of progression, it is best to have a tax system which covers value added at all stages of processing and trade but which, however, does not create problems of cascading and distortions in relative factor prices. These characteristics are found in two types of taxes, namely, a comprehensive retail or last point sales tax on all goods and services and a comprehensive VAT. The retail sales tax, however, suffers from the disadvantage that there is a concentration of the entire burden at one stage - and that too at the last stage. It is considered extremely difficult to administer a retail sales tax which should yield the major part of the indirect tax revenue needed by the Government. It is for this reason that many countries have turned to the VAT. Today, as indicated in the preceding Chapter, almost the whole of Western Europe (including the United Kingdom) as well as a number of developing countries, such as Brazil, Argentina and Ivory Coast have switched over to the VAT system

VAT IN INDIA

18.6 As observed earlier, our terms of reference require us to examine the feasibility of adopting some form of VAT in the field of indirect taxation in India. If the answer is in the affirmative, we have been asked further to indicate the appropriate stage at which the principle of VAT could be applied. When we elicited the views of trade and industry on the subject, we found that although there were several, who expressed doubts and reservations about the administrative feasibility of adopting VAT in India in the near future, there was an impressive measure of support for such a step, one source of support being the Federation of Indian Chambers of Commerce and Industry itself. In accordance with our terms of reference, we shall now address ourselves to an examination of the merits of adopting some form of VAT in India and of the administrative and other implications of making such a change. In the light of our examination, we shall indicate the stage at which the principle could be adopted with advantage in the Indian context.

18.7 A detailed exposition of the VAT system has already been given in the preceding Chapter. Essentially, VAT in its comprehensive form is a tax on all goods and services (except exports and government services), its special characteristics being that it falls on the value added at each stage — from the stage of production to the retail stage. However, in practice, no attempt is made to directly ascertain the amount of value added, but instead each tax-payer is allowed to deduct from the tax payable on his output the taxes which he has paid on his inputs. This is an indirect but simpler method of reaching value added. This method also clearly brings out the fact that the producers are in effect freed from the taxation of inputs at every stage. Thus, VAT enables a country to have an extended commodity tax system and yet avoid the familiar problems created by other general taxes like the cascade-type sales taxes and excises. It is also relatively easy under the VAT system to free exports almost completely of internal commodity taxation

18.8 The VAT, in its comprehensive form, extends from the mining and manufacturing stages to the retail stage. In principle, it can replace all other forms of internal indirect taxes, and can also be extended to cover imports in so far as they are to be taxed for revenue reasons. Protective duties, where needed, would be levied; but apart from them, imports and domestic production would be put on a par and be subject to a single system of commodity taxation. There is great attractiveness in the simplicity and comprehensiveness of such a system of taxation, because it not only would enable the country to get rid of multiple forms of taxation but would also ensure coordination in the taxation of various products and services.

18.9 The economic advantages of the VAT system are many and obvious. However, in considering the necessity or desirability of moving over to VAT system in India, we have to examine a number of important questions:

(a) First, after the recommendations that we have made in regard to excises, and import duties have been implemented, what would be the further benefits to be derived by the introduction of VAT?

(b) Second, should the long-term objective be the replacement of the existing systems of excises, sales taxation, octroi and certain other indirect taxes by a comprehensive VAT?

(c) Third, if a comprehensive VAT system is ruled out, to what stages should VAT be confined?

(d) Fourth, would the advantage to be gained be significant in quantitative terms so that the attempted reform would be worth the cost and efforts involved?

(e) And, finally, would the administration of VAT be feasible in India?

18.10 As regards the first question, we have already expressed the opinion that while the measures of reform that we have recommended for immediate implementation are capable of bringing about a significant improvement in the system of indirect taxes prevailing in the country, they go only part of the way. Moreover, unless we put the excise tax system on a rational basis, it is really not possible to rationalise the import duty structure. The major objectives we have had in view in reforming excise taxation are : (i) to achieve a determinate degree of progression; and (ii) to avoid cascading and distortions. In attempting a rationalisation of the duty structure on final products, we came up against the problem of divergence between nominal rates and cumulative levies. We found that appropriate rates of duty on final products could not be determined on economic and social considerations unless we could find a way to deal in an adequate fashion with the cumulation of taxes at successive stages of production. As an interim measure, we have recommended that wherever a marked divergence between cumulative and nominal rates is found to exist, input duty relief under rule 56-A of Central Excise Rules may be provided. We have also suggested a gradual extension of the application of this rule, but these at best are half-way measures. In the long run, it would certainly not be desirable that input relief be provided only in respect of certain lines of production while in others cascading and distortions would be allowed to continue. Such discrimination would produce its own harmful effects. To pursue our reasoning to its logical conclusion,

we must think in terms of introducing a generalised form of tax credit. Such a system of tax credit would have to be made applicable not only to excises but also to import duties in course of time. Whether the system of tax credit should be operated under an explicit system of VAT or through a full application of the procedures under rule 56-A is a matter that needs separate consideration and is dealt with later.

18.11 As regards the second question, the introduction of a comprehensive VAT, which would replace at least the excises and sales taxes and which, in course of time, cover also the revenue as distinct from the protective element of import duties, would indeed have several advantages from the economic point of view. It would also be consistent with the oft-expressed desire of trade and industry to deal with a single tax authority in the indirect tax field, which in turn is at the root of the demand for the merger of sales tax with excises. There could be, however, two major arguments against the introduction of a comprehensive VAT in India: one is political and the other is administrative. The political argument is the obvious one that the loss of power to levy sales taxes would seriously erode the fiscal autonomy of the State Governments and weaken the federal principle that each subordinate level of Government should have the discretion to raise more or less revenue as the people of the State concerned desire. Without taking any side on this issue, we simply draw attention to the political judgment involved. The second argument points to the administrative problem of enforcing VAT at the wholesale and retail stages. Enforcement of VAT in relation to wholesalers and retailers is likely to create serious problems because, firstly, the number of taxpayers to deal with gets larger as we move further down the line in the chain of transactions; and secondly, the smaller dealers in a developing country, and even in developed countries, maintain only a primitive form of accounting and may find it extremely difficult to cope with the accounting requirements of VAT. Besides, the wholesalers, and more so the retailers, are likely to be dealing in a variety of commodities so that the matching of output and input taxes becomes more difficult in their case.

18.12 We, therefore, feel that it would not be prudent to think in terms of extending VAT to the retail and even wholesale stages in the near future. However, we recognise the validity of the argument that if the benefits of reform of the other parts of the tax system are not to be nullified, taxation at the wholesale and retail stages must be freed of the defects associated with the usual forms of sales taxation. Therefore, while not endorsing the plea for the abolition of sales tax, we have, in Chapter 13, urged that certain limitations be placed on the powers of the States to levy sales taxes and that sales tax systems themselves should be so re-oriented as to be in consonance with the reformed system of indirect taxation at the Central level.

VAT AT MANUFACTURER'S STAGE (MANVAT)

18.13 As regards the third question, it is our view that the VAT system should be introduced at the manufacturing stage. In the ultimate analysis, a satisfactory solution to the various distortions and problems that arise from an extended commodity tax system lies in the adoption of VAT at the manufacturing stage - the so-called MANVAT. The reformed system of sales taxation would act as a necessary supplement to MANVAT; while the MANVAT itself could in course of time be made to replace the revenue element in import duties. Given our federal system and the administrative problems of enforcing VAT at the post-manufacturing stages, the right course of action, in our view, is not to pursue the theoretically best solution, namely, one integrated system based on the VAT principle but to adopt the second best solution of MANVAT combined with a reformed system of sales taxation. While this solution would not completely eliminate the problems of cascading and cumulation, it

would reduce them to negligible proportions.

18.14 There is considerable truth in the view that elimination of distortions and cascading under excise system alone would not serve much useful purpose. However, unless the excises are put on a rational basis, it would be difficult to justify placing restrictions on sales taxation so as to rid it of its major harmful effects. Elimination of levies on inputs under the sales tax is a necessary sequel to the conversion of the excise tax system into MANVAT. Thus, while formally VAT would be applied at the manufacturing stage in lieu of the present excise system, it would be extended to cover imports; and the essential principle of VAT, namely, freeing of inputs from taxation, would get embodied in the sales tax systems. This is the long-term objective towards which we should move in a time-bound programme. It must be made clear that under MANVAT, relief will be provided only in respect of MANVAT paid at earlier stages.

18.15 As regards the fourth question, namely, whether there would be quantitatively significant benefits flowing from the adoption of MANVAT, we commissioned a study of the implications of applying VAT to the automobile industry with particular reference to the production and sale of trucks. An adapted version of the study is given in Appendix 22. Here, we may refer to the main findings of the study.

18.16 The cumulative levy of all indirect taxes on trucks and cars, sold in Bombay, are respectively 58.9 per cent and 50.2 per cent of the tax exclusive price, whereas the nominal rates add upto 31.9 per cent and 31.6 per cent respectively. Thus, without there being conscious intention, trucks and buses are taxed more than passenger cars. Under the proposed MANVAT system, since the rate applicable to the final stage would reflect the total burden on it (presuming inputs are also freed of sales taxes), the Government can adjust the burden/rate according to its scale of preference.

18.17 The benefits arising from the switch-over to VAT in replacement of all indirect levies could be quantified as follows in respect of trucks. The existing system results in two types of inflationary effects without adding to Government revenues. First, at each stage of production where the product changes hands, the mark-up is inflated to the extent that it is calculated on its total cost inclusive of taxes paid up to that stage; and second, higher interest costs are incurred because working capital is unnecessarily locked up as tax component of the cost of inventories of raw materials, work-in-progress, indirect materials and finished goods. For a truck or bus chassis, the inflated mark up effect comes to about Rs. 1, 500 per vehicle and the extra interest cost is estimated to be Rs, 1, 600 per vehicle. Thus, the increase in the ex-factory price of a truck or bus is Rs. 3, 100 higher than the amount which accrues to the Exchequer by way of indirect taxes, simply because of the cascading effects produced by the present system. This amounts to about 5 per cent of the tax exclusive price of a truck/bus chassis. The reduction in the cost of production will still be sizeable even if MANVAT were to be adopted in lieu of excises alone.

18.18 At present, export duty drawback is available at best for excise, customs and countervailing duties paid on direct material inputs. This is often much less than the total Central taxes paid on inputs at different stages of production. Under the MANVAT, there will be no indirect tax component in the price of exports.

18.19 There are other advantages that cannot be precisely quantified. At present, the cumulative tax burden on a product depends on the value added and the tax rate at the different stages as well as

on the number of stages involved. The cumulative tax-burden will be higher if the value added is more at the earlier stages and also will increase with the number of stages at which taxes are levied. The MANVAT would not mete out such discriminatory treatment.

18.20 Relative price distortions would also be eliminated under MANVAT because in effect inputs are freed from taxation. Manufacturers would, therefore, use factor combinations which would be most economical. The benefits in this case would accrue to the economy as a whole rather than to the industry as such and cannot, therefore, be easily quantified.

18.21 Finally, as regards the administrative question, the enforcement of MANVAT should not present insurmountable difficulties. In Brazil, a manufacturer's excise embodying the value added principle has been in operation for several years now and from all accounts has not caused any serious administrative problems. In India too, from the point of view of accounting, the larger manufacturers would not find it difficult to cope with the requirements of VAT and the number of manufacturers to be dealt with would be manageable. The smaller manufacturers in certain industries would pose some administrative problems, but this should not be considered a serious hindrance in view of the fact that the major part of the excise revenue is collected from a relatively small number of large producers. We have got conducted certain field studies to assess the magnitude and nature of the administrative problem and to get an idea of the type of accounting which the different types of businesses keep. These and other details relating to the administration of MANVAT are discussed later in this Chapter.

18.22 As explained in the previous Chapter, VAT can be applied in a number of ways. We would, however, recommend the tax credit method for adoption in India for MANVAT. The considerations behind this recommendation are as follows: First, it would always ensure that the actual rate of tax paid on a final product would be equal to the nominal rate of tax on it, because the entire tax paid on inputs is refunded at each stage. Per contra, under the alternative method, if there is more than one tax rate, the actual rate of tax on the final product will be the weighted average of the rates applied at the different stages of its production and would, therefore, not be equal to the nominal rate on it except for rare cases of coincidence. Second, many raw materials used by industry would not be subject to MANVAT. The sales minus purchase method would implicitly grant tax credit even in respect of those materials because the tax base is reduced by the cost of all raw materials including those on which no tax has been paid. This would mean not only loss in revenue but also an unwarranted exemption for certain materials from taxation at all stages. Third, the tax credit method is easier to operate because it does not require the computation of the precise amount of value added at different stages.

18.23 The tax credit provision under VAT is intended essentially to ensure that no cascading arises and distortions in relative factor prices are avoided. Keeping these objectives in view, we need to consider whether (a) the tax credit should apply to all inputs and (b) investment goods should also be made eligible for tax relief. The existing provisions for input tax relief such as rule 56-A are applied only to physical ingredients. Under MANVAT our aim should be to provide relief in respect of taxes on all current inputs including physical ingredients, consumer good stores and packaging material. As regards the treatment of investment goods, as indicated in the previous Chapter, in most of the European countries that have adopted VAT, full tax credit is given at the time of investment so that capital investment is in fact

TREATMENT TO INPUTS

freed of taxation. Such treatment is expected to boost capital formation in the country. The treatment, however, is not uniform in developing countries and there are instances where no credit for investment goods is allowed. Under Indian conditions, it would not be prudent to provide such relief not only because of revenue considerations but also because we have to avoid any action that would give encouragement to capital intensive methods of production.

MANVAT AND RULE 56-A

18.24 The intent and operation of rule 56-A under the present excise system has been explained earlier in the report. It provides for, in effect, an adjustment of tax paid on inputs against the tax payable on the output under certain conditions. The tax credit available under the VAT is exactly of the same kind. The extension of the scope for relief under rule 56-A which we have earlier recommended would in fact be one of the preparatory steps for the introduction of MANVAT. In fact, if the application of rule 56-A is generalised, it would amount to a virtual adoption of VAT at the manufacturing stage. However, a straight-forward adoption of MANVAT would have many advantages over full extension of the scope of the rule 56-A. Under the procedure laid down by rule 56-A, there are various requirements of maintenance of records and documentary evidence, as well as physical verification by the excise authorities. In terms of records, commodity-wise accounts in form RG-23 have to be maintained. For a multiple product firm with a wide range of ancillary spares, the efforts and costs involved in the up keep of such records could be prohibitive. Besides, as at present, we are informed that any cancellation/ erasure (even though genuine) in documentation disqualifies the tax credit claim.

18.25 As for physical verification, the rules specify that the manufacturer has to inform the proper officer within 24 hours of the receipt of duty paid inputs. The officer can then come and verify the quantity thereof. As the scope of application of rule 56-A gets extended, this process would entail considerable harrassment to a manufacturer who receives his materials and components through various consignments every day. It is learnt that in the case of a particular truck manufacturing unit, for example, around 300 consignments covering 300 different items are received daily. At present the departmental officers are required to verify the receipts where the duty involved exceeds a certain limit. The enforcement of this check under an extended operation of rule 56-A is bound to impose a severe burden on the tax administration and in a way it would be tantamount to reimposition of physical control on all factories.

18.26 To sum up, if the existing restrictions and checks are retained, a general application of rule 56-A to all or most of the inputs would involve several problems of administration and compliance. The system would become too cumbersome. If the restrictions are removed and more reliance is laid on accounts, we would, in fact, be moving towards the system of MANVAT. Therefore, while we have recommended a wider application of rule 56-A in the interim, we feel that in the long term solution lies in switching over to a system of MANVAT.

RATE STRUCTURE

18.27 As has been amply demonstrated by the experience of other countries, it would not be possible to work the VAT system with a plethora of rates of tax on different inputs and finished products. A single rate of VAT would greatly simplify the operation of the system. It is also favoured by theorists who advocate complete neutrality in indirect taxation. However, even most of the developed countries have found it necessary to have more than one rate of VAT and also to impose additional higher levies on a range of products including luxuries. In some countries such as Sweden, instead of a

fo mal increase in the number of rates, the tax base is reduced by a given percentage in certain cases so that additional discrimination in favour of the concerned commodities is brought about with the same number of rates.

18.28 It is sometimes argued that in a developing country like India, where taxa has to be used as a tool for achieving socio-economic objectives, it would not be possible to have a limited number of rates in our commodity tax system and that, therefore, VAT cannot be adopted here. We have endeavoured to show that a multiplicity of rates on final products is not necessary to achieve the social objectives of an adequately progressive distribution of the tax-burden among the different income or expenditure classes. In fact, we have favoured non-discrimination as between products belonging to the same class in the sense of being consumed predominantly by one income group or another. In our view, the desired degree of progression is more easily achieved with a limited number of rates than with a multiplicity of rates all of whose effects it is difficult to trace and control. Moreover, we have made a distinction between the basic long-term structure of rates on the one hand and additional taxes or rates that may be imposed for special purposes or temporarily, on the other hand. The latter would, by and large, be kept out of the MA VAT system. For example, if an additional duty on a scarce input is to be imposed in order to encourage economy in its use, then its very purpose dictates that it should not be eligible for tax credit under MANVAT. However, even these additional levies imposed for special reasons should be limited in number in order that the tax system does not become cumbersome once again. As far as the MANVAT is concerned, it could be operated on the basis of the four or five rates that would be applied to the vast majority of consumer products. The rationalisation of the duty structure on the basic raw materials and inputs would also have resulted in the reduction of rates on them. This would facilitate the operation of MANVAT.

18.29 We have indicated in the previous Chapter that in European countries as well as in certain developing countries, such as Brazil, which has adopted VAT, while the system is made applicable to all industries, some products like petroleum, tobacco and liquor are in addition subjected to non-refundable excise duties. In some countries, such as West Germany, certain luxury commodities are added to this list and are subjected to additional duties known as consumption taxes. We are of the view that under Indian conditions it would be preferable to keep a certain number of industries outside the scope of MANVAT and continue on them the present system of excises. These would include industries in respect of whose final products not much cascading is involved as well as those whose products have to be taxed at special or at high rates for economic or sumptuary reasons. Taxation of such products has to follow its own logic and cannot be fitted into the general system. The industries of this kind that we have particularly in mind are petroleum products, tobacco and tobacco products, sugar, coffee, tea and matches. Together they yielded in 1976-77 Rs. 2,081 crore, which formed 46.4 per cent of total excise revenue.

18.30 Theoretically, it would be a more satisfactory solution to follow the European practice and bring these industries also under MANVAT and then in addition subject them to non-refundable special duties. However, we have favoured their exclusion from MANVAT for three reasons: (i) for safeguarding revenue; (ii) for reducing the administrative burden of running the new system; (iii) for avoiding complications that might arise in claiming and verifying tax credits with two taxes operating in respect of a product, only one of which being eligible for relief.

18.31 In other countries which have adopted VAT, except France which gradually evolved the tax, the switch-over to the new system was brought about at one stroke. This was considered necessary to avoid frequent changes in rates which would be necessitated by a piecemeal conversion to the new system. We should also avoid a step-by-step extension of the MANVAT system. At the same time, we would not recommend a general switch-over without proper experimentation. We would recommend that a start should be made with three or four industries which produce final products (such as automobiles and diesel engines) in respect of which cascading and other ill-effects arising from wide-spread input taxation are pronounced. The introduction of MANVAT in the first instance over this limited area would enable Tax Administration to identify problem areas, test out procedures and study the reactions of tax-payers. On the basis of the experience so gathered, preparations could then be made to fully extend the system excluding the industries that we have listed above. On the basis of such evidence as we have been able to gather about the operation of VAT in a number of developed countries (some details of which have been presented in the preceding Chapter), it would appear that the administration of a VAT confined to the manufacturing level would not be beyond the capacity of tax authorities in India. However, we have recommended a cautious approach of starting with a pilot project because in the interest of safeguarding revenue, it is necessary to establish the workability of the new system before its widespread application is contemplated.

PROBLEM AREAS

18.32 An important problem that would have to be faced in extending the system of MANVAT would arise on account of the fact that, as revealed by our field studies (given in Appendix 21) several inputs are bought even by the bigger manufacturers through the medium of dealers who are not subjected to Central excise. Such a problem has been faced and successfully tackled by countries which have adopted VAT only at the importer's and manufacturer's level. France had to tackle this problem when, in 1954, VAT was initially experimented with at the manufacturing stage and special schemes were devised for this purpose. Based on the experience of other countries, it should not, therefore, be difficult to find an appropriate solution to the problem in the Indian context. The existing procedure under rule 56-A already allows tax credit if there is only one dealer in between two manufacturers. One method of tackling the problem is to allow dealers to register themselves voluntarily and to empower them to issue tax- vouchers. They would be expected to subject their books of accounts to verification by tax officials at the latters' discretion. A variant of the solution would be to permit the dealers, if they so choose, not only to register themselves but also to pay MANVAT at the appropriate rate, claiming tax credit as other MANVAT - payers. The payment of tax by the dealer would not, of course, increase the total burden of tax on the product concerned because the tax on the value added by him would, in any case, be collected at one stage or another. A better method may be to allow tax credit on a notional basis after deducting from the invoice prices a gross margin for the wholesale sector. Under this scheme, tax credit would be granted at notified rates, which would be related to the relevant rates of tax on the inputs as also to the pattern of production of the inputs in the organised and small-scale sectors. A number of Collectors of Central excise in the country, whom we consulted on this issue, were of the view that a system of notional credit would be workable and that sufficient precautions could be taken to prevent its abuse. A critical study of the schemes operating in other countries would be of help in devising the most appropriate solutions in the Indian context.

18.33 Before taking up the problems related to administration and accounting, we need to consider the proper treatment of small producers under MANVAT. The major point here is that we need to ensure that MANVAT would not materially reduce the relative advantages enjoyed by the small producer under the present system. An erosion of the benefits enjoyed at present may come about

because under VAT, a total exemption from tax is not an unmixed blessing. Non-payment of tax at one stage would automatically break the chain of tax credit which would be denied to the consumers of the exempted producer. In considering this question, we might conveniently divide small producers into two categories (i) those who manufacture and sell final products which would not be bought at any later stage by a producer for further processing and (ii) those who manufacture and sell components used in further manufacture. As far as the first category is concerned, total exemption would bring no diminution of benefit. But a mere exemption of the second category of small producers might place them at a disadvantage vis-a-vis the tax-paying larger manufacturer of components. Theoretically, the best solution is not to exempt the small producer of components, but to issue them licences under a special scheme and to zero-rate their products. (In other words, tax payable would be zero but tax credit in respect of inputs would be positive). However, this would involve refund of duty paid on inputs to the small producers and might be thought subject to abuse. Alternatively, instead of refunding the duty paid on inputs to the small manufacturer, a tax credit voucher could be issued to him for an equivalent amount which would be encashable not by him but by the taxable manufacturer who buys from him. Even under this alternative, there could be inflation of input costs. A practical solution would be to grant tax credit on a notional basis to manufacturers in respect of inputs bought by them from smaller producers working under a special scheme to be introduced for that purpose.

ADMINISTRATIVE FEASIBILITY

18.34 A point often made is that the book-keeping requirements under the VAT system are very rigorous and that even if VAT is to be introduced in lieu of excise, it would impose a severe burden on small and medium scale manufacturers. In the representations received by the Committee also, several Chambers and Associations have in fact made a similar plea. Especially, the trading interests have voiced serious apprehensions about a wholesale switch-over to VAT. As for VAT in lieu of sales tax, after considering the various issues and problems, we have, as mentioned earlier, reached the conclusion that the time is not yet ripe for a switch-over to VAT. However, as for a value added tax at the manufacturer's stage in lieu of excise, we felt, that prima facie, the additional documentation requirements may not be much. The Committee's Secretariat undertook a feasibility study on a small sample of manufacturing units mainly to assess the extent of documentation that presently obtains in manufacturing units in relation to their sales, purchases, stocks and production and make an evaluation of the gap in documentation between the present one and that required under a normal VAT system. Even though the sample study as such did not have a very wide coverage, care was taken to include in the sample manufacturers with different sales turnovers ranging from less than Rs. 2 lakhs per annum to that exceeding Rs. 1 crore per annum. The results of the study are brought in Appendix 21.

18.35 The main findings of the study are that in general, manufacturers whose turnover is in excess of Rs. 15-20 lakhs per annum get most of their inputs under cover of regular invoices, due accounts of which is kept in the books of the manufacturers. These invoices evidencing purchase of various types of inputs contain by and large the particulars which are required in the invoice under the VAT system, with the exception of a mention of the excise duty paid on the inputs. In the case of supplies received from the manufacturers, which constitute the major portion of the purchases of inputs by units whose turnover exceeds Rs. 1 crore, even this information gap is made good by the duty particulars contained in the excise gate-pass. Thus, in such cases, the invoice and the excise gate-pass together contain more than adequate particulars and if they could be suitably fused

into one, the basic documentary requirement under MANVAT would be met and also result in reducing scriptory work. However, invoices for purchases made from dealers do invariably fall short of one basic requirement under VAT in as much as they do not show the excise duty amount therein. If the same practice is continued even under the MANVAT, it would mean that purchases made from dealers would not be eligible for tax credit, unless alternative schemes of providing credit for such purchases are devised. (We have referred to this problem earlier). As regards the level and extent of coverage of book-keeping, we find that the present practice observed by units of this category should be adequate for VAT purposes also.

18.36 In the case of manufacturers whose turnover is less than Rs. 15-20 lakhs per annum, we find that the records relating to purchases, production and sales cover basic details though the system of accounting itself may not fully meet the requirements under a VAT system. To this extent, it may be necessary for them to maintain books of accounts in a more elaborate manner. The major accounting problem in their case would arise on account of the fact that the majority of their purchases of inputs is from dealers who do not indicate the excise tax amount separately in their invoices.

18.37 Thus, it could be assumed that manufacturers whose turnover exceeds Rs. 15 to Rs. 20 lakhs per annum could be reasonably expected to conform to VAT documentation without much difficulty. As for the other manufacturers, there may be a need to free them from the normal rigorous of VAT accounting. As indicated earlier, in the countries which have a VAT system, special schemes have been devised for similarly placed small assessees, under which they have to maintain only simple accounts and submit returns and pay duty at longer intervals than usually required under VAT. For determining the eligibility to such schemes, the turnover of the unit is usually taken as the criterion. We feel that in our country too, it should not be difficult to devise special schemes for the smaller producers whose turnover is below certain value limit, which could be about Rs. 20 lakhs as shown in the above-mentioned study or even higher if the circumstances so warrant. The Forfeit system as applied in France, Belgium and Brazil could be suitably modified and adopted in our country too. In fact, the simplified procedure scheme in regard to a few selected industries already in operation for collection of excise duty is quite similar to the Forfeit system. We have already suggested certain modifications to make the simplified procedure scheme more acceptable and also recommended its extension to most industries.

18.38 Our study of the pattern of clearances and duty realisation for units under different value slabs (given in Appendix 17) has shown that manufacturers with outturn not exceeding Rs. 15 lakhs per annum contributed about 3 per cent of the total excise revenue collections in 1975-76 (leaving a few industries like tobacco and petroleum products). Therefore, devising special schemes for smaller manufacturers under MANVAT would not pose any serious risk to Government revenue either.

18.39 In the MANVAT, as contemplated, there should not be much additional administrative burden as the number of units to be controlled under it will not increase. Besides, most of the smaller units would be covered by special schemes. It is, however, a fact that control and audit will have to be qualitatively superior and, perhaps, more elaborate too. It would be wrong to suppose that

VAT, even if confined to the manufacturing stage, could be administered solely or even mainly through the accounts method. While in some respects the system is self-policing, it also opens up some avenues for evasion. Thus, since, unlike the excise levy based on gross value, VAT is assessed on net value, there could be an inducement to overstate input costs. Under the tax credit method, this would take the form of claiming more than the tax paid on the amount of inputs actually used. Such a possibility is somewhat limited by the fact that the extra amount of inputs can only be sold to the untaxed sectors. Nevertheless, tax evasion under VAT has been noticed not only in developing countries but even in European countries. To prevent abuses of this kind apart from elaborate audit of accounts by trained personnel, periodic physical checking of inventories of goods on hand would be necessary under MANVAT. The magnitude of the additional administrative burden in this regard could be assessed while considering the pilot scheme referred to by us earlier and appropriate steps taken to strengthen the various aspects of tax administration in case MANVAT is extended to other industries.

18.40 The introduction of VAT in other countries was proceeded by a period of intensive training for tax administrators and education for tax-payers. As we contemplate the application of VAT only to the manufacturing stage in India and since in practice it would fall mostly on producers who are also excise tax payers, the problem of educating the tax-payers would not assume such a large proportion as in countries like Brazil where the system has been extended right up to the retail stage. Nevertheless, the importance of an adequate educational programme cannot be over-emphasised. Moreover, if our recommendation for the adoption of MANVAT is accepted by the Government, it would be necessary to send a small team to study the operation of VAT in some countries including a few developing countries. After that, a detailed programme of implementation should be worked out which would include, inter alia, devising of appropriate invoice and return forms, making the concerned industrial units familiar with their use, transitional problems relating to the treatment to be given to inventories on which excise tax would already have been paid, and the modalities of computerisation.

RELATION OF MANVAT TO IMPORT DUTIES AND SALES TAXES

18.41 If the excise tax system were to be put on a value added basis, relief would be given only for excise taxes paid on inputs. Such a relief cannot be given either in respect of sales taxes or customs duties. We have had occasion to point out that import duties on inputs often contribute significantly to escalation of costs and distortions in factor prices. Also sales taxation cannot be dismissed as a minor offender because one and the same input is sometimes taxed by more than one State and further because sales taxation encourages vertical integration and militates against the policy of encouraging ancillary industries. In the long run, therefore, relief in input taxation must be made available under all the three major indirect taxes in India. We would, therefore, like to reiterate our view that simultaneously with the introduction of MANVAT, or even preparatory to it, the existing system of sales taxation would have to be reformed along the lines we have indicated in Chapter 13. As regards import duties, we recognise that they cannot immediately be brought within the ambit of MANVAT. One of the main reasons for this is that at present fairly stiff rates on imported raw materials or intermediates are levied to bring in a sizeable amount of revenue. Import duties on inputs would have to be first rationalised according to our recommendations. They would then consist of a revenue element plus a component needed to protect domestic industry and to discourage the use of particular imported products (corresponding to the degree of import control). The revenue element in course of time should be

made equivalent to MANVAT on the same or similar domestic products, which would thus become a true countervailing duty; and when revenue needs permit, relief under MANVAT should be made admissible in respect of such countervailing duties.

18.42 We conclude our discussion of Long-term Reform of the indirect taxation structure as well as of our Report as a whole, by summarising very briefly how we envisage the process of change.

CONCLUDING OBSERVATIONS

Compulsions of mobilising resources on an adequate scale have led to a steady spread in the range or products covered by indirect taxation. In the process, since ad hoc changes were made from year to year with additions and super-impositions on a structure which was evolved during the phase of reliance on the taxation of inputs and selective taxation, a very complex tax structure has come into being in which the attempts to achieve progression by suitably fixing nominal rates on final products have been often eroded by the taxation of inputs; cascading has caused higher price increases than would be justified by the revenues accruing to Government; and there have been other distortions which are undesirable from the social, economic and administrative points of view. Distortions have also arisen as a result of the inter-action of independent indirect tax systems operated by two levels of Government independently of each other.

18.43 As a first step in reform, there must be a reduction in the number of excise duty rates applicable to different finished products, along with a similar change in the rates applicable to inputs, and a widespread application of procedures for giving relief from the taxation of inputs to those products which are themselves subject to excise levies. Side by side, the sales-tax system should be reformed so that it does not get enmeshed into the manufacturing process but becomes an instrument of taxing consumers within each State at such rates as the State Government and the State legislatures decide. Similarly, customs duties should be so adjusted that in addition to the element needed to provide protection to domestic industries, any additional levy on them is about the same as the excise on like products of domestic origin. Once this kind of restructuring of the existing tax system has been done, we will be ready to move on to MANVAT so that the taxation of the manufacturing sector of the economy is done through a system which will automatically ensure that the kind of distortions which have manifested themselves in the past do not appear. We have no doubt that MANVAT will be a vastly superior system over the existing regime. At the same time, we recognise that MANVAT requires certain capabilities in the matter of accounting on the part of those subject to it as well as administrative procedures different from those currently in force. The process of change may, therefore, have to be a phased one. To start with, MANVAT should be applied to industries in which the taxation of inputs has some definite dimensions and in which the manufacturers concerned are large. When the time comes to introduce MANVAT, which will only be after the requirements and changes particularly in regard to sales tax have been made, a number of industries could be selected for the initial phase, to be brought under MANVAT. In making the choice, apart from the criteria we have suggested, the willingness of the individual industries to switch over could also be given due weight. Once MANVAT has begun to function smoothly in respect of a few well-chosen industries, it could be extended to others, though it may well be that even in the long run certain products, such as, tobacco and tobacco manufactures and petroleum family, may continue to be subject to excise rather than MANVAT.

CHAPTER 19

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Indirect taxes as a source of revenue

19.1 In the effort to mobilise resources for development, indirect taxes levied by the Central and State Governments have been playing an increasingly important role; in 1976-77, they accounted for 79.3 per cent of total tax revenues. The share of indirect taxes in India was appreciably higher than the average share of such taxes in many developing countries as well as industrialised countries.

(Paras 1.9, 1.10)

19.2 Among the indirect taxes, the share of excise duties and sales taxes has been rising steadily while the share of customs duties, which has been subject to wide variations, has lately shown a downward trend.

(Para 1.11)

19.3 A study of the automatic change in the tax yields in response to changes in national income, in respect of individual indirect taxes for a recent period, shows that while sales taxes and customs duties had a fairly high degree of income elasticity, excise duties had an elasticity much below the desired level. The main reasons for the higher degree of elasticity in respect of import duties and sales taxes have been their universal coverage and predominance of ad valorem duties. As against this, excises, until recently, have been selective and have been by and large specific in nature.

(Paras 1.13, 1.14, 1.15)

Central Taxation - 1 Central excise duties

19.4 A major step in the rationalisation of excise duties was initiated in 1934 when their coverage was extended to sugar, matches and steel ingots. Since then, there have been selective additions beginning with products in the nature of mass consumption goods. As revenue needs increased the emphasis shifted to inputs. Year after year, the excise tax base was widened till almost the entire range of manufactured products was covered under excises in the year 1975.

(Paras 2.3 to 2.12)

19.5 For the purpose of control and assessment, several procedures and systems have been evolved leading to self-assessment and more reliance on documentary control. The administration of tax concessions to small scale manufacturers has also been sought to be simplified by introducing special procedures.

(Pareas 2.17 to 2.21)

19.6 Of the consumer products subject to excise, the major portion of revenue is derived from a select range of mass consumption goods. However, during recent years excise revenues from wage goods as a percentage of total excise revenues have shown a declining trend.

(Paras 2.24, 2.25)

19.7 Apart from the extension of the excise tax base, a notable feature of the excise tax structure is the move towards ad valorem duties in the place of specific duties. Nevertheless, a substantial portion of excise tax revenue is still derived from items subject to specific duties the more important of which are petroleum products, unmanufactured tobacco and ferrous and non-ferrous metals.

(Para 2.26)

19.8 One of the considerations which have been kept in view, while fixing the rates on final products, has been the progression in tax burdens. Similarly, objectives such as correcting imbalances between demand and supply, promotion of exports and protection to small scale industries and several other less important social and economic considerations have influenced the excise rate structure. There has been an extensive use of exemptions bringing into effect differential rates. As a consequence, the rate structure consists of a multitude of rates on consumer products, raw materials, intermediates and other inputs which differ not only between commodity groups but even within the same commodity group.

(Para 2.27)

19.9 The taxation of inputs has been looked upon as an important source of revenue even after excises have acquired a universal character. Procedures to mitigate the distortions caused by multi-stage excise taxation are applied on a limited scale.

(Paras 2.10, 2.30, 2.31, 2.32, 2.33, 2.34)

Central taxation - 2 - Customs Duties

19.10 Import duties, though primarily used for revenue purposes, have also been made use of to afford protection to domestic industries and to conserve foreign exchange.

(Paras 3.3 to 3.18)

19.11 After several attempts at rationalisation, the structure of basic import duties has now acquired stability. The scale of import duties has been related to the degree of processing undergone by different kinds of imported products. Accordingly, lower rates have been prescribed for basic raw materials and capital goods. A middle rate has been fixed for goods which have undergone some processing from the basic raw material stage and a high rate has been prescribed for fully processed goods. Some products, e.g., foodgrains, skimmed milk powder, etc., have been exempted from import levies on social considerations and some others on considerations of assisting exports. In contrast, on considerations of protection, higher import duties have been prescribed for some other articles of import. In the course of the evolution of the tariff, release from bindings under General Agreement on Trade and Tariff (GATT) for several items has been secured on considerations of protection to indigenous industry and revenue.

(Paras 3.19, 3.20, 3.21, 3.22)

19.12 Apart from the basic import duties which have been fixed on a three-tier basis, there are auxiliary duties applied on a similar basis and countervailing duties which are calculated on the basis of c.i.f. price plus the basic duty and auxiliary duty. Thus, even though the basic duty structure has apparently been rationalised, application of auxiliary and countervailing duties ultimately results in a large variety of rates.

(Paras 3.23, 3.24)

19.13 The yield from import duties when broken up shows that the major contribution is from the import of inputs - raw materials and intermediate products.

(Para 3.28)

19.14 Export duties have begun to perform more of a regulatory than a revenue earning function.

(Para 3.25)

19.15 There has been a limited adoption of the Customs Cooperation Council Nomenclature for import duty purposes. The new tariff merges a very large number of nomenclature headings in the CCCN and, in the process, has apparently led to an increase in the effective rates of duty on a number of products.

(Paras 3.30 to 3.32)

Indirect taxes at State and Municipal Levels

19.16 Sales taxation is the most important source of revenue to the States accounting for about 57 per cent of their total tax revenues. Its share has been steadily increasing. Correspondingly, the importance of land revenue and State excise has been declining.

(Para 4.2)

19.17 Following the recommendations of the TEC, a major change was brought about in the sphere of inter-State sales tax with the enactment of the CST Act whereby exporting States were conferred powers to impose a tax on inter-State exports at the rate prescribed in the Act. The development of the sales tax systems subsequent to the TEC Report, did not adhere to the pattern recommended. It has rather been conditioned by several considerations such as raising revenue, encouraging investment and providing simpler administration. There are three types of sales taxes levied - the single point, the double point and the multi-point. In practice, there are mixtures of these types in individual States. There are variations in the systems of sales taxation found in different States, but a common trend towards the imposition of a single-point tax can be discerned.

(Paras 4.4 to 4.11)

19.18 The rate of multi-point sales tax is generally 4 per cent. In the States following the single point system, the general rate varies from 4 per cent to 7 per cent. Luxuries are generally subjected to a single point levy and taxed at higher rates up to 15 per cent.

(Paras 4.12, 4.13)

19.19 As regards the treatment of raw materials and intermediate products under sales tax, the practice followed by individual States varies. While some grant full exemption, others grant only partial concessions. These are often linked to the fulfilment of certain conditions.

(Paras 4.15 to 4.22)

19.20 As sales taxation in the country is based both on origin and destination principles, it often happens that the sales tax levied by one State falls on the residents of other States.

(Para 4.23)

19.21 One of the measures of Central regulation of sales taxation is the enactment of the CST Act. The provisions of this Act have been used to regulate the rate of sales tax on goods of special importance in inter-State trade and to fix a ceiling on the rate of CST; with the efflux of time the CST rate has increased to 4 per cent from the original rate of 1 per cent.

(Paras 4.24 to 4.28)

19.22 Another important development is the levy of Additional Excise duty in lieu of sales tax on tobacco, sugar and textiles. As the State Governments complained that their share of revenue from Additional Excise duties had not kept pace with the increase from time to time in the yield of Basic excise duties, the matter was considered in 1970 by the National Development Council which decided that the rates of Additional Excise duties should be revised upwards within a period of two to three years so as to yield 10.8 per cent of the value of clearances and that in future the ratio between Basic and Additional Excise duties should be roughly 2 : 1.

(Paras 4.29 to 4.31)

19.23 Sales tax on motor spirit is levied under a separate enactment in many States, while others have merged it with the general sales tax. The yield from this source has increased fairly rapidly in the last 15 years.

(Para 4.32)

19.24 After sales taxation State excise on liquor is an important source of revenue for the States. In addition, excise duties on medicinal and toilet preparations containing alcohol and narcotics are levied through a Central Act. The rates of duty under this Act on such preparations are considerably higher than those applicable to medicines leviable under the Central Excise Act. Other taxes, which include, inter alia, tax on motor vehicles and tax on passengers and goods taken together contribute about 18 per cent of the State tax revenues.

(Paras 4.34 to 4.39)

19.25 For many States, electricity duty does not have considerable revenue significance. The base and rate of electricity duties vary from State to State.

(Paras 4.40 to 4.45)

19.26 In many States, octroi is the foremost source of revenue to local bodies. In some States, revenue has been raised for local bodies without resorting to octroi. The system of collection and the rate for octroi vary considerably as between States as well as between local bodies within a State.

(Paras 4.51, 4.52)

Interaction of Central and State Taxes

19.27 The overlapping co-existence of excises and the sales tax, each compounding the effects of the other through inter-action has given rise to uncontrolled and unintended incidence on different commodities. Where the commodities involved have an imported content, the compounding effects are further aggravated.

(Paras 5.1, 5.2)

19.28 The extensive taxation of inputs as well as final products and that too by different authorities has led to the following effects:

(i) The total burden on the consumer is usually much higher than the rates of tax imposed on final products. The levy of taxes on taxes and higher profit mark-ups and financial burden due to the need for a larger amount of working capital resulting from multi-stage excise and sales taxation of inputs contribute to an all-round escalation of costs and profits. Extensive taxation of inputs has caused divergence between the nominal rates on final products and the cumulative rates on them.

(Paras 5.3 to 5.10)

(ii) A heavy tax at the input stage also tends to be regressive. It encourages manufacturers to produce more of expensive varieties out of the same input.

(Para 5.12)

(iii) Taxation of inputs also tends to encourage vertical integration, the manufacturer producing more and more of the inputs needed by him rather than buying these from ancillary industries.

(Para 5.13)

(iv) Taxation of inputs affects exports adversely inasmuch as the former becomes a part of the costs of production. The effectiveness of the drawback system is eroded, as it becomes virtually impossible to calculate exactly the total quantum of indirect levies on a product which is to be exported. Further, sales taxes and octroi duties are not taken into account in the drawback calculations, while the States generally extend only limited concessions in respect of inputs under their sales tax systems.

(Paras 5.14 to 5.17)

The Incidence of indirect taxes (1973-74)

A study of the distribution of the burden of indirect taxation among different expenditure groups has revealed the following features:

19.29 The share of the tax burden on the rural sector in 1973-74 is seen to have fallen as compared to 1963-64, while the share in population of the rural sector declined slightly.

(Para 6.9)

19.30 In terms of percentage of expenditure, the tax burden appears to have been distributed in a progressive manner. The progression is also seen to prevail among rural and urban households taken separately. As far as indirect taxes alone are concerned, despite widespread taxation of inputs, the tax burden turns out to be uniformly progressive.

(Paras 6.11 to 6.13)

19.31 Indirect taxes fall even on the poorest sections of society.

(Para 6.14)

19.32 Central taxes account for the largest share of incidence in both the rural and the urban sector. As between Central and State indirect taxes, the former are more progressive. In the rural sector, the incidence of taxes on intermediate goods is higher than that of taxes on consumption goods for the lowest two per capita expenditure groups; for all the groups above them, the incidence of tax on consumption goods is higher. In the urban sector, the incidence of taxes on intermediate goods is slightly lower for the same two lowest per capita expenditure groups.

(Paras 6.16, 6.17, 6.19)

19.33 In respect of excises as well as import duties, intermediate goods claim the largest share of the incidence both in the rural and urban sectors.

(Para 6.20)

19.34 In the case of State taxes, consumption goods account for a very high share of incidence as compared to the other two groups of commodities in both the rural and urban sectors.

(Para 6.22)

19.35 Among food products, the taxes on sugar, foodgrains and atta affect all expenditure groups but their impact is regressive with respect to total expenditure. A reduction in the weight of taxes on mass consumption goods such as sugar, foodgrains and kerosene that tend to be regressive or proportional would serve to increase the degree of progression of the indirect tax system. The taxation of certain intermediate products such as iron and steel, diesel oil and tyres and tubes has a pervasive effect. However, incidence of these taxes turns out to be progressive.

(Paras 6.23, 6.24)

The Role of indirect taxes

19.36 Since one of the prime objectives of taxation is to restrain increases in consumption with a view to divert real resources for purposes of development, taxation has necessarily to fall on the bulk of the population.

(Para 7.1)

19.37 Taxation, while raising resources for the Government, should also subserve important socio-economic objectives.

(Para 7.3)

19.38 A system, where articles of comfort and luxury are taxed at substantially higher rates than basic necessities of life, will be in accord with the objective of progression.

(Para 7.4)

19.39 In India, indirect taxation will have to be non-neutral for bringing about reallocation of resources according to Plan priorities and for achieving progression.

(Para 7.5)

19.40 Indirect taxation should be non-discriminatory in so far as the objective is to raise revenue; but where intervention is called for, indirect taxation may be selectively used for causing diversion of resources through changes in relative prices.

(Para 7.8)

19.41 If the tax system were made more income elastic than in the past, there would be less need for raising the rates of tax on individual commodities from time to time.

(Para 7.11)

19.42 Some features of the tax structure like heavy taxation of raw materials or differential taxation of raw materials and other inputs imposed mainly to raise revenue reduce the efficiency of the system.

(Para 7.12)

Principles of reform - excise and customs

19.43 The rationalisation of indirect taxation in the country hinges on the reform of the excise tax system into which other components could be dovetailed.

(Para 8.2)

19.44 In the sphere of Central indirect taxation, though import duties and excises are to be treated similarly from the point of view of raising revenue, they have to be given their distinctive roles and tailored to produce the desired economic effects.

(Para 8.5)

19.45 On various considerations, a single integrated indirect tax system in the country extending from import and manufacturing stage down to the retail stage might have to be ruled out in favour of two or more taxes to be levied by more than one authority. If so, the endeavour should be to ensure that they are rid of their major deficiencies and become the building blocks for a harmonious indirect tax system.

(Para 8.5)

19.46 Low elasticity of excises has been due to inadequate coverage and widespread reliance on specific duties in the past. The crux of the reform of excise taxation is the fashioning of an extended system with an adequate device for eliminating the harmful effects of input taxation. Further, ad valorem duties are preferable to specific duties to avoid frequent revisions of rates for meeting revenue needs which tend to create distortions and irrationalities.

(Paras 8.14, 8.15)

19.47 The basic structure of the system should not bring about unintended re-allocation of resources or influence producers' choice in relation to the use of inputs, location of industries, etc., in a manner that leads to loss of efficiency and welfare.

(Para 8.16)

19.48 Where there is no special reason for interference, like products should be taxed in a non-discriminatory fashion. While consumer goods largely consumed by upper income groups should be taxed at higher rates to ensure progression and to restrict the flow of investment into the production of non-essential goods, it would be desirable to apply the same high rates to the entire range of products in this class unless there are good social or economic reasons for introducing differentials.

(Para 8.17)

19.49 A plethora of rates makes tax administration as well as tax compliance a complicated matter. Various consumer products should, in course of time, be fitted into four or five (cumulative) rate categories.

(Para 8.18)

19.50 It may be necessary to have some in-between rates in the initial stages of rationalisation of nominal rates. Certain category of products such as petroleum products, tobacco, matches and textiles, whose taxation has its own logic, may have to be kept out of the above rate structure.

(Para 8.20)

19.51 There would be considerable advantage in introducing as early as possible a scheme of comprehensive classification so that in effect tariff item No.68 should be done away with and each new product from the very beginning be brought under the appropriate rate category. It would be necessary to examine whether some of the items that are now taxable only at 2 per cent should not be taken out of that list and fitted into the appropriate rate categories.

(Para 8.21)

19.52 The yardstick of price before tax would be the best one to employ in determining whether particular varieties of a product should be considered as being primarily consumed by the rich or the poor

(Para 8.24)

19.53 As a general rule, a single rate should be applied to a class of similar products unless there is a clear cut distinction, arising on account of a differentiation based on substantially different prices

(Paras 8.24, 8.25)

19.54 The heavy reliance on the taxation of inputs has led to several undesirable effects. In an extended system of taxation of final products, it would not be possible to unconditionally free from taxation goods that are used as inputs or components. The ideal solution would be to make a distinction, for tax purposes, on the basis of the nature of use and not on the basis of category of goods. Whatever is used for further production by manufacturers, who are themselves subject to tax, should be given suitable tax relief, while the same product, if it goes direct to the consumer, will pay tax at the appropriate rate.

(Paras 8.28, 8.32)

19.55 Studies undertaken show that basic raw materials as a class bear a substantially higher average rate of duty than semi-processed and final products. One of the steps towards rationalisation of the excise duty structure would thus be to bring about a reduction in the average rate of taxation on raw materials. Any significant reduction in the average rate of tax on raw materials would, however,

have to be accompanied by a compensatory upward revision in the rates on final products to safeguard revenue.

(Paras 8.33 and 8.34)

19.56 It would neither be feasible nor desirable to reduce the rates of tax on raw materials to such a low level as to obviate the need for a system of tax credit. In the long run, a proper relationship between the rates of tax on final products and on raw materials will have to be brought about.

(Para 8.35)

19.57 The following general guidelines for the taxation of inputs are recommended:

(i) A generalised system of tax credit should be introduced in course of time.

(ii) Various raw materials and other inputs should also be subject to a limited number of rates of duty in place of the present wide variations in rates.

(iii) Raw materials which are substitutes for each other, should, as a rule, be taxed at similar rates unless the use of a particular raw material needs to be economised on wider considerations justifying a higher levy. In the latter case, it would be desirable to levy a separate differential duty which should not be eligible for tax offset at later stages.

(iv) Inputs which are capable of being used as final products should be subject to such rates of duty as may be appropriate for them as finished consumer products, while those goods which are primarily used as inputs and do not have much use for replacement purpose should be subjected to the same rate of duty as applicable to the finished products in whose manufacture they are mostly used. In both cases, the aim should be to provide tax credit in respect of duty paid on such inputs to producers who use them for further manufacture, even if it needs some adjustment in the rates of tax on final products.

(v) Taxation of packaging materials also calls for rationalisation. In general, the excise duty burden on different packaging materials should be broadly the same except for the discrimination in favour of packaging made of waste material. Further, wherever the duty on packaging materials adds considerably to the cost of manufactured commodities, which are essential in nature, suitable relief in respect of duty paid on packaging materials should be considered.

(Para 8.36)

19.58 A value added tax system at the manufacturer's stage would be the best means of achieving the twin objectives of having an extended tax system and avoiding the distortions that flow from input taxation. Pending its introduction, the fullest use should be made of the existing provisions and procedures to give relief from the cascading effects of input taxation.

(Para 8.37)

19.59 There should be a substantial extension of the application of rule 56-A. The tax credit allowed under this rule should cover, wherever economic considerations so warrant, packaging materials and consumable stores also.

(Paras 8.38, 8.40)

19.60 The provisions of rule 56-A should be preferred to other procedures for extending relief of input taxes. However, the differential excise duty that may be specially imposed on some raw materials for promoting their economic use should not be eligible for tax relief.

(Paras 8.41, 8.42)

19.61 The steps towards rationalisation of the excise rate structure should be taken in the following order:-

(i) Rationalisation of the duty structure in relation to basic raw materials, keeping in mind the constraint that the resultant reductions in the average rate of tax on raw materials should not appreciably exceed 5 percentage points for the time being

(ii) Rationalisation of the rate structure of final products (excluding certain groups such as petroleum and tobacco products, but including consumer goods now falling under tariff item No.68) in terms of nominal rates of duty ranging from 2 to 35 per cent

(iii) Extension of the application of rule 56-A to the manufacturers of all products (whether final or intermediate or capital goods) in respect of which the difference between the nominal rate and cumulative rate is significant indicating the presence of appreciable cascading

(iv) Corresponding adjustments in the nominal rates of duty on the same final products so that they will fall under one or other of the cumulative rate categories we have suggested

(v) More or less simultaneous adjustments in the rates of duty on packaging materials, components and goods that are used both as inputs and final goods for replacement purpose.

(Para 8.45)

19.62 While under Indian conditions it may not be justified to free capital goods of taxation as in European countries, there are good reasons for keeping the rate low. By and large, the cumulative rate on most machinery items now range from 2.6 to 5 per cent. This being so, it would be preferable to leave the nominal rate of duty on capital goods at 2 per cent barring certain exceptions.

(Para 8.48)

19.63 The measures recommended should impart sufficient elasticity as well as a measure of stability to the system. If, at any time, it is desired to divert a still higher percentage of national income to the exchequer, then a small and uniform percentage increase in the rates of tax on all products should be preferred to selective increases so that the basic structure of taxation and the relative rates on different products are not disturbed.

(Para 8.50)

19.64 Long term investment priorities can be built into the long term structure of the excise tax system. Moreover, there are a number of other objectives which need to be considered separately and the means of achieving them, in so far as it is desirable to do so through indirect taxation, would have to be grafted on to the basic long term structure. In general, adjustments in levels of excise

taxation should not be used to achieve minor or trivial objectives. To prevent abnormal profits being made in a situation of scarcity of a product, there could be a temporary increase in the excise duty in the form of an additional levy, with readiness to lower it as the supply position improves. It must not, however, be so high as to discourage fresh investment which would be necessary to relieve the shortage. It would be preferable to keep the additional levy distinct from the Basic excise duty, and its period of validity should automatically expire when the next Budget is presented - unless a decision is taken at that time to continue it for a longer period. Similarly, if for an unforeseen contingency substantial additional revenues have to be raised, there may be advantage in making a small surcharge applicable across the board to all the items which are subject to excise duties for a fixed temporary period.

(Para 8.51)

19.65 Apart from being a revenue measure, import duties have also two important economic functions to fulfil, namely, to protect domestic industries as decided upon by Government and, wherever necessary, to discourage the expenditure of scarce foreign exchange.

(Para 8.53)

19.66 In the absence of quantitative import controls, protection to domestic industries has to be afforded by the protective components of import duties. A coordination of import control policies with the import tariff would be necessary where import control is in existence and is the major means of giving protection and conserving foreign exchange.

(Para. 8.54)

19.67 Where imports of a number of goods are severely restricted and substantial excess demand is generated at prices equal to the landed costs of imports, heavy import duties could be justified to prevent the import licensees or others from making large unearned incomes. It would be preferable, in such cases, wherever possible, to canalise imports through a State agency or to arrange that they go directly to the actual users with appropriate arrangements to ensure that the benefits of the low price is passed on to the ultimate consumers. This would help keeping the protective element at the appropriate level so that potential domestic producers would get the right signals.

(Para 8.55)

19.68 A rationalised structure of import duties should broadly consist of the following elements:

(a) A levy adequate to give the degree of protection deemed necessary for particular products

(b) A revenue element, which may be called the countervailing duty, being equal to the excise duty leviable on the same or similar domestic products

(c) A discriminatory duty on products necessary to skim off the excess profits. This can be looked upon as a surcharge for discouraging imports.

Of these, between (a) and (c), whichever is higher should apply. For the purpose of arriving at the base for the countervailing duty, it would be proper to include only the landed cost of imports (excluding duties) and the notional protective element, if that should be lower than the discriminatory duty.

(Para 8.56)

19.69 The import duty structure, as it obtains today, does not satisfy a consistent set of principles. The economic effects of high duties have been severely ignored in the interests of revenue. As a result, several high-cost, uneconomic industries have come to be established. The rates of duty on most products today appear much higher than what would be justified on the basis of the principles enumerated above. Duties on intermediates and machinery will particularly have to be brought down to lower levels. In view of the substantial revenues involved, this could be attempted in phases.

(Para 8.59)

19.70 It is not possible to adumbrate a general principle or policy as to whether import duty in respect of capital goods should be fixed at a level sufficient to give protection to domestic industry and then their import should be liberalised or whether it would be necessary to continue a fairly strict import control policy in order to continue the protection to the domestic industry producing machinery. For capital goods industries which are well established, it would be preferable to liberalise imports, the protective tariff being retained at a level sufficient to give protection to domestic producers. For newly set up industries meeting only a part of the country's requirements, a much greater reliance on import control will have to be continued.

(Para 8.61)

19.71 The present rate of duty at 75 per cent on intermediates and semi-processed materials is too high to be justified on any rational economic considerations. Where indigenous capacity of intermediates and semi-processed goods already exists, or is likely to be set up in the near future, the rate of duty on them should not be much more than what is just adequate for protection, provided the level of imports is sufficient to meet the full requirements of industries using such intermediates and semi-processed goods.

(Para 8.62)

19.72 The level of duties on individual products or categories should be determined on an industry by industry study, which might appropriately be entrusted to an organisation like the Bureau of Industrial Costs and Prices. Such an organisation could also indicate the level of imports necessary for proper utilisation of capacity of user industries.

(Para 8.63)

19.73 The scaling down of duties on imported products will have to be both selective and phased. The following areas may deserve priority action -

(a) where a reduction in duty will help lowering the price of basic necessities such as food, clothing, shelter, education, health and transport;

(b) where a reduction in duties while lowering the revenue realisation per unit of import, would in fact augment revenues because the volume of imports would go up.

(c) where the cheapening of certain imported products would have a long term favourable impact on the development process, including the promotion of employment; and

(d) where the duty on a particular input is unduly high, compared with the levies on competing inputs.

(Para 8.64)

19.74 As import controls continue to exist, there should be proper coordination of tariff policy with import control policy while effecting changes in duties on any product. The following general approach in certain category of cases is recommended:

(a) On items in which we are self-sufficient and it is considered desirable to meet the additional demand (with the growth in economy) by way of imports rather than increasing indigenous production, import duty levels should be such as to equate the landed costs of imports to domestic prices.

(b) In the case of inputs, a substantial proportion of the demand for which, is met out of local production and only a relatively small gap between domestic production and demand is met by imports licensed to actual users, the level of duty should be such as to keep domestic and import prices at par

(c) Where a small proportion of demand of a product is met out of local domestic production and the rest of the demand is met out of imports that are much cheaper, the proper way of protecting domestic industry would be either to give a subsidy to the domestic producer or to arrange for a pooling of prices.

(Para 8.65)

19.75 Import duties on inputs have become a major contributor to cascading and general escalation of costs, besides often producing distortions in relative prices.

(Para 8.66)

19.76 Keeping in view the revenue implications, in the immediate future input tax relief may be extended even for import duties (under a procedure similar to rule 56-A) in relation to a limited number of products in whose cases cascading and other distortions seems to be particularly severe and harmful.

(Para 8.67)

19.77 No countervailing duty should be levied on imported goods not being produced at home and not competing with any indigenous products. However, it would be legitimate to subject them to a revenue duty at the appropriate level, after a careful consideration of the duties likely to be applied to them if produced at home.

(Paras 8.70, 8.71)

19.78 The role of export duties in the future would be essentially an economic one of driving a wedge between high overseas prices and lower domestic prices so that export demand does not unduly raise internal prices. It should be ensured that frequent and sudden changes in export duties on short-term considerations do not damage the long term prospects of our exports.

(Para 8.72)

Approach to Rationalisation

19.79 The task of rationalising the indirect tax system has to be viewed neither as a revenue raising exercise nor as an occasion for lowering the overall tax burden.

(Para 9.5)

19.80 If account is taken of the levy on the inputs, the average cumulative rate of excise on consumer products works out to something like 20 per cent (excluding tobacco and petroleum products as well as goods falling under tariff item No.68); but, the nominal and consequently the cumulative rates show a wide amplitude. However, a study of the prevailing rate structure does not indicate that the levies on different products have in fact been determined on clearly defined criteria, like progression, economic considerations for discouraging consumption of an article, making a draft on scarce resources, and prevention of investment in low priority areas.

(Para 9.6)

19.81 A multitude of rates is not desirable either on considerations of progression or on economic and administrative ones.

(Para 9.7)

19.82 In fitting different consumer products into the appropriate categories, the approach could be to examine whether there are reasons to tax a given product at a higher or lower rate than 20 per cent (cumulative). Where the levy on inputs does not cause a divergence of more than 3 per cent between the nominal rate and cumulative levy of excise, the final rate could well be fixed, ignoring the levy on inputs. Where, however, the divergence is greater and relief under rule 56-A or other procedures is not available, the rates of duty on final products could be fixed at appropriately lower levels to narrow the gap. When a rate higher than 40 per cent (cumulative) is to be imposed on any product, its implications should be carefully considered.

(Paras 9.8, 9.10)

19.83 If relief to the lower income groups is considered to be desirable, powers under the CST Act can be used to lower the tax on inter-State sales of foodgrains.

(Para 9.14)

19.84 While the rates on levy sugar may well be kept low, a wide disparity in the rates of tax on levy and free sale sugar can lead to some undesirable consequences.

(Para 9.15)

19.85 Consumers' choice between like products should not be unnecessarily interfered with by differential levies on refined oil and vanaspati. Consideration should be given to applying the same ad valorem rate to both products.

(Para 9.16)

19.86 Having ad valorem duties increasing with the price is one of the simplest ways of achieving progression in the excise levy on textiles. With the compulsion on textile mills to use a certain proportion of synthetic fibres and yarns instead of cotton only and in the light of the reference in the Industrial Policy Statement to the use of polyester fibre as a raw material for khadi, it would be safe to presume that the initial policy of discouraging the use of synthetic fibres and yarn stands reversed. Various studies show that lower income groups do make use of synthetic and blended fabrics, provided the price is low enough.

(Paras 9.18, 9.19)

19.87 The real test to apply in distinguishing between the cloth consumed by the rich and the poor should be the price factor. On this basis, the cheaper cloth should be taxed at a lower rate. If progression is desired, those in higher price brackets can be taxed at higher ad valorem rates. This should be done on a slab system. Such a gradation will encourage mills to produce lower priced fabrics and at the same time eliminate the dangers of abuse.

(Para 9.20)

19.88 The mere fact of the cloth being categorised as coarse or fine is not a good basis for discriminating levies, either on social or economic considerations.

(Para 9.21)

19.89 A switch over to ad valorem duties on cotton yarn would have the added advantage of reducing assessment disputes, laboratory tests and other complications which arise because a difference of even one count can make a material change in the tax liability. If it is necessary to levy discriminating duties on fabrics on account of difference in raw material content, it would be appropriate to introduce the necessary differentials at the yarn or fibre stage.

(Paras 9.22, 9.23)

19.90 About the extent of the discrimination at the fibre/yarn stage and the considerations on which it should be based, trends of Government policy as well as an assessment of the situation suggest that the very wide differential between cotton and yarn of man-made fibre has to be steadily reduced. In bringing about a reduction in the cumulative levy on fabrics made of man-made fibres and yarn, the trend should be towards shifting the levy from the raw material stage towards the more processed articles. Overall, the attempt should be to shift as much of the burden to the fabric stage and to fix the tax at the yarn stage at such a level that its incidence on the decentralised sector is just adequate to obviate the need for excise control.

(Paras 9.23 & 9.24)

19.91 To overcome the cumbersome process of ascertaining denier/count/ composition and to ensure progression and equitable incidence of duty, the levy on fibre and yarn should be on an ad valorem basis.

(Para 9.25)

19.92 Taking into account the wide disparities of climatic conditions in the country, woollens should not be ranked much below cotton in importance. Considering that hand-knitting woollen yarn has a potential of becoming a major source of employment and for meeting domestic demand and for export purposes, the existing levy thereon seems to be much too high on any criterion.

(Paras 9.28 & 9.29)

19.93 The duty incidence on woollen textiles should be shifted forward and to start with the customs duty on raw wool should be substantially lowered. The duty on the final product should be graded in a manner which will weigh more heavily on the more expensive fabrics than on cheaper ones. High levies on polyester and acrylic fibres create distortions and undesirable repercussions.

(Para 9.30)

19.94 The present odd rate, on printing and writing paper, which is used by the student class, should be maintained at the existing low level and rounded off to 5 per cent ad valorem.

(Para 9.32)

19.95 Wide tax differences can adversely affect the production of varieties of paper taxed at relatively higher rates, whose production may be otherwise desirable. It would be more rational for all printing and writing paper, other than those subject to an informal price and distribution control to be taxed at a uniform rate.

(Para 9.33)

19.96 A reconsideration of the need for continuing the duty differential between packaging and printing paper, which often leads to classification disputes, is called for.

(Para 9.35)

19.97 There is need for making changes in the existing excise duty concessions to smaller paper mills. It would be more scientific and rational to link the concession with the value of production than base it on capacity considerations. Unless it is Government's intention to discourage production of certain varieties of paper by smaller paper mills, there seems to be no strong reason for the denial to them of the benefit of concessional duty in respect of those varieties of paper and all varieties of paper boards.

(Paras 9.36 & 9.37)

19.98 In regard to certain industrial varieties of paper, there is a case for lowering the present rate of customs duty of 100 per cent, as they are used as inputs and not as consumer products.

(Para 9.38)

19.99 The list of medicines in the nature of life saving drugs, which are taxed at a specially low rate, needs more frequent review and suitable expansion.

(Para 9.40)

19.100 While a higher rate of duty on medicines, which can be properly regarded as patent and proprietary, could cause a beneficial shift towards the production of medicines sold under a generic name, the existing difference in rates should be narrowed down.

(Paras 9.42, 9.43)

19.101 A panel of qualified experts should be set up to suggest (i) a list of drugs covered by the Medicinal and Toilet Preparations Act, which cannot possibly be used for non-medicinal purposes, so that they could be excluded from the scope of high levies and (ii) a list of drugs needed for treatment in critical ailments - which despite the risk of diversion, may merit taxation at lower rates.

(Para 9.44)

19.102 Import duties on bulk drugs as well as intermediates have also to play a protective role. In considering any adjustments in order to reduce the cumulative levies which are judged to be too high, it would have to be ensured that domestic production of like products, if it exists, is not hurt. Where

there is no domestic production, the import duty could well be lowered to a level, which is deemed adequate for affording protection to new investment.

(Para 9.47)

19.103 The special study on the taxation of road transport industry shows that:

(a) indirect taxation of road transport has a perceptible impact even on the lowest expenditure groups.

(b) The pervasive and multi-stage taxation on manufacture and sales of trucks and buses results in a very high cumulative levy.

(c) The system of taxation results in the locking up of extra working capital.

(d) Trucks and buses meant for transport are taxed higher than personalised transport like cars and scooters.

(e) Taxes that affect the cost of operation increase operating costs by about 50 per cent for trucks and 45 per cent per passenger bus per passenger km.

(f) There is considerable divergence between States in the tax rates on goods and passengers.

(Para 9.49)

19.104 A strong case seems to exist both on social and economic considerations for a reduction in the total burden of the various levies affecting road transport.

(Para 9.50)

19.105 Since the Centre and the States tax the road transport industry, a concerted plan of action is needed. Discussions between representatives of the Centre and the States would be worthwhile. The following suggestions are made:

(a) A measure of uniformity in rates of taxation of this industry by the State Governments with no further increase in the rates should be made for, say, 10 years.

(b) To start with, the Centre could bring down the capital cost of vehicles by giving reliefs from input taxation. The loss in revenue will be more than made up by the increased contribution arising on account of the augmentation of urban bus fleets and expansion of operations by small operators.

(Para 9.51)

19.106 There is need for rationalisation and a measure of uniformity in respect of the plethora of taxes and fees levied by State Governments and local bodies.

(Para 9.52)

19.107 The question whether the time has come when with the improved foreign exchange position, price of petroleum products should be lowered, merits consideration.

(Para 9.54)

19.108 If in Government's view the time has not yet come for a general revision of the price structure of petroleum products, a fresh look may be given at least to the prices and taxes applying to individual products for giving appropriate relief.

(Para 9.57)

19.109 If the prices of different steel sections are themselves determined with due regard to having such elements of discrimination as are socially and economically justifiable, there is no particular reason why the tax structure should also seek to introduce differentials. A uniform ad valorem rate could well be introduced to determine the revenue element and thereafter the Joint Plant Committee could have the freedom to adjust prices of individual sections. In any case, the rate should be ad valorem rather than specific so that there is an automatic and proportionate change in the tax whenever prices change.

(Para 9.63)

19.110 A lower incidence is recommended in respect of alloy and special steels as they are generally used for industrial purposes.

(Para 9.64)

19.111 Too high a level of customs duty for alloy and special steel and stainless steel not only encourages high cost producers but reduces possibilities of additional employment at subsequent stages.

(Para 9.65)

19.112 There is a good case for reducing levies on copper, zinc and lead as these have a wide variety of applications in the production of electrical goods and accessories and capital goods. The conversion of the import duty on copper into a specific one because its international price is subject to violent fluctuations is recommended. Imports of metalic concentrates should be made duty free so that spelters in the country do not have their costs raised. The exemption for copper concentrates can be continued and similar exemption provided for zinc concentrates. Alternatively, the whole question of pricing and differential taxation could be looked at de novo.

(Para 9.66)

19.113 Commercial grade aluminium has multifarious uses but the present duty on non-levy aluminium which is high affects industries significantly. Though the present juncture is not opportune for reducing the duty due to the scarcity of this metal, there is a good case in the long run for considerable lowering of the existing duty and extension of duty free clearances in deserving cases.

(Para 9.71)

19.114 There should be a shift in taxation in respect of plastics from the raw material stage to the final product stages as well as a net reduction in the average incidence on final products. This would enable greater progression being achieved with reference to the finished products consumed by the well to do and those that largely cater to the lower income groups.

(Para 9.76)

19.115 It would be desirable instead of having different rates for different plastic resins to have a uniform rate of customs duty for all of them.

(Para 9.77)

19.116 A reduction in the burden of tax on raw materials as is likely to result from the rationalisation exercise could be partly made up by increases in rates at the final products stage and partly be compensated by increase in output.

(Para 9.78)

19.117 On balance, the taxation of inputs of agriculture has to be determined on a wide variety of considerations including the possibilities of raising the requisite revenue from alternative sources.

(Para 9.79)

19.118 Although machinery as a class has till recently been free from excise levies at the final stage, the fairly heavy taxes on its main raw materials, namely, metals, has meant that capital goods generally have been contributing to revenues on a not insignificant scale.

(Para 9.80, 9.81)

19.119 Having regard to all considerations, a levy of the order of 5 per cent (including the taxation of inputs) on capital goods could in the interests of revenue be retained. A separate tariff classification should be created and machinery items should be taken out of tariff item No.68. Government may wish to re-examine whether there are adequate economic reasons for retaining higher levies on some of the industrial items of machinery, particularly those needed for improving irrigation.

(Para 9.82)

19.120 The view that machinery items which are not indigenously produced at present, should be allowed to be imported without any duty, cannot be accepted.

(Para 9.83)

19.121 The present rate of duty of about 28.5 per cent on cement is very high, as it raises the cost of all capital projects. The rates of duty on cement should be gradually reduced as more supplies become available.

(Para 9.87)

19.122 In any restructuring, rates on many final products, even those which are consumed by lower income groups, may have to move up.

(Para 9.88)

The Revenue Angle

19.123 One of the reasons, which today makes the tax structure, seem in need of a major change is that while most of the existing levies had adequate justification when they were imposed, it was but rarely that there was any subsequent re-examination of these to see whether the circumstances which had warranted them, had changed and a reduction would be desirable.

(Para 10.3)

19.124 Due to the greatly widened scope for self-assessment procedures, most of the considerations that stood in the way of bringing more products under excise and led to the heavy reliance on taxation at high rates of a few product families and basic inputs, have lost much of their validity.

(Para 10.4)

19.125 Developments in the economy necessitate changes in the indirect tax structure as a whole having regard to the social and economic impact of the existing levies.

(Para 10.6)

19.126 A restructuring of consumer product rates including those new falling under tariff item No.68 and taxing them at rates of 10, 20, 30 or 40 per cent (cumulative), with exceptions - where justified on special considerations - would throw up revenue possibilities of a sufficiently large order; the yield being Rs. 20 crores per percentage point increase, even in respect of items now falling under tariff item No. 68 other than capital goods. Whilst a generalised and substantial revision of the rate in respect of items covered by tariff item No.68 has large potentialities, the appropriate course would be to fix suitable rates for identifiable groups of products covered by this tariff item.

(Para 10.7)

19.127 It should be examined whether the exemption granted to certain products, because the rates applicable to them under the appropriate tariff had been earlier considered to be too high, should be withdrawn and if this could not be taxed at the rate applicable to items covered by tariff item No.68.

(Para 10.8)

19.128 Where as a result of the reduction of duties on inputs, there is a consequent reduction in the cumulative tax burden on certain products using them, the revenue loss can be recouped by making appropriate increases in the nominal rates of duty.

(Para 10.10)

19.129 It may not be possible or even desirable to make all the changes that are considered advisable in one single Budget. The pace of change may well be spread over three years or so. The complete phased programme for bringing about the needed changes might be accepted by Government even at the first stage.

(Para 10.12)

19.130 If a reduction in excise duties stimulates production or reduction in import duties leads to higher imports and - in the case of inputs - also to increase in domestic production, the loss of revenue may well be amply compensated, because though the rate of duty would have gone down, the volume of goods to which it applies will have gone up.

(Para 10.12)

19.131 In so far as reductions in duties have to be phased, priority should be given to a reduction in customs duties over a reduction in excises because in terms of resource mobilisation, imports not only contribute to the Exchequer by the amount of duties they bear but they also help to cushion the impact of Budgetary deficits by bringing about a contraction in the money supply to the extent that the foreign exchange reserves as well as external credits are drawn upon.

(Para 10.13)

19.132 A resource mobilisation effort which is spread in an equitable way across the board is preferable to selective increases which inevitably lead to distortions. Instead of a flat percentage point increase which may tend to be regressive, the better method would be to have a surcharge at a fixed per cent of the existing rates of duty on consumer products. This method of mobilising additional revenues will obviate the need for raising the rates applicable to inputs, which should only be undertaken if it is intended to discourage the use of particular inputs because of their short-term or long-term scarcity.

(Para 10.15)

Stimulus to production and investment

19.133 Although, psychologically, a sacrifice of revenue gets more readily accepted than an outflow from the Exchequer, which subsidies entail the fact that the latter, by their very nature, attract constant attention tends to ensure that they are neither excessive nor continued even though circumstances might have changed.

(Para 11.1)

19.134 Excise duty reductions are more likely to be effective, where the prevailing level of excise duty is significant and the price elasticity of demand for the product is relatively high.

(Para 11.5)

19.135 When an investment has already been made with Government approval, and subsequently it is felt that the industry should be accorded a lower priority, it would be preferable to take steps to prevent new investment rather than to render the investment already made wholly or partly infructuous.

(Para 11.6)

19.136 It should be ensured whilst extending any concession to a sector of industry facing difficulties that the benefit accrues only to deserving units and not those suffering from the results of mismanagement.

(Para 11.8)

19.137 In considering reliefs in the indirect tax system for encouraging production, a comprehensive view has to taken of the total relief available under the fiscal system.

(Paras 11.11, 11.12)

19.138 The existing scheme for granting excise relief for higher production has resulted in benefits, which are far from uniform as between industries to which it applies and even between units in the same industry.

(Para 11.16)

19.139 If preliminary indications are any guide, the major impact of the scheme would seem to be a redistribution of the same level of production among different manufacturers in which the more efficient have been the net gainers. The scheme should be discontinued after the period of three years is over.

(Paras 11.17, 11.19, 11.20)

19.140 In its initial years, a new capital-intensive unit may be confronted with a situation in which if it has to sell its products at the prevailing market price it would suffer losses due to its higher capital costs and the time lag in reaching the optimum production level. Concessions in direct taxation may not adequately take care of this situation.

(Para 11.23)

19.141 In respect of capital intensive industries which are considered essential and which any how have to be expanded, concessions under the direct taxes do not provide an adequate answer, some concessions in regard to levies in the initial years of production both to new units and to cases of substantial expansion of old units would be justified. The concession could well be in the form of a 10 per centage point reduction in the full rate of tax on the product. It should become applicable from the date of and commencement of commercial production and remain valid for a limited number of years not exceeding five. The total amount of the concession should be expressed as a percentage of the investment in fixed capital. This would enable a composite view to be taken including other concessions like the investment allowance under the direct taxes, so that the total quantum is reasonable and adequate, but not excessive. A review should be made to enable making of changes that are warranted, but with adequate notice.

(Para 11.26)

19.142 In respect of the sugar industry, which is already subject to a dual pricing system, any incentive to compensate for the higher cost of production during certain seasonal periods, should, to the extent possible, be in the form of modification of the existing pricing system rather than be at the expense of the Exchequer.

(Para 11.29)

19.143 Differential excise taxation for encouraging the production of low-priced consumer durables, especially for those which are now out of the reach of the poor and lower middle class people, is a welcome step. A case by case examination is, however, necessary, the prime consideration being the provision of relief in cases where the price reduction could be sizeable and the product would become cheaper. The criterion to be applied should be the price or value rather than physical specifications.

(Paras 11.30, 11.31, 11.32)

19.144 In deciding upon the nature and magnitude of concessions to the particular sectors or types of production, a distinction should be made between cases where the desired objective is to stimulate a particular type of economic activity and those where it is merely to protect and ensure the survival of the existing units.

(Para 11.33)

19.145 In future, any exemptions granted should have a time limit appropriate to particular cases but not exceeding five years.

(Para 11.34)

Encouragement to small producers

19.146 Most of the Committees/Commissions which examined the case for fiscal preference, in the form of excise duty concessions, for the small scale sector vis-a-vis organised units had accepted the preference in principle.

(Para 12.12)

19.147 Though it would be advantageous to lay greater emphasis on measures other than taxation to encourage the growth of the small scale sector, purely from the revenue angle, a measure of protection to them through differential excises is as legitimate as protection through import tariff is for an industry as a whole.

(Para 12.16)

19.148 The industries having potential for growth and new avenues of employment would certainly deserve fiscal concessions, but they should be supplemented by other measures to improve quality, design and marketing facilities, so as to avoid over-dependence on fiscal benefits.

(Para 12.17)

19.149 The existing scheme of concessions, particularly in respect of the criteria which should be applied for the grant of concessions and the extent to which concessions should be given, needs to be rationalised.

(Para 12.21)

19.150 The value of production of a unit would be the most rational basis for granting concessions to smaller producers.

(Para 12.21)

19.151 There should be a total exemption from excise up to a certain value of production; any excess over it should be taxed at a concessional rate subject to an upper limit, beyond which the excess should be liable to normal rates. Where the production reaches a sufficiently high level in a given year, the producers should be subject to the normal rate of taxation from the following financial year.

(Para 12.22)

19.152 First clearances up to Rs. 2.5 lakhs (an assessee is required to maintain accounts under Section 44AA of the Income-tax Act if his turnover exceeds this figure) could be exempted fully for all units eligible for concessional treatment in an industry. Concessions based upon investment criterion are not favoured. Clearances falling in the slab Rs. 2.5 lakhs-Rs. 10 lakhs may be charged at a concessional rate of duty which may be lower by 3 percentage points as compared to the effective rate of duty payable by the organised units.

(Paras 12.29 to 12.31)

19.153 With the introduction of the concessions based on the value of production, it would be imperative to withdraw the existing concessions based on various criteria. A case by case review could also be made to ascertain whether there is any tendency to abuse the exemption or whether such concession causes serious distortions in the pattern of production between different sectors of the industry for appropriate follow-up action.

(Para 12.33)

19.154 A review of the working of the scheme of simplified procedure of assessment for small producers at present applicable to 46 industries shows that there has not been as much response to the scheme as was anticipated.

(Para 12.41)

19.155 If appropriate modifications are made in the scheme, there is no reason why it should not find greater acceptance by the small scale sector.

(a) The approach could be to give concessions to small producers on the value slab basis as indicated earlier.

(b) There should be a concerted attempt to educate the small manufacturers about the attractive features of the scheme. For this purpose, notifications and other provisions should be simplified and a version of it couched in understandable non-technical language should be made available.

(c) It should be considered whether the three-year block period for which the duty liability is fixed could not be shortened. If the period is reduced, Government should also consider whether there is any need for the duty liability fixed for the shortened period to be revised, even if the value of production exceeds the base value by 50 per cent.

(d) To help financially weak small producers, it may be provided that the duty could be paid within 7 days of the commencement of the month as against the present requirement of payment a week before the commencement of the month.

(Para 12.42)

19.156 There is little justification to limit the benefits meant for smaller producers to a selected number of industries. It should be extended, if necessary, in phases, to all commodities with few exceptions (e.g., tobacco, petroleum products, matches and goods falling under tariff item No. 68).

(Para 12.44)

Reform of sales taxation

19.157 A decision on the final choice regarding the future role of the sales tax system, as to whether it could be made a Central subject to bring about an integrated and rationalised system of indirect taxation on domestic production and consumption extending from the manufacturing to the retail stage or whether it would be enough if the existing systems themselves are reformed so as to free them from most of their weaknesses, has necessarily to be political.

(Paras 13.8, 13.9)

19.158 The excise system, despite the considerable widening of the base in recent years, is still not, and cannot also become, universal in coverage. The sales tax, on the other hand, is much more in the nature of a general tax, covering all commodities except those where the intention is to spare the consumer. Prima facie, there is a strong case for preserving sales taxes in addition to excise duties on the ground that both play distinct roles.

(Paras 13.4, 13.7)

19.159 The levy of sales tax on inputs, without appropriate procedures for relief through drawback or refund, deflects from the distinctive role of sales tax as a levy on consumers within the State and turns it, like excise, into a tax on production. It also gives rise to and compounds the problems of cascading, distortions in relative factor prices and vertical integration. The sales tax system should, therefore, be suitably amended to ensure that the taxation of inputs does not impinge in the way that it does today on the prices of final products, regardless of whether the production and/or consumption of the product is within the State or outside.

(Paras 13.13, 13.14)

19.160 It has been a mistake to raise the rate of tax on inter-State sales to its present level of 4 per cent as it goes against its basic rationale, namely, that while some revenue should accrue to the exporting State, the tax should not result in a significant burden on the importing State. Further, it has led to ways of avoiding the tax altogether. The trend, therefore, needs to be reversed.

(Para 13.19)

19.161 On a balance of all considerations, a single point sales tax at the last stage is favoured as it would eliminate cascading effects and make it easy for State Governments and State Legislatures to consider and determine the kind of burden that should be imposed on consumers of different products. The complete switch-over could be staggered over a period of years by having a double point system in the interregnum in respect of commodities where the risk of evasion is great.

(Paras 13.25, 13.28)

19.162 The limit of turnover of or above Rs. 2,50,000/- prescribed by the Income Tax Act for compulsory maintenance of accounts could be taken as a line of demarcation for purposes of compulsory registration of dealers for sales tax purposes with provision for compulsory registration without limits for manufacturers and importers. The law should also provide for voluntary registration of dealers whose turnover is less than Rs. 2.5 lakhs.

(Para 13.28)

19.163 Different rates of sales tax result in divergence in prices from State to State, even in respect of items for which maximum prices are fixed by the Government or manufacturers. A case, therefore, exists for introducing uniformity in sales tax rates in the case of such selected goods.

(Para 13.31)

19.164 The Regional Councils for sales tax should be made to play a more active role in investigating and discussing matters relating to sales tax.

(Para 13.34)

19.165 If the States do not switch over to a uniform pattern of taxation, it would obviously be difficult to bring about equality of rates. There are, however, some products of widespread consumption, produced by a relatively small number of producers, where the desired uniformity as well as savings in cost of collection and elimination of harassment can be achieved by imposition of Additional Excise duty in lieu of sales tax.

(Para 13.40)

19.166 The rate of Additional Excise duty in lieu of sales tax should move proportionately with the change in the basic duty. There should be an attitude of partnership between the Centre and the States. Whenever there is agreement about applying a uniform rate of sales tax to any product, it should be the endeavour to have a similar uniformity in rates in respect of the most important of its inputs which do not have any other significant alternative use.

(Paras 13.38, 13.42)

19.167 Keeping in view the extra territorial impact caused by CST, it should in stages be brought back to the original level of one per cent.

(Para 13.47)

19.168 While there may be a good case for lowering the rate of sales tax on some of the basic necessities of life, such as foodgrains and pulses, limitations imposed by Parliament on the levy of local sales tax in regard to internal consumption should be the minimum.

(Para 13.49)

19.169 If on national considerations it is regarded desirable to lower the imposition on any product, it would be quite legitimate, in the context of the Centre lowering the excise duty, to take recourse to the declared goods procedure in respect of them.

(Para 13.49)

19.170 The definition of "backward areas" for the purpose of sales tax concessions should be uniform and no concessions should be given to industries located outside the backward areas as nationally defined.

(Para 13.50)

19.171 Steps should be taken to implement the recommendations contained in the 61st Report of the Law Commission in regard to taxation of works contracts, hire-purchase transactions, as well as the enactment of a provision for facilitating and enforcing the recovery of any amount illegally realised as tax by a private person, whether as sales tax or any other tax.

(Para 13.51)

19.172 It would also be advantageous both to State Governments and to business and industry, if uniformity in sales tax legislation and procedures is achieved in all States either through Central legislation or by the drafting of a model law by a Central agency like the Law Commission which each State could adopt. If need be, the provisions of Article 252 could be availed of for this purpose. Alternatively, a small group of representatives from different States could be set up,who could jointly evolve the draft of such a law after agreement.

(Para 13.56)

19.173 As regards the apprehended loss of revenue pursuant to some of our suggestions, a reduction in the rate of CST need not result in a proportionate loss of CST revenue, as the subterfuge of consignment transfers presently adopted to avoid CST will not be a paying one. Further, the capacity of the importing State to have a higher sales tax on products originating outside the State would increase.

(Para 13.58)

Octroi and other taxes

19.174 Almost every Committee that examined octroi in the past found it to be undesirable and harmful.

(Para 14.3)

19.175 It is harmful and obnoxious as it interferes with the movement of trade and commerce and acts as a major source of delay and harassment. Its economic demerits are that it is a regressive duty, violates the principle of free flow of trade across local boundaries, and encourages the concentration of industries in metropolitan areas.

(Paras 14.15, 14.16)

19.176 A decision to abolish octroi should not be linked with the finding of alternate sources or avenue. It could be abolished in stages.

(Para 14.17)

19.177 Resources for the upkeep of municipal areas consequent on the abolition of octroi should be found by taxation by the local authorities or by the State Government; the burden of compensation should not be passed on to the Centre. Alternatives, like levy of a surcharge on excise duty on HSD, removal of check-posts followed by self-assessment by transport operators, levy of an entry tax are not suitable because of various undesirable consequences.

(Paras 14.18, 14.19, 14.20, 14.21, 14.22)

19.178 If commodity taxation is to be its substitute, the levy should be made by the State rather than by municipal bodies. A flat turnover tax with its rate being limited to less than 1 per cent would be a viable alternative.

(Paras 14.33, 14.34)

19.179 Each State Government could constitute a Standing Committee which could determine the basis on which the receipts from the additional taxation would get allocated to different local bodies.

(Para 14.37)

19.180 There are several arguments to support the taxation of services. However, the matter has to be proceeded with cautiously, taking into account the revenue potential and other practical problems.

(Paras 14.38, 14.41)

19.181 If it is intended to tax services, it should be through a Central legislation; the proceeds from the service tax should go to the States.

(Para 14.41)

19.182 For alternative sources of revenue, the question of increasing the ceiling of Rs.250 fixed by Article 276 of the Constitution for levy of Profession Tax could be considered after proper incidence studies.

(Para 14.42)

19.183 It would be advantageous to have studies about indirect taxes conducted by competent bodies, comprehensive enough to take into account all the resource possibilities. It would be better if the same body or agency undertook such a study for all the States.

(Para 14.44)

19.184 There is a good case for the abolition of electricity duty in view of the importance of electricity in the economic development of the country and also because it is a necessary input in almost all industries.

(Para 14.52)

19.185 If electricity duty is to be retained, its structure should be simplified to achieve at least near uniformity of treatment.

(Para 14.52)

19.186 State revenues from electricity can be increased if attention is paid to recoveries of dues, reduction of losses in transmission and rationalisation of the tariff.

(Para 14.55)

19.186 In fixing the rates of electricity duty, no considerations demanding differential treatment of different categories of consumers need be taken note of.

(Para 14.55)

19.187 The levy could be at a flat rate of 1 paisa per unit. If this is not considered progressive, it could be a flat ad valorem rate.

(Para 14.55)

19.188 The Central Government may seriously consider, in consultation with the Finance Commission, whether it would not be a good thing to provide that the income tax paid by any undertaking which is wholly State-owned should, in its totality, be given to the State Government which owns it.

(Para 14.56)

Procedural Reforms

19.189 Among the desirable features which a sound tax system should possess, operational efficiency in the matter of assessments, collection and enforcement of the various taxes is of great importance.

(Para 15.1)

19.190 What needs special emphasis is that, unlike in the case of direct taxes, delays and uncertainties about the amount of excise duty payable can cause serious hardship and entail financial losses. Further, it creates opportunities for corrupt practices.

(Para 15.2)

19.191 A time has come when statutory time limits should be fixed in the excise and customs laws in respect of the following:

(a) Approval of classification and valuation

(b) Sanction of refunds, rebates and drawbacks of excise and customs duties

(c) Finalisation of provisional assessments and assessment documents

(d) Decisions in short assessment demands. For each of the above, different time limits could be stipulated.

(Para 15.4)

19.192 Where a manufacturer does not generally sell to or through a related person, the submission and approval of the price lists prior to the removal of the goods may be altogether dispensed with. In other cases, a definite time for approval of both the classification and price lists should be fixed. The approval should not take more than 3 months. Where this is exceeded, the classification and value claimed by the assessee should be deemed to be final. Any revision in the lists should only be prospective in operation. Similar provisions should be made in regard to finalisation of assessments made on a provisional basis.

(Para 15.6)

19.193 A time limit of 3 months for the grant of refunds/rebates/drawbacks would be liberal enough. Interest should be payable in cases of delayed refunds.

(Para 15.7)

19.194 In regard to valuation, transactions between holding and subsidiary companies and companies under the same management can clearly be treated as transactions between related persons.

(Para 15.11)

19.195 Prima facie, transactions between relatives who are either lineal ascendants or descendants could be regarded as transactions between related persons, but not with other relatives, in the widest sense. There is much less reason for treating all agents and distributors as related persons. The standards followed in direct taxation should apply to indirect taxation also.

(Para 15.12)

19.196 In regard to other relatives and a distributor or sub-distributor of the assessee, the onus should be on the Excise Department to establish the kind of interest whether direct or indirect which would affect the price charged by the assessee.

(Para 15.13)

19.197 Difference between ex-factory price and the re-sale price of the dealer/distributor, may include transport, packaging, marketing and other costs. These elements should not be treated as part of the assessable value. The same approach should apply in regard to the transactions with a related person.

(Para 15.14)

19.198 Where the manufacturer establishes his average transport cost, he could be allowed to claim a deduction from the all India price while determining the assessable value.

(Para 15.15)

19.199 The cost of packaging without which the product cannot be sold even to a customer at the factory gate should be a part of the assessable value. But the cost on account of outer packaging required for transport or packaging to meet the special needs of any class of customers should not form part of the assessable value.

(Para 15.16)

19.200 The need for arriving at an early finality in matters regarding valuation is imperative and the question of amending the law should be examined urgently. In regard to pending disputes in High Courts, the Government should consider availing of the procedure prescribed by Article 139A of the Constitution, so as to get an early and final verdict.

(Para 15.17)

19.201 The time is now opportune for a total restructuring of the existing Central excise tariff schedule, so as to evolve a tariff based upon a scientific system of classification, comprehensive in scope and more precise and unambiguous.

(Para 15.20)

19.202 Adoption of BTN even for excise tariff procedures would have a number of advantages.

(Para 15.21)

19.203 Whilst it would be desirable to extend the application of BTN for excise purposes, it would be preferable to use the Indian commercial or trade identity for describing a range of products, whenever appropriate.

(Para 15.22)

19.204 No refund in respect of past clearances due to a revision in classification should be permissible to the manufacturer. The law could be amended to make the position clear. Unless forgery, fraud or collusion is involved, a change in the classification should have only prospective effect.

(Para 15.23)

19.205 The provisions relating to the taking of bonds should be streamlined and either a single bond should be devised to cover all operations or in the alternative a drastic reduction should be made in their number.

(Para 15.26)

19.206 In cases where goods are generally not sold at the factory gate or the sales are very few, the extension of warehousing facility with appropriate safeguards may be given favourable consideration.

(Para 15.29)

19.207 In excise matters also, production norms should be gradually evolved, particularly to cover industries which have a large number of producers.

(Para 15.30)

19.208 The balance of advantage lies in not imposing any pre-Budget restrictions on clearances.

(Para 15.31)

19.209 A self-contained and comprehensive Act replacing the existing Central Excise Act, with adequate provisions to deter evasion, would make excise procedure and administration smooth, efficient and objective-oriented. The views of the trade and industry should also be taken while drafting the new Bill.

(Para 15.34)

19.210 Bills of entry may be taken up for processing without waiting for the manifest and should normally be accepted if it shows evidence of classification.

(Paras 15.35, 15.36)

19.211 The period of 3 years for warehousing imported goods may block goods on the imports of which foreign exchange has been expended and may be cut short by a year or even two.

(Para 15.37)

19.212 In the interests of operational efficiency, and to ensure comparability between the Customs schedule and the Import Trade Control schedule, it is imperative that the Customs schedule is also wholly CCCN-based without any contractions or adaptations. This will also help in the matter of comparing international trade statistics. Further, the Customs administration would derive an immediate and continuing benefit from the explanatory notes and classification opinions of the Nomenclature Committee.

(Para 15.41)

19.213 It would be worth considering whether the manner of computation of drawback amount could be liberalised by suitable changes in the Customs Act, so as to obviate the precise determination of the exact quantum of duty burden on the components/ingredients of the products exported.

(Para 15.45)

19.214 As sales taxes falling on inputs enter into the cost of production of export products, the coverage of drawback might be made more comprehensive so as to authorise refund of an amount equivalent to the element of sales tax and terminal taxes.

(Para 15.46)

19.215 The present minimum qualifying amount of drawback may be raised to Rs. 25 in respect of exports by post parcels and Rs. 100 for other exports.

(Para 15.47)

19.216 For reducing the scope of litigation, Government should carefully consider whether, when the verdict goes against them, they should or should not accept it. If they find it unsatisfactory, they should further consider whether the better answer would not be to seek to amend the law so as to place the matter beyond doubt rather than to attempt to get a higher judicial authority to reverse the legal view already taken.

(Para 15.49).

19.217 For classifying a particular medicinal preparation as restricted or unrestricted, the better course would be to provide in the law itself appropriate criteria.

(Para 15.51)

19.218 If the end product in its final form does not contain alcohol, no duty should be levied under the Medicinal and Toilet Preparations Act. To set at rest doubts in this regard, it would be desirable to write the correct position in the law itself.

(Para 15.52)

19.219 Adoption of the metric system as against the present practice of determining duty in some cases at a specific rate per litre of the strength of London-proof spirit is preferred.

(Para 15.53)

Administrative framework

19.220 Whilst reforming the tax system, it is necessary simultaneously to ensure that the adminstration of the laws, while being objective, sympathetic and human in its approach, does also enable taking of expeditious decisions.

(Para 16.1)

19.221 One of the objectives of a reformed administration should be to explain each law, notification or procedure in the lanugage of the layman. A public relations approach has to be built into the tax machinery so that people of small means, particularly the small producers, are fully aware of their rights and obligation. Publications, like working schedules, tariff guides and digest of important rulings, should be regularly updated and published.

(Para 16.2)

19.222 In the context of the growing complexity of Customs and Excise administrations and with the switch-over to more account based controls under excise, there is an immediate need to reorient the training of the officers to meet the professionalised needs of administration.

(Para 16.3)

19.223 Keeping in view the phenomenal increase in the responsibilities of the Central Board of Excise and Customs, the restraint stipulated by the Central Boards of Revenue Act, 1963, limiting the number of members, should be removed.

(Para 16.6)

19.224 The Collectorates should be reorganised so that each Collectorate ordinarily should not have more than four to six divisions.

(Para 16.7)

19.225 To make the internal audit system efficacious, the audit function should be performed by an independent organisation within the control of the Central Board of Excise and Customs. Prompt follow-up action should be taken on audit objections, so as to avoid repetitive mistakes.

(Para 16.8)

19.226 It is well recognised that an adequate information system is a prerequisite for the effective administration of broad based or comprehensive taxes, such as extended excises and general sales taxes.

19.227 Steps should be taken to (a) enlarge the coverage of data collection, (b) strengthen the data collection wing and (c) strengthen the Research wing, so as to equip it for carrying out more comprehensive studies on a continuing basis. The process will be considerably facilitated through computerisation. The same improvement in the information system should also be effected in relation to the State indirect taxes.

(Para 16.9)

19.228 Early steps should be taken to eliminate the deficiencies and inadequacies in respect of test facilities.

(Para 16.16)

19.229 An independent body to hear appeals would inspire public confidence, which the decisions of executive officers, no matter how impartial they try to be, do not. Whilst delays in settling issues pertaining to indirect taxation must be avoided, there is no reason to assume that the replacement of an executive agency by a quasi-judicial one must necessarily mean the adoption of diletory procedures.

(Paras 16.18, 16.19,
16.20 & 16.21)

19.230 A two-tier appellate machinery with a Tribunal independent of the Board for hearing appeals both on facts and law from the first court of appeal should be established. All relevant procedural provisions in the Income Tax Act, can, with suitable adaptations, be incorporated into the Central Excise and Customs Acts, with the variation namely, that the procedure in vogue under the Income-Tax Act whereby an assessee/department has to move the Tribunal for drawing up a statement of the case to the High Court be dispensed with.

The members and the Chairman of the Tribunal should have appropriate status and to inspire the necessary confidence, the membership should have an equal sprinkling of professional experts and judicial officers besides departmental officers. For the present the Tribunal should have six members. The question of further strengthening the Tribunal could be taken up on an appropriate future occasion.

(Paras 16.22, 16.23 & 16.24)

19.231 Uniformity and an early final ruling on classification are of utmost importance for the healthy growth of trade and industry and for normal interplay of commercial competition. As the desired objective cannot be achieved through the normal appellate machinery, the balance of advantage, would be in a single body being vested with the necessary authority to dispose of disputes relating to classification, such decisions being made binding on all concerned including the

Appellate Tribunal. An All India Classification Tribunal should therefore be set up with the members having appropriate status and qualification.

(Paras 16.28, 16.29)

19.232 Every State should have also a uniform pattern of appellate procedures.

(Para 16.31)

Value Added Tax - Basic Features

19.233 VAT, in its comprehensive form, may be simply defined as a tax to be paid by all sellers of goods and services, other than those specifically exempted, on the basis of value added by their respective firms. By contrast, a cascading type turnover tax, which may also be comprehensive, falls on the total value at each stage.

(Para 17.4)

The difference between a retail sales tax and VAT is that while the former is collected at one stage, VAT is collected in instalments at successive stages of production and distribution.

(Para 17.5)

The main characteristics of VAT are:

(i) It is a multi-stage tax rather than a single stage one like the retail sales tax, and, in its ideal form, is to be levied on all stages of production and distribution.

(ii) It is, in principle, comprehensive unlike selective excises.

(iii) It is collected in bits at each stage of production and distribution which, when added equal a tax on the retail sale of the final product at the same rate as the VAT.

(iv) Finally, it falls on each input entering into final products once and once only.

(Para 17.18)

19.234 The essential feature of VAT is not neutrality but rather the fact that it avoids cumulative taxation of inputs.

(Para 17.19)

19.235 The chief merits of VAT are:

(i) It ensures that an input is taxed only once and hence not only is cascading avoided, but the incidence on any final product can be controlled.

(ii) It combines the advantages of being a general tax, without the disadvantages of extended input taxation.

(iii) It is free of other economic demerits of cascade type turnover or sales taxes.

(iv) It does not promote vertical integration so long as there are no exemptions to important sectors in the middle of the chain of production.

(v) It does not discriminate against products embodying a larger part of value added at the earlier stages of production.

(vi) It does not change the relative prices of inputs and give wrong signals to producers regarding factor combinations.

(vii) It does not raise costs through input taxation and since under it exports could be fully relieved of internal indirect taxation, it helps a country to maintain the relative competitiveness of its industries in the world market.

(viii) It could be made non-neutral with regard to consumers' choice between final products.

(ix) In developing countries, a mild bias could be built into the system against capital intensive methods.

(x) Economy in the use of scarce inputs could be promoted through an additional non-refundable duty.

(Para 17.20)

19.236 As against its merits, there are several features which demand a strong and efficient administrative structure as well as additional efforts on the part of tax payers. These features are:

(i) More elaborate book keeping is required of the tax payers, probably involving additional expenditure.

(ii) Where small traders are insufficiently educated, it will be too much to expect them to maintain adequate records of purchases of inputs to match against output.

(iii) There would be a large increase in the number of tax administrators, in countries where sales taxation does not exist, because of the need to bring in a multitude of retail outlets.

(iv) It is possible for a number of tax payers to collude and evade taxes, like those who sell services directly to consumers.

(Para 17.26)

19.237 Introduction of several rates complicates the administration of VAT considerably. In a developing country where large inequalities of income exist, a set of differential excise duties which would not come under the system of tax credit might be called for.

(Para 17.30)

19.238 From various points of view, the tax credit method is easier to apply, which can be enforced even with specific duties at some stages. The need to submit vouchers of tax paid also acts as a check on artificial increases in claimed deductions.

(Para 17.33)

19.239 The introduction of VAT in almost all countries was preceded by detailed public debate in chambers of commerce, industry, associations and other firms; in Parliament and educational institutions, etc.

(Para 17.68)

19.240 Due to the detailed training imparted to revenue officials and the education of assessees by Government and trade chambers etc; the introduction of VAT in several countries did neither create many problems nor did it cause much distortions.

(Para 17.70)

Long Term Reform of the Indirect Tax Structure

19.241 The excise tax system at the Central Government level forms the bulwark of the entire tax structure of indirect taxes in the country and unless it is placed on a sound footing, it would not be possible to bring about a full rationalisation of that structure.

(Para 18.3)

19.242 From the economic point of view and for easily achieving a determinate degree of progression, it is best to have a tax system which covers value added at all stages of processing and trade but which, however, does not create problems of cascading and distortions in relative factor prices.

(Para 18.5)

19.243 VAT enables a country to have an extended commodity tax system and yet avoid the familiar problems created by other general taxes like the cascade-type sales taxes and excises. It is also relatively easy under the VAT system to free exports almost completely of internal commodity taxation.

(Para 18.7)

19.244 There could be two major arguments against the introduction of a comprehensive VAT in India - one is political and the other is administrative. The political argument is the obvious one that the loss of power to levy sales taxes would seriously erode the fiscal autonomy of the State Governments and weaken the federal principle that each subordinate level of Government should have the discretion to raise more or less revenue as the people of the State concerned desire. The administrative argument is that the enforcement of VAT in relation to wholesalers and retailers is likely to create serious problems due to the need for dealing with a large number of tax-payers and the difficulties likely to be faced by a majority of the traders to cope up with the accounting requirements.

(Para 18.11)

19.245 It would not be prudent to think in terms of extending VAT to the retail and even wholesale stages in the near future. However, if the benefits of reform of the other parts of the tax system are not to be nullified, taxation at the wholesale and retail stages must be freed of the defects associated with the usual forms of sales taxation.

(Para 18.12)

19.246 Given our federal system and the administrative problems of enforcing VAT at the post-manufacturing stages, the right course of action is not to pursue the theoretically best solution, namely, one integrated system based on the VAT principle but to adopt the second best solution of VAT applied to the manufacturing stage (to begin with) combined with a reformed system of sales taxation.

(Para 18.13)

19.247 While formally VAT would be applied at the manufacturing stage in lieu of the present excise system, it would be extended to cover imports; and the essential principle of VAT, namely, freeing of inputs from taxation, would get embodied in the sales tax systems. This long term objective should be achieved through a time-bound programme.

(Para 18.14)

19.248 Under the MANVAT, there will be no indirect tax component in the price of exports. The MANVAT would not mete out any discriminatory treatment as other systems do, on account of the differences in the stages at which value is added. Relative price distortions would also be eliminated, because in effect inputs are freed from taxation. Administration should not also present insurmountable difficulties.

(Paras 18.18 to 18.21)

19.249 If the existing restrictions and checks are retained, a general application of rule 56A to all or most of the inputs would involve several problems of administration and compliance. Whilst in the interim, there should be a wider application of rule 56A, the long term solution lies in switching over to a system of MANVAT.

(Para 18.26)

19.250 MANVAT could be operated on the basis of four or five rates that would be applied to the vast majority of consumer products, as a result of the rationalisation of the duty structure on the basic raw materials and inputs.

(Para 18.28)

19.251 Under Indian conditions it would be preferable to keep a certain number of industries outside the scope of MANVAT and continue on them the present system of excises. These are industries in respect of whose final products not much cascading is involved as well as those whose products have to be taxed at special or at high rates for economic or sumptuary reasons. These will include petroleum products, tobacco and tobacco products, sugar, coffee, tea and matches.

(Para 18.29)

19.252 The introduction of MANVAT in the first instance could be confined to three or four industries which produce final products like automobiles and diesel engines where there is evidence of considerable cumulation of levies. Such a pilot project would enable tax administration to identify problem areas, test cut procedures and study the reactions of tax-payers. Studies have revealed that a VAT confined to the manufacturing level would not be beyond the capacity of tax authorities in India. In the interests of safeguarding revenue, it is necessary to establish the workability of the new system before its widespread application is contemplated.

(Para 18.31)

19.253 An erosion of the benefits enjoyed at present, may come about because under VAT, a total exemption from tax is not an unmixed blessing. Non-payment of tax at one stage would automatically break the chain of tax credit which would be denied to the consumers of the exempted producer. A practical solution would be to grant tax credit on a notional basis to manufacturers in respect of inputs bought by them from smaller producers working under a special scheme to be introduced for that purpose.

(Para 18.33)

19.254 In our country, it should not be difficult to devise special schemes for the smaller producers whose turnover is below certain value limit.

(Para 18.37)

19.255 To prevent abuses and evasion, apart from elaborate audit of accounts by trained personnel, periodic physical checking of inventories of goods on hand would be necessary under MANVAT.

(Para 18.39)

19.256 If recommendation for the adoption of MANVAT is accepted by the Government, it would be necessary to send a small team to study the operation of VAT in some countries including a few developing countries.

(Para 18.40)

19.257 Simultaneously with the introduction of MANVAT or even preparatory to it, the existing system of sales taxation would have to be reformed as indicated in Chapter 13. As regards import duties, the revenue element in course of time should be made equivalent to MANVAT on the same or similar domestic products, which would thus become a true countervailing duty; and when revenue needs permit, relief under MANVAT should be made admissible in respect of such countervailing duties.

(Para 18.41)

APPENDIX 1.

TEXT OF UNION FINANCE MINISTER'S INAUGURAL ADDRESS TO THE COMMITTEE DELIVERED ON 24.7.1976.

I am happy to welcome Governor Jha and other members to the first meeting of the Committee on Indirect Taxation. I am grateful to Shri Jha for having agreed to undertake the onerous and difficult task of acting as Chairman of this Committee in spite of the several preoccupations of his full-time office. Also, I greatly appreciate the spirit of co-operation shown by the non-official members in accepting membership of the Committee, which would undoubtedly make substantial demands on their valuable time.

2. The Government attaches great importance to the work of this Committee. It is coming into being at the most opportune moment when the nation is experiencing a new sense of awakening and the Government is keen to give new directions to the economy. I am glad that we have been able to get such representative committee as yours and members with such high qualifications and experience.

3. This is the most important Committee on taxation to be appointed after the Taxation Enquiry Commission of 1953-54 headed by Dr. John Mathai. In some ways perhaps, this Committee has even more difficult a job to perform than the Mathai Commission. While that Commission's work covered a wider range, encompassing as it did the review of the entire tax system, the present Committee's work would be more technical, requiring more sophisticated analysis. The reason is clear. The tax system is far more complicated today than it was in early fifties. When you are raising only 5 to 6 per cent of national product in taxation, the system can be simple and the burden is relatively light. When the rates are low, even some inequity could be tolerated and one can get by with a non-optimal system. Take for example, sales taxation. Experts have always disfavoured the multi-point sales tax because of its tendency to produce cascading effects, to induce vertical integration and to distort factor prices. However, the Taxation Enquiry Commission could recommend such a levy because it only envisaged a rate of quarter per cent (1/4th of one per cent). But the approach must be radically different if much higher rates are envisaged. Trouble arises if a multi-point system is retained and higher revenue is sought to be raised by periodically hiking up the rates of the multi-point tax. This is just an example to show that a tax system producing a 15% tax ratio cannot be structurally the same as that yielding a 5% tax ratio. Also, the economy which in a sense demands a higher tax ratio is likely to be more complex.

4. I think that the crux of the problem is really this, namely, how shall we adapt our tax system such that while substantially fulfilling the cannons of equity and economic efficiency, it will be capable of generating an increase not only in the absolute amount of revenues but also in the tax ratio.

5. In this connection, I would like the Committee to have in mind one important requirement. As you know, the tax ratio has risen from 10 per cent in 1960-61 to about 15 per cent in 1975-76. In my view, there is no doubt that it would have to rise to about 20 per cent by the end of the next ten years.

6. The greater part of the increase in the tax ratio has, in the past 15 years, been brought about by rate increases, introduction of new levies and discretionary extension of coverage. In future we would have to rely more and more on the built-in elasticity of the tax system. Since indirect taxes account for about 80 per cent of the total tax revenue of the Centre and the States, we need to impart a large element of elasticity to our indirect tax system. An automatic increase in coverage is also preferable to ad hoc changes from year to year.

7. There is a general feeling that the historical, uncoordinated growth of excise and sales taxation has led to a complicated maze. This general feeling is somewhat confirmed by certain preliminary studies undertaken at my instance in the Economic Division of the Ministry. We would, of course, have a much more detailed picture of the situation after the Committee has carried out an in-depth study of the system. But I may say that the main objective in setting up this Committee is to find out the ways in which the over-lapping systems of Central and State taxation could be rationalised so that we could have a buoyant and efficient system that would subserve national purposes without affecting, or at least unduly affecting, the relative financial position of the States. I think that it is clear that wide-spread taxation of inputs is not desirable, it is also clear that national objectives should not be thwarted by regional actions. At the same time, we cannot afford to forget the legitimate interests of the State Governments.

8. Of course, one of the basic causes of overlapping action by the two layers of Government is that essentially the same tax power has been given to the Centre and States under two different names with some restrictions as regards the stage of taxation. From the purely economic point of view there is not much difference between an ad valorem excise on a commodity and a sales tax on it at the same percentage. Now, if we wish to reform the present system which has grown as a result of the exercise of this overlapping power by the Centre and the States, we are likely to come up against constitutional constraints. That is why the Committee has been asked, in its terms of reference, "to suggest changes, if any required, in the Constitution and in the related taxation statutes, for the implementation of the changes suggested in the tax structure....." I do not, of course, foreclose any solution that the Committee might like to put forward. However, I think that there would be general agreement that there is a presumption in favour of a solution that minimally reduces the tax powers of the States. The Committee may wish to indicate the range of trade-off between efficiency and regional freedom; this would help the political authorities at the Central and the State levels to understand the implications and arrive at an optimum solution. More concretely, a good deal of attention of the Committee is likely to be centred on the feasibility of adopting the principle of value added taxation and the minimum constitutional changes need to make it workable. The administrative implications are also important, but if a system is particularly desirable from several other points of view - here of course the Committee will put forward its view - then administration will have to be geared up to the task sooner or later.

9. There are now the experiences, of applying the VAT, of several developed and developing countries to study and profit by. I am sure the Committee would tell us what we could learn from those experiences.

10. I come finally to import duties. Whether value added taxation is recommended or not, any reform of the taxation of internal transactions is bound to produce repercussions on import taxation. I do not know whether it can be said that the present systems of import taxation and taxation of internal transactions form a coherent whole. But we would like the Committee to tell us the best manner of dovetailing import levies with excises in terms of overall incidence and economic effects.

The Government's intention in appointing the Committee is to effect, if possible, a sharp breakaway from ad hocism and to replace it by purposeful actions to build a more enduring system which may be adequate for our purposes during the next 20 or 25 years as the taxation Enquiry Commission system was during the 'fifties and the 'sixties. The recommendations of the Committee will initiate a new stage in the evolution of our tax system. You have a difficult task to perform. For this purpose, you will, I am sure, receive the fullest co-operation from the concerned agencies of the Government and in particular from the Central Board of Excise and Customs. I wish your work all success and hope that your deliberations will ultimately leave their impress on the history of our tax system.

Thanking you,

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APPENDIX - 2

A. GENERAL QUESTIONNAIRE

1. Please indicate the type of commodities in respect of which the excise duties and sales taxes are in your opinion unduly high having regard to their impact on costs, prices, production, investment and employment.

2. In so far as the rates of excise duty on some commodities may require reduction, which are the other commodities on which the rates could be increased in order to compensate for the loss of revenue.

3. Does the taxation of inputs have in your opinion any harmful effects ? If so, what are they and which industries are most affected?

4. Would you favour the replacement of the existing system of cumulative levies by Centre, States and local bodies partially or wholly by the Value Added Tax system? If you do which of the various models that you are familiar with would you recommend?

5. There are a number of excise duty concessions to industries depending on their size, scale of production, method of production or end use of the product. Do you consider these arrangements to be satisfactory or do they create problems or lead to abuse? Have you any reforms to suggest?

6. Would you like to suggest any change in the import tariff or import control having due regard to the need for protecting indigenous industry and conserving foreign exchange, keeping in view the revenue implications?

7. Would you propose any changes in the tax structure with a view to develop exports? Have you any comments or suggestions on the working of the existing system of drawback of duties on the export of goods? Would the Value Added Tax have any definite advantage in this regard?

8. Have you any observations on the working of sales-tax and octroi levies? In particular do you have any comments on the following:

   (a) the system of concessional treatment of inputs in respect of sales taxation in force in several States;

   (b) the working of Central sales-tax in respect of inter-State trade and commerce, and

   (c) the impact of sales tax on exports.

9. Are there any major problems of a procedural nature to which you would like to draw the attention of the Committee?

B. SUPPLEMENTARY QUESTIONNAIRE ISSUED TO THE STATE GOVERNMENTS.

1. One of the issues which the Committee has to consider and on which it would welcome the views of the State Government is the merger of State Sales-tax with Union Excises. The pros and cons of such a course of action have been discussed in paras 11.3 to 11.6 of the Committee's interim report. In the light of the considerations mentioned in the report the Committee would appreciate the State Government's considered views in the matter.

2. Another issue before the Committee is the suggestion for extension of additional excise duty in lieu of sales tax /which has now been in operation for about two decades in respect of sugar, tobacco and textiles/ to more commodities. A discussion of this issue is contained in paras 11.12 to 11.14 of the interim report. The extension suggested ranges from certain selected commodities like paper, cement, petroleum products, tyres, fertilizers, etc. to all commodities. There is also a view that no objection could be taken in principle for extension of the levy to more commodities, provided the growth in revenue accruing to the State from this source keeps pace with the Excise revenue accruing to the Centre. In the light of these considerations and the observations made in the interim report the State Government may give its views on the following specific aspects:

(i) Should there be a wholesale extension of the scheme of additional excise duty to all excisable commodities?

(ii) If only a partial extension of the scheme is favoured, reasons in support of the view may be given along with a list of commodities which could be brought under the scheme. In such a contingency, what is the State Government's reaction to the suggestion made in para 11.14 of the interim report.

3. Suggestions have also been received from business interests for expansion of the list of 'goods of special importance' (i.e. declared goods). It is said that a wider coverage under 'declared goods' would ensure uniformity in the taxation of goods of vital importance to the country as a whole as well as raw materials and intermediaries. What is the State Government's view on this suggestion: If only partial expansion of the list is favoured, please indicate the commodities which could be brought under the list of declared goods.

4. On the assumption that the continuance of the sales tax system in its present form is favoured, an issue raised with the Committee is that a State should by and large tax only its own residents. To this end, a switch over to a single point sales-tax leviable at the last point has been suggested. Keeping in view the administrative aspects in dealing with a large number of retail registered dealers, the registration will be compulsory only where the turnover exceeds 2 lakhs, for mitigating the hardship that might arise by denial of the benefits of registration like tax free purchases in the cases of small dealers, the latter could be given an option to get themselves registered, even if their turnover is below the prescribed limit. The advantages of such a system, it is argued, would be, elimination of the harmful effects of inter-State sales taxation and distortions in prices caused by the present system. The situation of the two taxes falling on the same 'tax base' would also be avoided. The Committee is keen to know the State Government's views in the matter. If any serious administrative difficulties are anticipated, its extent may be indicated.

If the State Government has other alternatives to suggest a brief resume thereof may be given.

5. There is also the suggestion for adoption of a model sales tax law by all States on which the Committee has commented in paras 11.9 of the interim report. It is argued that such a step will ensure uniformity in the matter of registration, assessment the tax treatment of purchases of raw materials, exemptions etc. Would the State Government kindly indicate its views and suggest concrete proposals in this regard?

6. A section of the trade feels that Central Sales Tax (CST) interferes with inter-State trade and commerce and hence it should be abolished. The Committee has dealt with this issue in para 11.21 of the interim report. In the light of the observations made therein the Committee would appreciate the State Government's views in the matter.

7. The levy of octroi has been criticised by all the Committees who have gone into the issue of the retention of the levy. A discussion on the issue is contained in paras 11.33 to 11.40 of the interim report. What are the views of the State Government on the preliminary recommendations made in the report? Is it imperative that an alternative source of revenue should be first identified before octroi is abolished? If so, which one of the alternative sources suggested below would the State Government prefer and for what reasons? —

(i) suitable subvention from Central Government for a limited period during which the States could explore the possibility of raising resources from other taxes or by any other methods.

(ii) levy of a surcharge - the tax will be collected from the respective metropolitan cities, local areas and panchayats,

(iii) a general turnover tax at a low rate,

(iv) the collection of Entry tax from the consignee on the lines of the system tried by the Government of Madhya Pradesh. If the State Government has any other alternative suggestion to make the same may be indicated.

8. One of the terms of reference of the Committee is "to examine the feasibility of adopting some form of value Added Tax in the field of indirect taxation where appropriate and, if found feasible, to suggest the appropriate stage to which it should be extended having regard to Indian conditions, i.e. whether the stage of coverage should be manufacturers, wholesalers or retailers". Some of the options which come up for consideration in this regard are —

(i) extension of the system of Value Added Tax to the entire field of indirect taxation, including sales tax and turnover taxes.

(ii) extension of the system of value added tax to Central Excise and Sales Tax separately. /This would envisage two systems, one in substitution of Central indirect levies, and one in lieu of State indirect levies/.

(iii) replacement of Central Excises by a value added tax system and switch over to last point sales taxation with reduction in the taxes on inputs. What are the State Governments' views on each one of these options? If either of the options at (ii) and (iii) is preferred, how should the transactions arising on account of an intermediary wholesaler acting between two manufacturers be treated?

9. Lastly, the question arises of safeguarding and expanding the revenues of the States. Paras 11.28 to 11.31 of the Committee's interim report deal with this issue. While the Committee would welcome the State Governments considered views on the suggestions contained in the abovementioned paragraphs of the interim report the State Government's views in particular are invited on the following issues:—

(i) mobilisation of resources through higher taxation of agricultural incomes, property, professions and trades and services in general;

(ii) the need for a comprehensive study of the resources position of the State and if so, whether such study should be undertaken by a body to be constituted by the State Government as has been done by some in the past or whether there should be a Central agency, who should be entrusted with this task.

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APPENDIX — 3A

LIST OF ORGANISATIONS/INDIVIDUALS WHO SENT MEMORANDA IN RESPONSE TO THE QUESTIONNAIRE/PRESS NOTE OF INDIRECT TAXATION ENQUIRY COMMITTEE.

* * *

I. PUBLIC

(A) Chambers of Commerce

1. Andhra Chamber of Commerce, Madras.
2. Bengal Chamber of Commerce and Industry, Calcutta.
3. Bengal National Chamber of Commerce & Industry, Calcutta.
4. Bharat Chamber of Commerce, Calcutta.
5. Bombay Chamber of Commerce & Industry, Bombay.
6. Central Gujarat Chamber of Commerce & Industry, Baroda.
7. Coal Field Chamber of Commerce, Raniganj.
8. Federation of Indian Chambers of Commerce & Industry, New Delhi.
9. Federation of Karnatake Chamber of Commerce & Industry, Bangalore.
10. Gondal Chamber of Commerce & Industry, Gondal.
11. Gujarat Chamber of Commerce & Industry, Ahmedabad.
12. Hindustan Chamber of Commerce, Bombay.
13. Hindustan Chamber of Commerce, Madras.
14. Indian Chamber of Commerce, Calcutta.
15. Karimganj Chamber of Commerce & Industry, Karimganj.
16. Maharashtra Chamber of Commerce, Bombay.
17. Merchants Chamber of Commerce, Calcutta.
18. Merchant Chamber of Uttar Pradesh, Kanpur.

19. North Bihar Chamber of Commerce & Industry, Muzafarpur.

20. North Eastern Bihar Chamber of Commerce & Industry, Kathihar.

21. Punjab Haryana and Delhi Chamber of Commerce, Delhi.

22. Punjab Merchants Chambers, Delhi.

23. Rajkot Chamber of Commerce, Rajkot.

24. Raniganj Chamber of Commerce, Raniganj.

25. Steel Chamber, Bombay.

26. The Associated Chambers of Commerce & Industry of India, New Delhi.

27. The Belgaum Chamber of Commerce & Industry, Balgaum.

28. The Cochin Chamber of Commerce & Industry, Cochin.

29. The Indian Merchant's Chamber, Bombay.

30. The Madras Chamber of Commerce & Industry, Madras.

31. The Maharashtra Chamber of Commerce & Industries, Poona.

32. The Nawanager Chamber of Commerce & Industry, Jamnagar.

33. The Sivakasi Chamber of Match Industries, Sivakasi.

34, The South India Chamber of Commerce & Industry, Madras.

35. The Southern Gujarat Chamber of Commerce & Industry, Surat.

36. The Southern India Chamber of Commerce & Industry, Madras.

37. Trichurapalli District Chamber of Commerce and Indistry.

38. United Chamber of Trade Association, Delhi.

39. Upper India Chamber of Commerce, Kanpur.

(B) Organisations other than Chambers

40. All India Air Conditioning & Refrigeration Association, New Delhi.

41. All India Automobile & Ancillary Industries Association, Bombay.

42. All India Bidi Industry Federation, Bombay.

43. All India Crimpers Association, Bombay.

44. All India Distillers' Association, New Delhi.

45. All India Electric Motor Manufacturers' Association, Bombay.

46. All India Federation of Photographic-trade Association, Delhi.

47. All India Food Preserves Association, New Delhi.

48. All India Glass Manufacturers' Association of India, Bombay.

49. All India Glass Manufacturers' Federation, New Delhi.

50. All India Importers' Association, Bombay.

51. All India Instrument manufacturers & dealers Association, Bombay.

52. All India Manufacturers' Association, Bombay.

53. All India Manufacturers' Organisation, Bombay.

54. All India Organisation of Chemists & Druggists, Madras.

55. All India Pottery Manufacturers' Association, Calcutta.

56. All India Radio & Electronics Association, Delhi.

57. All India Rubber Industries Association, Bombay.

58. All India Small Scale Paint & Allied Industries Association, Bombay.

59. All India Small Paper Board Mills Association, Bombay.

60. All India Small Paper Manufacturers Association, Bombay.

61. All India Small Paper Mills Association, Bombay.

62. All India Steel Rerollers' Association, New Delhi.

63. All India Trade Union Congress, New Delhi.

64. Andhra Pradesh Paper Merchants' Association, Secunderabad.

65. Andhra Pradesh Plastic Manufacturers' Association, Hyderabad.

66. Association of Indian Automobile Manufacturers', Bombay.

67. Association of Indian Engineering Industry, New Delhi.

68. Association of Man-Made Fibre Industry, Bombay.

69. Association of Merchants & Manufacturers' of Textiles Stores and Machinery (India), Bombay.

70. Association of Polyester Staple Fibre Manufacturers, Bombay.

71. Association of Synthetic Fibre Industry, Bombay.

72. Automotive Tyre Manufacturers' Association (P) Ltd., New Delhi.

73. Bengal Chemists & Druggists Association, Calcutta.

74. Bengal Sugar Merchant's Association, Calcutta.

75. Beopar Mandal, Chandigarh.

76. Bombay Piece-Goods Merchants Mahajan (Association), Bombay.

77. Cabin Holders Union, Satna.

78. Calcutta Traders Association, Calcutta.

79. Cable and Conductor Manufacturers' Association of India, New Delhi.

80. Cigarette Manufacturers' Association, Bombay/New Delhi.

81. Cine Laboratories Association, Bombay.

82. Cloth Manufacturers' Association of India, Bombay.

83. Coimbatore Cotton Association, Coimbatore.

84. Coimbatore Pioneers Fertilizers Association, Coimbatore.

85. Delhi Hand-Made Matches Dealers' Association, Delhi.

86. Delhi Hindustan Merchantile Association, Delhi.

87. Delhi Iron and Hardware Merchants' Association, New Delhi.

88. Delhi Factory Owners' Federation, Delhi.

89. Delhi Motor Traders' Association, Delhi.

90. Delhi Pen Dealers Association, Delhi.

91. District Small Scale Industries Association, Mysore.

92. Dyes & Chemicals Dealers Association, Amritsar.

93. Elayirampannai Matches & Fireworks Manufacturers Association, Elayirampannai.

94. Elecoma Electric Lamp & Component Manufacturers' Association of India, Bangalore.

95. Estate Industralists Association, Industrial Estate, Endarpal.

96. Fan Markers Association of India, Calcutta.

97. Federation of All India Automobile Spare Parts Dealers Association, Delhi.

98. Federation of Association of Small Industries of India, New Delhi.

99. Federation of Association of Small Industries of India, Bombay.

100. Federation of Biscuit Manufacturers of India, Delhi.

101. Federation of Co-operative Sugar Factories, Delhi.

102. Federation of Corrugated Box Manufacturers of India , Bombay.

103. Federation of Hotel & Restaurant Association of India, New Delhi.

104. Federation of Indian Art Silk Weaving Industry, Bombay.

105. Federation of Indian Export Organisation, New Delhi.

106. Federation of Indian Plywood & Panel Industry, New Delhi.

107. Federation of Small & Medium Industries, West Bengal, Calcutta.

108. Fertilizer Association of India Ltd., New Delhi.

109. Filter Manufacturers Association, Delhi.

110. Fruit and Vegetable Processing Industries Association.

111. Glass Manufacturers' Association of Bihar, Ramnagar, Bihar.

112. Gujarat State Rifle Association, Ahmedabad.

113. Gujarat Waterproof Packing Materials Association, Ahmedabad.

114. Gunny Trades Association, Calcutta.

115. Indian Ceramic Society, Ghaziabad.

116. Indian Chemical Merchants & Manufacturers' Association, Calcutta

117. Indian Confectionary Manufacturers' Association, New Delhi.

118. Indian Cotton Mills Federation, Bombay.

119. Indian Dry Battery Manufacturers' Association, New Delhi.

120. Indian Electrical Manufacturers' Association, Bombay.

121. Indian Jute Mills Association, Calcutta.

122. Indian Non-ferrous Metals Manufacturers Association, Calcutta.

123. Indian Paper Mills Association, Calcutta.

124. Indian Paint Assoication, Calcutta.

125. Indian Soap & Toiletries Makers' Association, Bombay,

126. Indian Sugar Mills Association, New Delhi.

127. Indian Tea Association, Calcutta.

128. Indian Woollen Mills Federation, Bombay.

129. Indian Zinc Oxide Ma[illegible]rs Association, Calcutta.

130. Industrial Fasteners Association of Madhya Pradesh, Indore.

131. Industries Association, Jagadhri.

132. Iron & Steel Scrap Association of India, Bombay.

133. Jaffara Tobacco Curers' Association, Kodirvari.

134. Jodhpur Industries Association, Industrial Estate, Jodhpur.

135. Joint Advisory Committee on Road Transport Association, Madras.

136. Kaira District Co-operative Milk Producers' Society Ltd., Madras.

137. Khurja Pottery Manufacturers Association, Khurja.

138. Ludhiana Nut Bold Manufacturers Association, Ludhiana.

139. Madurai District Small Industries Association, Madurai.

140. Madurai Industrial Estate Manufacturers Association, Madurai.

141. Maharashtra State Rifles Association, Bombay.

142. Man-Made Fibre Spinners' Association, Bombay.

143. M.I.T. Alumini Association of India, Bombay.

144. Moradabad Industrial Factories Association, Moradabad.

145. National Alliance of Young Entrepreneurs, New Delhi.

146. National Federation of Co-operative Sugar Factories, New Delhi.

147. Non Schedule Small Industries Association, Calcutta.

148. Northern India Small Scale Straw Board Mills Association, Delhi.

149. Pesticides Association of India, New Delhi.

150. Pesticides Formulators' Association of India, (Small scale industry), Bombay.

151. Power Cables & Conductors Manufacturers' Association, New Delhi.

152. Powerloom Vastra Utpadak Sangh, Pilkhowa.

153. Rajkot Trust Bearing Manufacturers' Association, New Delhi.

154. Rashtriya Mill Mazdoor Sangh, Bombay.

155. Roller Flour Millers' Federation of India, Delhi.

156. Small Scale Non-ferrous Industries Association, Calcutta.

157. Small Scale Zinc Oxide Manufacturers' Association, of India, Bombay.

158. Southern India Mill Owners' Association, Coimbatore.

159. Southern Region Industrialists' Society, Madurai.

160. Sports Goods Manufacturers & Exporters Association, New Jullundur.

161. State Industrialists' Association, Calcutta.

162. Tamil Nadu Kuzhivai Pukayilai Viyabarigal, Sangam Palladev.

163. Tamil Nadu Shooters' Association, Madras.

164. Tamil Nadu Small Scale Industries Association, Madras.

165. Tamil Nadu Steel Rerollers' Council, Madras.

166. Tea Packeteers Association of India, Calcutta.

167. The All India Federation of Photographic Trades Association, Bombay.

168. The All India Metallised Products Manufacturers' Association, Vadhu.

169. The All India Metallised Products Manufacturers' Association, Bombay.

170. The All India Gear & Allied Products Manufacturers' Association, Bombay.

171. The Association of Small Tool, Manufacturers' Madras.

172. The Cashew Export Promotion Council, Cochin.

173. The Clothing Manufacturers' Association, Bombay.

174. The Consultative Committee of Plantation Association of India, Delhi.

175. The Dyes and Chemical Merchants' Association, Calcutta.

176. The Dyestuffs Manufacturers' Association of India. Bombay.

177. The Federation of Gujarat Mills & Industries, Baroda.

178. The Handloom Export Promotion Council, Madras.

179. The Indian Drug Manufacturers' Association, Bombay.

180. The Indian Paint Association, Bombay.

181. The Krishna District Steel Furniture Manufacturers Association, Vijayawada.

182. The Madras Dyes & Chemicals Merchants' Association, Madras.

183. The Madras Motor Parts Dealers' Association (Regd.) Madras.

184. The Madurai District Small Industries Match Manufacturers' Association, Tirumangulam.

185. The Processed Foods Export Promotion Council, New Delhi.

186. The Salem Sago Manufacturers' Association, Salem.

187. The Sankarankovil Cottage Match Manufacturers' Association, Sankaranayinarkovil.

188. The Sattur Small Match Manufacturers' Association, Sattur.

189. The Small Scale Industrial Association, Batala.

190. The South Indian Swadesh Match Manufacturers' Association, Sattur.

191. The Surat Art Silk Cloth Manufacturers' Association, Surat.

192. The Textile Processors' Association-India, Bombay.

193. The Vanaspati Manufacturers' Association of India, Bombay.

194. The Vanaspati Manufacturers' Association of India, Delhi.

195. Tinplate Fabricators' Association, Calcutta.

196. Tinplate Fabricators (Bombay) Association, Bombay.

197. Tirunapalli District Cottage Match Manufacturers' Association.

198. United Trades Union Congress, Calcutta.

199. Vidarbha Industries Association, Nagpur.

200. Winding Wires Manufacturers' Association of India, Bombay.

(C) Individual Manufacturers and Trading Agencies.

201. Abbott Laboratories (India) Pvt. Ltd., Bombay.

202. Abhay Industries, Sonepat.

203. AEICORP Private Limited, Calcutta.

204. Agarwal Iron & Steels, Jodhpur.

205. Ahuja Radios, Delhi.

206. Allied Instruments Pvt. Ltd., Bombay.

207. Atic Industries Limited, Atul.

208. B.R. Herman & Mohatta (India) Pvt. Ltd., Bombay.

209. Basic Chemical, Pharmaceuticals and Cosmetics Export Promotion Council, Bombay.

210. Bharat Carpets Limited, New Delhi.

211. Bharat Heavy Electricals Limited, New Delhi.

212. Bihar State Agro-Industries Development Corporation Ltd., Patna.

213. Bombay Metal Exchange Ltd., Bombay.

214. Chemical & Fibres of India Limited, Bombay.

215. Coimbatore Power Fertilizer Ltd., Coimbatore.

216. Cominco Binani Zinc Ltd., Cochin.

217. Coventry Metals Rajasthan Private Ltd., Jaipur.

218. Crystal Company, New Delhi.

219. Danfoss (India) Ltd., New Delhi.

220. Dara Industrial Syndicate, Madras.

221. Datta Fertiliser Company, Godhra.

222. Delhi State Cloth Retailers Board, Delhi.

223. Estrella Batteries Ltd., Bombay.

224. Fertilizer Corporation of India, New Delhi.

225. Gangadharan Match Works, Elayirampannai.

226. Geep flash light Industries Ltd., Allahabad.

227. Godrej & Boyre Manufacturing Co. Pvt. Ltd., Bombay.

228. Guindy Machine Tools Pvt. Ltd., Madras.

229. Heemanshu Trades, Bombay.

230. Hindustan Aluminium Corporation Ltd., Bombay.

231. Hindustan Copper Ltd., Calcutta.

232. Hindustan Lever Limited, New Delhi.

233. Hindustan Organic Chemicals, Bombay.

234. Hindustan Petroleum Corpn. Ltd., Bombay.

235. Hindustan Teleprinters Ltd.,

236. Honesty Traders, Madras.

237. India Hard Metals Ltd., Calcutta.

238. Indian Oil Corpn. Ltd., New Delhi.

239. Indian Organic Chemicals Ltd., Madras.

240. Indian Petrochemicals Corpn. Ltd., Baroda.

241. Indian Rubber Manufacturers' Ltd., Calcutta.

242. Indo Asari Glass Company Ltd., Calcutta.

243. Indo-Burma Petroleum Company Ltd.,

244. Jayshree Tea & Industries Ltd., New Delhi.

245. Jindal Aluminium Ltd., Bangalore.

246. J.K. Synthetic Ltd., New Delhi.

247. K.B. Foams Pvt. Ltd., Bangalore.

248. K.M.S. Rubber Industries, Madurai.

249. Kamal Match Works, Sivakasi.

250. Khodiyar Pottery Works Ltd., Sihor.

251. Madras Refineries Ltd., Madras.

252. M.P. Chitale & Co., Bombay.

253. Marine Product Exports Development Authority Cochin.

254. Matallurgical and Engineering Consultant India Ltd., Delhi.

255. Minerals and Metals Trading Corpn., Delhi.

256. Modi Spinning & Weaving Mills Co. Ltd., Modinagar.

257. Multi Metals Ltd., Kota.

258. National Dairy Development Board, Anand.

259. Oberoi Hotels (India) Pvt. Ltd., Delhi.

260. Paharpur Cooling Towers Pvt. Ltd., Calcutta.

261. Parle (Exports) Pvt. Ltd., Bombay.

262. Polychem Ltd., Bombay.

263. Prabhat Colour Co., Kanpur.

264. Pulp Pape and Allied Industries, Kanpur.

265. R. Basu & Company, Calcutta.

266. R.K. Desai & Co., Calcutta.

267. Ravi Match Co., Sivakasi.

268. Sanyukta Sachiv, Bihar Bharashthachar Samiti, Patna.

269. Sikand & Co., New Delhi.

270. Small Industries Service Institute, Indore.

271. Soft Beverages Ltd., Vilangadi.

272. Sri Rang Vanshy Singh & Co., Kanpur.

273. Standing Conference of Public Enterprise, New Delhi.

274. State Trading Corporation, New Delhi.

275. Steel Rolling Mills, Mandi Gobind Nagar, Patiala.

276. The Coronation Match Works, Sivakasi.

277. The Gramophone Co. of India Ltd., Calcutta.

278. The Indian Ceramic Society, Ghaziabad.

279. The Institute of Chartered Accountants of India, New Delhi.

280. The Marine Products Export Development Authority, Cochin.

281. The Metal Box Company of India Ltd., Calcutta.

282. The Metal Powder Company Ltd., Tirunangalam.

283. The South India Flour Mills Pvt. Ltd., Madras.

284. Tulsi Synthetics, Bombay.

285. Union Carbide India Ltd., New Delhi.

286. Wal Chand Group of Industries, Bombay.

(D) Individuals

287. Dr. Bhabatosh Datta, Former Professor and Head of the Deptt. of Economics, Presidency College, Calcutta.

288. Dr. K.N. Reddy, Deptt. of Economics, M.S. University, Baroda.

289. Dr. M. Adiseshiah, Vice Chancellor, Madras University, Madras.

290. Dr. N. Jha, Pro-Vice Chancellor, Bhagalpur University, Bhagalpur.

291. Dr. P.B. Mathur, Assistant Director, Central Electrochemical Research Institute, Karaikudi.

292. Dr. P.K. Bhargava, Reader Economics, BHU, Varanasi.

293. Shri B.M. Birla, Calcutta.

294. Shri Dewan Chand Dhanpat Rai Bhatia, Patiala.

295. Shri G. Muruganathaswamy, President, Cotton Association, Coimbatore.

296. Shri G.P. Goyal, Consultant (Paper), Kanpur.

297. Shri Kantilal, Patel Street, Bombay.

298. Shri K.N. Sivasubramanian, F.3, Nava Geeta Co-op. Housing Society Ltd., Bombay.

299. Shri M. Varadarajan, Managing Director, IDL Chemical Ltd., Hyderabad.

300. Shri N.C. Sutaria, Flat No.5, 'Nishat' Little Gibbs Rd. Malabar Hills, Bombay.

301. Shri N.A. Palkhivala, Bombay.

302. Shri Pragoda Coteriah, General Secretary, All India Handloom Weavers' Association of India, Madras.

303. Shri R.A. Jalan, 119 B, C.R. Avenue, Calcutta.

304. Shri R.G. Savaiya, Narsari Chambers, Fort, Bombay.

305. Shri Raja Ram Khatel, President Tax Bar, Jhansi.

306. Shri Satish Kumar Modi, Modi Nagar.

307. Shri Shyama Prasad Mukhopadhyay, 97, Garfa Main Road, Calcutta.

308. Shri T. Rajan, 6-1-101/19 Padmaraonagar, Secunderabad.

II DEPARTMENTAL

309. Shri A. J. F. D' Souza, Director of Internal Audit, Directorate of Inspection, New Delhi.

310. Shri A.K. Bhowmik, Collector of Central Excise and Customs, West Bengal, Calcutta.

311. Shri A.K. Mitra, Deputy Director, Regional Training Institute, Calcutta.

312. Shri A. L. Nanda, Deputy Collector, Central Excise, Allahabad.

313. Shri A. L. Vohra, Asstt. Collector, Central Excise, Baroda.

314. Shri A. T. Pal, Assistant Collector, Central Excise, Calcutta.

315. Shri Anant Ram, Assistant Collector, Central Excise, Jullundur.

316. Shri B. C. Chakraborty, Asstt. Collector, Central Excise, Calcutta.

317. Shri B. C. Goswami, Assistant Collector, Customs and Central Excise, Dhubri, Assam.

318. Shri B. N. Das, Assistant Collector of Central Excise, Rourkela.

319. Shri B. L. Ganjapure, Assistant Collector, Central Excise, Nagpur.

320. Shri B. V. Krishna Rao, Inspector of Central Excise, Visakapatnam.

321. Shri C. K. Desai, Deputy Collector, Central Excise, Ahmedabad.

322. Shri C.K. Gopala Krishan, Collector of Customs & Central Excise Cochin.

323. Shri Darshan Singh, Assistant Collector, Central Excise, Chandigarh.

324. Shri D. Chatterjee, Assistant Collector, Central Excise, Calcutta.

325. Shri D.K. Sarkar, Deputy Director, Directorate of Training Customs & Central Excise, New Delhi.

326. Shri D.N. Mehta, Collector of Central Excise & Customs, Ahmedabad.

327. Shri D.P. Dubey, Assistant Collector, Central Excise, Raipur.

328. Shri Devindra Singh, Assistant Collector of Customs and Central Excise, Patiala.

329. Shri E.R. Srikantia, Collector, Central Excise, Bombay.

330. Shri G.J. Kewalramami, Superintendent (Tech.) Divisional Office, Bhopal.

331. Shri G.L. Choukse, Superintendent (Tech.), Central Excise Division, Indore.

332. Shri H.M. Kadri, Assistant Collector, Central Excise, Anand.

333. Shri H.N. Raina, Collector Central Excise, Allahabad.

334. Shri .H.N. Sahu, Collector Central Excise, Patna.

335. Shri H.R. Syiem, Collector Central Excise, Baroda.

336. Shri H.S. Verma, Assistant Collector Central Excise, Jabalpur.

337. Shri H. Vumkhawthang, Collector Central Excise, Orissa.

338. Shri I. J. Rao, Collector Central Excise, Madras.

339. Shri J.A. Patel, Assistant Collector Central Excise, Ahmedabad.

340. Shri J. M. Verma, Collector Central Excise, Pune.

341. Shri K. Bharali, Superintendent, Customs & Central Excise, Tezpur.

342. Shri K. C. Chakravarthy, Assistant Collector Customs & Central Excise, Agartala.

343. Shri K. K. Dwivedi, Collector Customs & Central Excise, Chandigarh.

344. Shri K. M. Goswami, Assistant Collector Customs and Central Excise, Gauhati.

345. Shri K. M. Tiwari, Assistant Collector, Central Excise, Rampur.

346. Shri K. N. Patnaik, Assistant Collector Central Excise & Customs, Orissa .

347. Shri Keshav Prasad, Deputy Chief Chemist Central Revenue Control Laboratory, Delhi.

348. Shri K. P. Singh, Assistant Collector Central Excise, Moradabad.

349. Shri K. Rai, Assistant Collector (I. O.) Customs & Central Excise, Allahabad.

350. Shri K. S. Dilipsinhji, Collector of Central Excise, Kanpur.

351. Shri K. S. Saha, Collector Customs & Central Excise, Shillong.

352. Shri Koshy Chandy, Assistant Collector (Training) Madras.

353. Shri L. C. Malik, Chemical Examiner Central Excise, Baroda.

354. Shri M. Chakravarty, Assistant Collector, Customs and Central Excise, Silchar.

355. Shri M. G. Chitnis, Dy. Director Regional Training Institute, Bombay.

356. Shri M. L. Badhwar, Collector Central Excise & Customs, Delhi.

357. Shri M. R. Ramachandran, Member Central Board of Excise & Customs, New Delhi.

358. Shri M. R. Sachdeva, Assistant Collector Central Excise, Ratlam

359. Shri M. S. Subramanyam, Collector Central Excise, Madurai.

360. Shri M. V. S. Apparao, Inspector Central Excise & Customs, Visakhapatnam.

361. Shri N. Chaturvedi, Assistant Collector Central Excise, Varanasi.

362. Shri N. G. Patil, Assistant Collector, Central Excise, Baroda.

363. Shri N. Ramanathan, Assistant Collector Central Training Institute, New Delhi.

364. Shri N. S. Mehta, Assistant Collector Central Excise, Amravati.

365. Shri Om Parkash, Assistant Collector Central Excise, Rohtak.

366. Shri Onkar Nath, Asstt. Collector Central Excise, Ujjain.

367. Shri P. B. Ghosh, Dy. Collector Central Excise, Ahmedabad.

368. Shri P. M. Varkkey, Dy. Director, DICCE, SRU, Madras.

369. Shri P. L. Ganguli, Superintendent, Law Branch, Collectorate of Central Excise, Calcutta.

370. Shri P. R. Bajaj, Assistant Collector Central Excise, New Delhi.

371. Shri P. R. Biswas, Collector Central Excise, Calcutta.

372. Shri P. Roy, Collector Central Excise, Jaipur.

373. Shri R. N. Desai, Assistant Collector Central Excise, Surat.

374. Shri R. N. Shukla, Collector Central Excise, Bangalore.

375. Shri R. N. Verma, Assistant Collector Central Excise, Sagar.

376. Shri R. P. Das Assistant Collector Customs & Central Excise, Tezpur.

377. Shri R. P. Mathur, Assistant Collector Central Excise, Allahabad.

378. Shri Sethi, Dy. Collector Central Excise, Jaipur.

379. Shri S. Banerjee, Asstt. Collector Central Excise, Nagpur.

380. Shri S. D. Khare, Assistant Collector, Central Excise, Lucknow.

381. Shri S. D. Mohile, Dy. Collector Central Excise, Bombay.

382. Shri S. K. Srivastava, Collector Central Excise, Hyderabad.

383. Shri S. K. L. Malhi, Dy. Collector Central Excise, Faridabad.

384. Shri S. L. Sethi, Assistant Collector, Central Excise, Directorate of Training, New Delhi.

385. Shri S. M. Banerjee, Asstt. Collector Central Excise, Calcutta.

386. Shri S. N. Roy Chowdhury, Asstt. Collector Central Excise, Calcutta.

387. Shri T. C. Mukherjee, Asstt. Collector Central Excise, Calcutta.

388. Smt. V. Rajamanickam, Dy. Director of Training, Madras.

389. Shri Z. Tochhawng. Asstt. Collector Customs & Central Excise, Dibrugarh.

390. All India Federation of Central Excise Executive Officers, Allahabad.

391. Assistant Collector of Central Excise Division II, Ahmedabad.

392. Assistant Collector of Central Excise, Cuttack.

393. Assistant Collector Central Excise, Jammagar.

394. Assistant Collector of Central Excise, Nadiad.

395. Assistant Collector Central Excise, New Delhi New Delhi (MOD - I)

396. Assistant Collector Central Excise, New Delhi (MOD - II)

397. Assistant Collector Central Excise, New Delhi (MOD - III)

398. Assistant Collector Central Excise, Rohtak.

399. Assistant Collector Central Excise, Srinagar.

400. Assistant Collector of Customs & Central Excise, Bhuj.

401. Assistant Collector Customs & Central Excise, Sambalpur.

APPENDIX - 3B

CENTRAL MINISTRIES/STATE GOVERNMENTS WHO RESPONDED TO COMMUNICATIONS OF THE COMMITTEE

PART 1

List of Central Ministries/Governors of State who sent specific replies to special communications addressed by the Chairman, Indirect Taxation Enquiry Committee.

I Central Ministries

1. Ministry of Agriculture & Irrigation.
2. Ministry of Commerce.
3. Ministry of Defence.
4. Ministry of Energy.
5. Ministry of Information & Broadcasting.
6. Ministry of Railways.
7. Ministry of Steel and Mines.
8. Ministry of Tourism & Civil Aviation.

II. Governors.

Shri L.P. Singh, Governor of Assam.

III. Chief Ministers.

1. Shri Kailash Joshi, Chief Minister, Madhya Pradesh.
2. Shri N.D. Tiwari, Chief Minister, Uttar Pradesh.
3. Shri R.K. Dorendra Singh, Chief Minister, Manipur,
4. Shri S.S. Ray, Chief Minister, West Bengal.

PART - 2

List of State Governments/Union Territory Administrations who sent replies to the supplementary Questionnaire eliciting views on important issues touching State taxes including those discussed in the interim report of the Committee.

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1. Government of Assam.
2. Government of Andhra Pradesh.
3. Government of Bihar
4. Government of Gujarat
5. Government of Himachal Pradesh.
6. Government of Kerala
7. Government of Madhya Pradesh.
8. Government of Maharashtra
9. Government of Manipur.
10. Government of Meghalaya
11. Government of Nagaland
12. Government of Pondicherry
13. Government of Rajasthan
14. Government of Sikkim
15. Government of Tripura
16. Government of Tamil Nadu
17. Government of West Bengal.
18. Dadra and Nagar Haveli Administration
19. Delhi Administration.

APPENDIX - 4

LIST OF WITNESSES EXAMINED BY INDIRECT TAXATION ENQUIRY COMMITTEE

DATE	PLACE	S. NO.	WITNESS EXAMINED
18.8.1976	New Delhi	1.	Shri S. S. Marathe, Chairman, Bureau of Industrial Costs and Prices.
		2.	Brig. B.J. Shahanay, Secretary (Technical Development) & Director General (Technical Development).
		3.	Shri Mantosh Sondhi, Secretary, Heavy Industry, Government of India.
16.9.1976	Srinagar	4.	Kashmir Chamber of Commerce.
17.9.1976	Srinagar	5.	Shri Girdharilal Dogra, Former Finance Minister, J&K.
		6.	Dr. S. S. Kahlon, Professor, Punjab Agricultural University.
		7.	Punjab, Haryana & Delhi Chamber of Commerce.
18.9.1976	Srinagar	8.	Shri Devi Das Thakur, Finance Minister and senior officials of the J & K Government.
8.11.1976	New Delhi	9.	Association of Indian Engineering Industry.
		10.	Delhi Factory Owners' Federation.
9.11.1976	New Delhi	11.	All India Airconditioning and Refrigeration Association.
11.11.1976	Bombay	12.	Bombay Chamber of Commerce and Industry.
		13.	Indian Merchants Chamber.
		14.	Association of Synthetic Fibre Industry.

DATE	PLACE	S. NO.	WITNESS EXAMINED
11. 11. 1976 (Cont'd)	Bombay	15.	Indian Woollen Mills Federation.
		16.	Silk & Artsilk Mills Association.
		17.	Federation of Indian Artsilk Weaving Industry.
		18.	Shri S. B. Chavan, Chief Minister, Maharashtra Government, Ministers and their Advisers.
		19.	Textile Processors Association.
		20.	Shri R. P. Kapoor, Textile Commissioner, and officials of the office of the Textile Commissioner.
13. 11. 1976		21.	Indian Cotton Mills Federation.
		22.	The Mill-owners Association, Bombay.
		23.	Association of Man-made Fibre Industry.
		24.	Polyester Staple Fibre Manufacturers.
2. 12. 1976	Madras	25.	Southern India Sugar Mills Association.
		26.	Consultative Committee of the City Chamber of Commerce, Madras.
		27.	Shri R. Venkataraman, Former Minister, Government of Tamil Nadu
		28.	Dr. Malcolm Adiseshiah, Vice Chancellor, Madras University.

DATE	PLACE	S. NO.	WITNESS EXAMINED
2. 12. 1976 (Cont'd)	Madras	29.	Southern India Millowners' Association.
		30.	Shri P.K. Dave, Adviser to Government of Tamil Nadu.
		31.	Shri R.V. Subramaniam, Adviser to the Governor of Tamil Nadu.
		32.	Shri S. Cunan, Finance Secretary, Government of Tamil Nadu.
4. 12. 1976	Trivandrum	33.	Dr. R.S. Gulhati,
		34.	Shri K.V. Nambiar, Chief Economic Division, State Planning Board, Kerala.
		35.	Cochin Chamber of Commerce.
		36.	Malabar Chamber of Commerce.
		37.	Ernakulam Chamber of Commerce.
6.1.1977	New Delhi.	38.	Federation of Indian Chambers of Commerce & Industry.
27.1.1977	Calcutta	39.	Indian Chamber of Commerce, Calcutta.
		40.	Bharat Chamber of Commerce, Calcutta.
		41.	Merchants Chamber of Commerce, Calcutta.
		42.	Indian Paper Mills Association.
		43.	All India Small Paper Mills Association.
		44.	Federation of Associations of Small Industries of India.

DATE	PLACE	S. NO.	WITNESS EXAMINED
27. 1. 1977 (Cont'd)	Calcutta	45.	Federation of Small & Medium Industries Association, Calcutta.
		46.	Dr. Babatosh Dutta, former Professor and Head of the Department of Economics, Presidency College, Calcutta.
28. 1. 1977	Calcutta	47.	Calcutta Jute Fabrics Shippers Association.
		48.	Indian Jute Mills Association.
		49.	Bengal Chamber of Commerce and Industry.
29. 1. 1977	Calcutta	50.	Indian Electrical Manufacturers' Association.
		51.	Association of Engineering Industries (East Region).
		52.	Shri S. S. Ray, Chief Minister, Government of West Bengal and other Advisers.
26. 2. 1977	New Delhi	53.	Shri S. S. Puri, Secretary, Department of Textiles, Government of India.
		54.	Shri R. P. Kapoor, Textile Commissioner.
		55.	Shri S. G. Bose Mullick, Secretary, Ministry of Commerce, Government of India.
28. 2. 1977	New Delhi	56.	Shri M. Fazal, Secretary, Ministry of Industrial Development, Government of India.
		57.	Dr. A. K. Ghosh, Additional Secretary, Ministry of Industrial Development, Government of India.

DATE	PLACE	S. NO.	WITNESS EXAMINED
28. 2. 1977 (Cont d)	New Delhi	58.	Shri L. C. Puri, Development Commissioner, Small Scale Industries.
		59.	All India Manufacturers' Organisation.
1. 3. 1977	New Delhi	60.	The Associated Chambers of Commerce & Industry.
2. 3. 1977	New Delhi	61.	Cigarette Manufacturers' Association.
18. 8. 1977	New Delhi	62.	Bhartiya Mazdoor Sangh.
		63.	Centre for Indian Trade Unions.
11. 8. 1977	New Delhi	64.	Shri M. L. Badhwar, Collector of Central Excise, Delhi.
		65.	Shri A. K. Bhowmick, Collector of Central Excise, West Bengal.
		66.	Shri J. Datta, Collector of Customs, Bombay.
		67.	Shri K. S. Dilipsinhji, Collector of Central Excise, Kanpur.
		68.	Shri K. K. Dwivedi, Collector of Central Excise, Chandigarh.
		69.	Shri S. V. Iyar, Collector of Customs, Calcutta.
		70.	Shri E. R. Srikantia, Collector of Central Excise, Bombay.

DATE	PLACE	S. NO.	WITNESS EXAMINED
11.8.1977 (Cont'd)	New Delhi	71.	Shri S.K. Srivastava, Collector of Central Excise, Hyderabad
		72.	Shri M.S. Subramanyam, Collector of Central Excise, Madurai.
		73.	Shri M.G. Vaidya, Collector of Customs, Madras.
		74.	Shri J.M. Verma, Collector of Central Excise, Pune.
		75.	Shri A.J.F. D'Souza, Director of Audit.
		76.	Shri Daya Sagar, Director of O & M.
		77.	Shri M.V.N. Rao, Director of Training.
		78.	Shri M.G. Abrol, Chairman, Central Board of Excise & Customs
		79.	Shri S. Venkatesan, Member, Central Board of Excise & Customs.
		80.	Shri G.S. Sawhney, Member, Central Board of Excise and Customs.
		81.	Shri B.B. Gujral, Member, Central Board of Excise and Customs.
12.8.1977	New Delhi	82.	Shri P.J. Fernandez, Secretary, Finance, Government of India.

DATE	PLACE	S. NO.	WITNESS EXAMINED
12.8.1977 (Contd.)	New Delhi	83.	Shri G. Ramachandran, Secretary, Expenditure, Government of India.
		84.	Dr. Manmohan Singh, Secretary, Economic Affairs, Government of India.
		85.	Dr. Ajit Mazoomdar, Secretary, Planning Commission.
		86.	Shri Jasjit Singh, Special Secretary, Department of Revenue, Government of India.
		87.	Shri M.A. Rangaswamy, Additional Secretary and Gold Control Administrator, Department of Revenue, Government of India.
		88.	Shri A.K. Bandyopadhyaya, Joint Secretary, Department of Revenue, Government of India.
		89.	Shri D.N. Lal, Joint Secretary, Department of Revenue, Government of India.

APPENDIX 5

BUOYANCY AND ELASTICITY OF IMPORTANT INDIRECT TAXES

I. INTRODUCTION

1. This study* analyses the major trends and composition of some of the important indirect taxes levied by the Centre and State Governments, namely, Union excise import duties, sales tax, taxes on motor vehicles and on passengers and goods and entertainment tax, and attempts to measure their responsiveness to changes in national income. The period covered in respect of Central taxes is generally from 1963-64 to 1974-75, though for particular computations, a shorter period has had to be chosen. Similarly, for State indirect taxes the period covered generally is 1960-61 to 1974-75 though for particular taxes, slightly different periods have been chosen.

2. The growth of taxes is generally judged in relation to increases in national income as absolute increases in the yield of various taxes may not by themselves have much significance. One way of getting a measure of the relative growth of tax revenue or of the yield of a given tax is to calculate the percentage change in revenue that has taken place for an one per cent change in income. If this figure comes out to be equal to one, it would mean that the yield of the tax or taxes concerned has increased proportionately with income.

3. Most taxes are based on, or in some ways related to, income wealth, expenditure or capital transactions. These bases of taxes tend to increase with the growth of national income. Hence, taxes also may be expected to grow automatically with an increase in national income. Great interest attaches to the question of how responsive particular taxes are to changes in real or money national income. To answer this question, one must consider the automatic change in the tax yield that taxes place as a result of the growth of income. This automatic change is usually different from the actual change in the tax yield which is also influenced by any discretionary tax measures introduced by the Government during the reference period. The percentage automatic change in the tax yield divided by the percentage change in national income is defined as the 'elasticity' of the tax**. This is distinguished from the 'buoyancy' of the tax, which is computed by dividing the percentage change in the actual revenue collection by the percentage change in income. While the elasticity co-efficient of a tax gives us an idea of the inherent responsiveness of that tax to the growth or decline in income, the buoyancy co-efficient simply indicates how the actual growth of revenue compares with the growth in income. In fact, since actual collections are influenced by discretionary tax (rate or base) changes introduced by the Government, such collections may bear no systematic relationship to national income in a period in which such actions have been significant. It may be even conceptually illegitimate to try to correlate actual revenue yield with national income. However, buoyancy co-efficients are often used in practice because it is not always possible to work out the hypothetical, automatic growth in revenue that would have taken place in the absence of discretionary changes. Also, in several cases, the bucyancy estimate may give us an idea of the extent to which the Government has relied on particular sources of revenue or has succeeded in bringing about increase in tax revenues, over a given period.

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*This study was undertaken by the National Institute of Public Finance and Policy, New Delhi.

**Sometimes, the term 'built-in elasticity' is used to emphasise the fact that only the automatic change in the yield is being taken into account.

4. As Governments frequently effect changes in the legal rates and bases of taxes, actual revenue series do not generally reflect accurately the automatic growth of revenue. Therefore, for the purpose of calculating the built-in elasticity of a given tax, or of the tax system as a whole, it is invariably necessary to work out a hypothetical revenue series that would reflect the revenue growth that would have taken place in the absence of discretionary changes. The details of the methodology of constructing such "cleaned" revenue series is discussed in Annexures II and III. Broadly, two methods are employed, depending on the availability of data. The first called the proportional adjustment method consists in taking the Government's estimate of the revenue effect of a discretionary action in the year in which the action was taken and estimating the amounts of revenue in subsequent years attributable to that action on the assumption that the original revenue effect of the change grew proportionately with the yield of the tax itself. The estimated amounts are then added (or subtracted) from the actual revenue series to obtain the "cleaned" series. The second method, called the constant rate-base method, applies the rates prevailing in the year chosen as the base year to the taxable bases in different years. The latter method could easily be applied in the case of Union excises, if only information on the taxable base, namely, value or quantity of clearance in respect of different excisable commodities could be obtained. Unfortunately, information on quantity cleared is not always given according to the rate categories of different commodities; and in respect of commodities subject to ad valorem duties, the value of clearance is not always available. We have, therefore, been led to resort to the proportional adjustment method in many cases, even though, as is explained in Annexure II, this method is subject to several limitations.

5. We attempt in the sections below to trace the trends in the automatic as well as the actual growth in revenue from the important indirect taxes. In the case of excise and import duties, the trends in the duties on major groups of commodities and in the total yield are shown and discussed separately. Following general practice, the assumption of a constant elasticity during the period under reference is made and a double-log (regression) equation is fitted to the revenue series to derive the values of elasticity co-efficients. Elasticities are computed not only with reference to national income, but also with reference to estimated bases.

II. UNION EXCISE DUTIES

A. Trends

6. The share of Union excise in the total tax revenue of the Central Government rose from 16.8 per cent in 1950-51 to 51.2 per cent in 1975-76. In former year it constituted only 0.7 per cent of national income; this percentage rapidly increased to 3.1 in 1960-61, 5.1 in 1970-71 and 6.1 in 1975-76 (Table 1). It is interesting to note that the percentage declined during the years 1972-73 and 1973-74 when there was a sizeable price inflation and the national income at current prices recorded an increase of 24 per cent. During the same two years excise tax revenue rose only by 12 per cent, indicating that they were by and large price in-elastic. We shall examine this characteristic of the excise system in greater detail at a later stage.

7. Over the period 1963-64 to 1975-76 the total revenue from excises increased at the rate of 15 per cent per annum. The rates of growth of revenue from the subgroups, however, varied widely, ranging from 35 per cent in the case of non-ferrous metals down to 2.5 per cent in the case

of vegetable oils and fats. Revenue from petroleum products and textiles grew more or loss at the average rate. It is found that the shares of chemicals and non-ferrous metals increased significantly whereas those of vegetable oil, tobacco and iron and steel products fell. The shares of other groups did not change significantly by the end of the period even though there were fluctuations in the intervening years.

8. As of 1975-76, the largest revenue earning group consisted of petroleum products, accounting for nearly 27 per cent of the total. Next in order of importance came textiles (12.7 per cent), other manufactured goods (11.32 per cent), tobacco (8 per cent), chemicals (7.5 per cent) and food and beverages (7.1 per cent).

9. We may now consider the trends in excise duty collections from the major groups of commodities.

(a) Food and beverages:

The major items in this group are tea, coffee, package tea, sugar, khandsari and confectionaries. Of the total excise duties collected, this group accounted for roughly 8 per cent over the reference period. In 1963-64 and 1975-76 the excise duty collected from food and beverages were Rs. 170 crore and Rs. 271 crore respectively. In 1965-66 about the whole of the excise duties collected from this group could be attributed to specific types of duty. In 1974-75, only about 17 per cent of the duties collected could be attributed to specific rates of duty, the rest being ad valorem.

(b) Tobacco:

The items in this group are cigarettes, biris, smoking mixtures, unmanufactured tobacco, and manufactured tobacco. The major revenue earning item in this group is cigarettes, which have had ad valorem rates of duty since 1965-66. The ad valorem rates of duty have increased from 125 per cent in 1965 to 300 per cent in 1974-75. The duty collected from this group has increased from close to Rs. 100 crore in 1965-66 to Rs. 200 crore in 1970-71 and to Rs. 300 crore in 1975-76. However, as stated earlier, the share of this group in the total Union excise duty collected has fallen from about 11 per cent in 1965-66 to 8 per cent in 1975-76. All the items other than cigarettes in this group are subject to specific rates of duty, which, from 1970-71 onwards, have been accounting for about one quarter of all excise duties collected from tobacco.

(c) Petroleum products :

This is the single most important group from the point of view of revenue collection. The important items in this group are motor spirit, refined diesel oil and vaporising oil, kerosene oil, furnace oil and blended or compounded lubricating oils and greases. The duties collected have monotonically increased from Rs. 201 crore in 1963-64 to Rs. 1030 crore in 1975-76. Excise duties on items in this group have been almost completely of the specific type, but were revised upward from time to time. The share of this group in total Union excise duties which was about 30 per cent in 1965-66, went up to 34 per cent in 1970-71 but dropped to 27 per cent in 1975-76.

(d) Vegetable oils and fats

The two items in this group are vegetable products and vegetable non-essential oils. This has been a relatively unimportant group from the point of view of revenue collection. On top of it, over the last ten to twelve years tax concessions have been repeatedly awarded to commodities in this group (more on this later). The share of this group in the total excise duty collected kept consistently going down from 0.95 per cent in 1965-66 to 0.84 per cent in 1970-71 and to 0.56 per cent in 1975-76. More than 90 per cent of the tax collected from this group is of the ad valorem type. Another striking feature is that the tax collected from this group in absolute amount has been fluctuating as shown in the table below :

Excise Duty Collected from Vegetable Oils and Fats

Year	Revenue (In crores of Rs)
1963-64	16
1965-66	9
1970-71	15
1971-72	14
1972-73	16
1975-76	22

Source: Statistical Year Book, Central Excise and Customs.

It is interesting to note that the revenue collected in 1963-64 was surpassed only in 1972-73, i.e., nine years later.

(e) Chemicals :

The major commodities in this group are fertilizers, plastic materials and synthetic resins, patent and proprietary medicines, soap, synthetic and organic dye-stuffs, organic surface active agents, calcium carbide and bleaching powder. Between 1963-64 and 1975-76, there was a more than eleven fold increase in revenue from Rs. 26 crore to Rs. 288 crore, and the increase was monotonic. In 1965-66, about 70 per cent of the revenue collected from this group was from ad valorem rates of duty. By 1974-75 almost all the items in this group were subject to ad valorem rates of duty. The share of chemicals in the total excise duty collected has gone up from 3.5 per cent in 1965-66 to 7.5 per cent in 1975-76 i.e., its importance in total excise duties collected has more than doubled over these years.

(f) Metals :

i. Iron and steel : The major items in this group are iron and steel products, metal containers, crude iron, tin plates, wire ropes and iron and steel ingots. The excise duty collected has moved from Rs. 45 crore in 1963-64 to Rs. 157 crore in 1975-76. In 1965-66, almost all of the taxes collected from items in this group were in the nature of specific taxes; however, by 1974-75 the amount of tax attributable to specific taxes was only a little more than a half, the rest being accounted for by ad valorem taxes. The share of this group in the total excise duty collected has gone down from about 9 per cent in 1965-66 to 4 per cent in 1974-75. The reason for this is to be found in the fact that the clearance of some of the major items in this group has stagnated over the years as shown in the table overleaf.

Clearance Data of Certain Major Commodities
(in the group of iron and steel)

(thousand metric tonnes)

	1968-69	1969-70	1970-71	1971-72	1972-73	1973-74
Semi finished steel including blooms, billets, slabs bars, tin bars, etc.	1787	1929	1858	1971	2288	1848
Plates and sheets	1084	994	1011	967	1223	793
Pipes and tubes	181	181	200	179	200	142

Source : Statistical Year Book
Central Excise and
Customs

(f) ii. Metals other than iron and steel

The major items in this group are aluminium, copper and copper alloys, zinc and lead unwrought, This group has shown a remarkable increase in excise duty collected. The revenue collected has increased from Rs. 2 crore in 1963-64 to Rs. 83 crore in 1975-76, a more than forty fold increase over twelve years. The fraction of taxes collected attributable to ad valorem rates of duty increased from one quarter to three quarters between 1965-66 and 1974-75. Over the same period the share of this group in the total excise duty collected moved from a little less than 1 per cent to more than 2 per cent.

(g) Manufactured Goods

i. Textiles : The major items in this group are cotton fabrics, cotton yarn, rayon and synthetic fibres and yarn, artificial silk fabrics, woollen fabrics, woollen yarn, wool tops, jute twist yarn, ready made garments and linoleum. More than 90 per cent of the taxes collected from this group were until recently due to specific rates of duty. The revenue collected moved up from about Rs. 100 crore in 1963-64 to Rs. 486 crore in 1975-76. After petroleum products, this group has been one of the major revenue earners. Over the past ten years, revenues from textiles have accounted for around 12-13 per cent of the total excise collected.

ii. Other manufactured goods : From the point of view of revenue, the place of this group is next to that of textiles. This group accounts for about 11-12 per cent of the total excise duties collected. This group has a large list of excisable items, the major revenue earning items being tyres and tubes, cement, paper, matches, glass and glassware, rubber products, chinaware and porcelain, asbestos cement products, footwear, plywood and steel furniture. In 1965-66 about 12 per cent of revenue collected from this group was due to taxes of the ad valorem type. In 1965-66, this proportion went up to roughly 67 per cent. The tax revenue collected from this source in 1975-76 was Rs. 432 crore, which showed a more than four-fold increase over the figure in 1963-64.

(h) Machinery and transport equipment :

Among the large number of items in this group are motor vehicles, motor vehicle parts and accessories, electric batteries and parts thereof, electric wires and cables, electric motors, motor starters, wireless receiving sets, refrigerating and air conditioning appliances and machinery. The revenue collected from this group has increased from Rs. 34 crore in 1963-64 to Rs. 218 crore in 1975-76. Whereas in 1965-66, only about 45 per cent of the revenue collected from this group was from ad valorem duties, by 1974-75 the entire group had only ad valorem rates of duty. Over a ten-year period from 1965-66 to 1975-76, the share of this group's revenue in the total moved up from 4.7 per cent to 5.7 per cent.

The trends of the total revenue from Union excise duties and of the yield from each of the major groups of excisable commodities are visually presented in Diagrams Nos. 1 and 2 (which are appended to the study).

B. Buoyancy and Elasticity of Union Excises :

10. In the preceding section, the time trends in excise duty collections and major changes in the composition of excise duties were indicated. We shall now consider the responsiveness of excises to the growth in national income. Before we estimate elasticities for the period chosen, namely 1963-64 - 1974-75, it may be useful to review briefly the results of earlier studies in this field.

(a) A review of some earlier studies :

11. One of the earliest contributions in this area is that of Sahota (1961). He made estimates of the buoyancy and elasticity of all the major taxes in India for the period 1948-49 to 1956-57. The built-in elasticity of Union excise duties with reference to national expenditure at market prices

was estimated by him to be 1.61, and its buoyancy for the period 1948-49 to 1957-58 to be 3.97. As will be seen presently, these estimates are substantially higher than the "corresponding" estimates we have made for the period 1963-64 to 1974-75. The commodities subject to excise during the period covered by Sahota's study were much narrower in range than now so that one could say that Sahota was dealing with a qualitatively different system. Besides, Sahota was dealing with a relatively short period of 8-9 years and the measure of statistical significance of his results was rather low (the R^2 value that Sahota obtains for the equation for the elasticity of Union excise duties is o.7). For obtaining the hypothetical series to represent the automatic growth in revenue, Sahota made use of a method identical to the proportional adjustment method that we have employed*.

12. Using data for the period 1960-61 to 1969-70 (10 observations) Lakdawala and Nambiar (1972) calculated the buoyancy and elasticity coefficients of Union excise duties to be equal to 1.32 and 0.61, respectively. For the same period they estimated the buoyancy of the tax system as a whole to be 1.19 and the elasticity to be 0.63. These authors used the constant rate-base method to arrive at the hypothetical series. They did, however, sound a note of caution that since there had been a large number of tax changes in the period 1960-70, and as the money equivalents of all these changes were difficult to ascertain accurately, the estimates might contain a significant margin of error.

13. Whereas both Sahota (1961) and Lakdawala and Nambiar (1972) were concerned with aggregate union excise duties, Dwivedi has recently attempted a commodity-wise estimate of the buoyancy of excises in his two papers (1976 a) and (1976 b). The two papers, however, present identical results except for some minor variations**. The period covered varies from one commodity to another, but generally at least a ten year time period is chosen. The author has divided the commodities covered into four categories, namely, (a) essential consumer goods (b) non-essential consumer goods (c) consumer cum commercial goods and (d) intermediate goods. Variations in excise tax yield are sought to be explained by variations in rate, base (physical) and price. Thus, what Dwivedi obtains are partial elasticity coefficients.

14. Dwivedi's methodology requires the kind of data that are simply not available. He attempts to measure the response of excise revenue to changes in rates, bases and prices of individual commodities***, In most cases, the specific rates of duty (during the reference period) were different for different varieties of particular commodities****. Also ad valorem rates often differed as between differently priced varieties. Therefore, it is almost impossible to translate legal rate changes into changes in average effective rate for the group concerned. Dwivedi makes use of the weighted average rate for the group. Such an expedient will give valid results only if the weights do not change

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* See Chelliah, R.J. and Sheetal Chand (1974). "A Note on Techniques of Adjusting the Tax Revenue Series for Discretionary Changes", IMF Working Paper (Mimeo) for a demonstration that the two methods yield identical results.

**For example the rate and base elasticities of vegetable products (edible oil) work out respectively to 0.28 and 0.22 in (1976 a) and 0,30 and 0.40 in (1976 b).

***For these goods that are subject to specific rates of duty, only the rate and the base are considered to be the explanatory variables.

**** Cigars and Cigarettes have been classified by Dwivedi under goods subject to specific duties (p. 246, 1976 a). This classification is erroneous because since 1965-66 cigarettes have been subjected to ad valorem rates of duty.

during the period. Besides, it is difficult even to get information on a proper cut of weights, because neither yield figures nor physical base figures are given in the available statistics according to the given rate categories. In the case of commodities subject to ad valorem duties, Dwivedi has used the price index of the brand assigned the highest weightage whenever indices of all brands were not available. The devices used by him are based on heroic assumptions which we would hesitate to make.

15 The results obtained by Dwivedi generally seem quite implausible. For example, he obtains negative rate and base elasticities in the case of matches, namely - 0.07 and - 0.73, respectively. He argues that the low rate and base elasticities of excise revenue from essential goods may be explained in terms of switchover to inferior substitutes and in terms of evasion. It is difficult to accept that when the price elasticity of demand for matches is low, the rate elasticity could be negative. Nor is it clear how evasion could be used as an explanation when the recorded taxable base of matches has been rising. Again, Dwivedi obtains partial price elasticities of - 3.1 and - 3.3 for revenue from electric bulbs and electric fans, respectively, while the yield of relatively more non-essential goods (with probably higher price elasticities of demand) such as air conditioning machinery and cosmetics are shown to possess price elasticities of 4.94 and 2.40 respectively. Finally, Dwivedi's study derives another conclusion and the higher the degree of essentiality of a commodity the lower will be the partial rate elasticity of the excise revenue from it. This result also seems implausible because it is precisely the items that are essential whose yield would be expected to have a high rate elasticity. The chief problem with Dwivedi's study is that he has employed a single equation framework to explain the percentage change in tax revenue in terms of percentage changes in the rate, base and price of the excisable commodity. This is bound to yield erroneous results because the explanatory variables are highly interdependent, thereby giving rise to the problem of multicollinearity.

(b) Estimates of buoyancy and elasticity of revenue from Union excise duties :

16. The buoyancy and elasticity of revenue from Union excise duties with respect to net national product at current prices (hereinafter referred to as national income) were calculated for an 11-year period, from 1963-64 to 1974-75, and they work out to 1.30 and 0.75, respectively*. The estimate of elasticity we obtained shows that the excise tax system was quite unresponsive to increases in national income at current prices. However, we have to sound a note of caution here. The methodology we have adopted for adjusting actual revenue collections for discretionary tax changes would give fairly accurate results only if the effects of those discretionary changes had been accurately estimated by Government, if, as is quite possible, the estimates of additional taxation were on the high side, the automatic growth in revenue would be correspondingly under-estimated. This might be one cause for our obtaining a fairly low value of elasticity. Again, the increase in the rate of a given tax could lower the automatic growth in revenue from other taxes. In any case, since there were several discretionary changes during the reference period yielding substantial amounts of revenue, the elasticity coefficient could not have been anywhere near the buoyancy co-efficient and was in all probability below one. We could safely conclude that all in all Union excise duties have proved to be inelastic to changes

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* The R^2 values of the buoyancy and elasticity regression equations were 0.975 and 0.962, respectively, indicating a fairly good fit. The elasticity of excises excluding petroleum products was also estimated and it turned out to be 0.61.

in national income. As will be seen, this conclusion is corroborated by an examination of the elasticity of major groups of excisable commodities. It is not in fact surprising that the elasticity of Union excise duties should have turned out to be low, because, taking the period as a whole, more than 60 per cent of the total revenue from excise duties was derived from taxes of the specific type.

17. Arithmetically, the income elasticity of a tax is the product of the elasticity of that tax to its base and the elasticity of its base to national income*.

In practice because of inevitable errors in estimation, the product of the estimates of these two component elasticities would only approximate the estimate of income elasticity, (the closer the fit of the equation, the closer will be the approximation). It follows that high or low elasticity of a tax could be explained by looking at tax to base and base to income elasticities. We could then see whether it is the tax structure, i.e., the structure of rate, that is inherently regressive with respect to the base or whether it is the base that has proved to be sluggish. Unfortunately, it was not possible for us to obtain data on the basis of excise duties for the whole period covered by our study. The Statistical Year Book, brought out by the Central Board of Excise and Customs, gives only figures of quantities cleared. Again, quantities of different varieties of a given commodity subject to different rates of tax are often clubbed together. Even when such was not the case, it was not possible to obtain the relevant price data so as to work out the value of clearances at ex-factory prices. Because of non-availability of data, we were unable to work out tax to base or base to income elasticities for the entire period.

18. However, we were able to obtain from the Directorate of Statistics and Intelligence, Central Board of Excise and Customs, information on the value of clearances of different excisable commodities from 1970-71 to 1975-76. The number of observations being limited, the regression method could not be used to derive elasticities. Therefore, we used a crude method, namely, computing the compound rates of growth of taxes, bases and income, and then estimating the elasticities of tax to base and base to income. Here the term base refers to assessed turnover or value of clearance.

19. On the basis of data from 1970-71 to 1975-76, we found that whereas the elasticity of base to income was as high as 1.5, the tax to base elasticity was only 0.5. This shows that the value of excisable commodities increased much faster than national income during this period, even if we exclude the commodities brought into the tax net during the period. The low income elasticity must be explained by the fact that the tax did not grow as fast as the base. In fact, it grew at half of the rate at which base was growing. This conclusion would be broadly valid even if we consider the elasticity of all excisable commodities other than petroleum products.

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* The elasticity of the tax to base is equal to the percentage change in tax-- the percentage change in base, and the elasticity of base to income is equal to the percentage change in base — the percentage change in income. Hence the product of the two gives the percentage change in tax — the percentage change in income.

(c) Elasticities of the major groups of commodities:

20. The overall income elasticity of excise revenue is the weighted average of the elasticities of the yield from the various groups of excisable commodities. One could, therefore, gather an impression about the causes contributing to the low elasticity of excise revenue by examining the elasticities of the component groups. Also, the elasticities of the major groups of commodities are of interest in themselves. The following Table gives the buoyancies and elasticities of the same groups of commodities as were discussed in the section on trends.

TABLE A

Buoyancy and Elasticity of Union Excise Duties with Respect to National Income*
(1963-64 - 1974-75)

	Buoyancy	R^2	Elasticity	R^2
Total Union Excise Duties:	1.31	0.9748	0.75	0.9623
A: Food & beverages:	1.14	0.8595	0.01**	0.0010
B: Tobacco	1.09	0.9317	0.13**	0.1737
C: Petroleum products	1.43	0.9663	1.03	0.9409
D: Vegetable oils and fats	0.41	0.2968	0.86	0.8817
E: Chemicals	1.96	0.9536	1.12	0.9069
F: Metals:				
(a) Iron and steel	0.83	0.8771	-0.16	0.1753
(b) Non-ferrous metals	2.53	0.7911	0.58	0.3521
G: Manufactured goods:				
(a) Textiles	1.08	0.9617	0.38	0.8534
(b) Other manufactured goods	1.06	0.9597	0.89	0.9670
H: Machinery and transport equipment	1.54	0.9412	0.99	0.9689

*National income here refers to net national product at factor cost (Current prices)
**Estimates not acceptable for reasons stated in the text.

Source: 1. Memorandum Explaining the Provisions of the Finance Bill, Cental Government Budget

2. Explanatory Memorandum on the Budget of the Central Government

3. National Accounts Statistics 1960-61 to 1974-75, Central Statistics Organisation.

21 The buoyancy coefficients for eight out of the ten groups is greater than one, the highest being that of non-ferrous metals (2.53), followed by chemicals (1.96). The two groups that have a buoyancy co-efficient of less than one are iron and steel (0.83) and vegetable oils and fats (0.41). The additional resource mobilisation effort is seen to have been spread over all of the groups of commodities except the last-mentioned two groups. The buoyancy of iron and steel products is low largely because this industry grew sluggishly during 1963-64 to 1974-75. Vegetable oils and fats form a unique group for which the buoyancy is lower than elasticity. This is because during the reference period repeated tax concessions have been awarded to this group, as shown in the table below:

Vegetable Oils and Fats : Tax Concessions Awarded

(In lakhs of rupees)

	Additional revenue due to discretionary changes
1963-64	381
1964-65	-
1965-66	-720
1966-67	-
1967-68	-
1968-69	-
1969-70	-
1970-71	-
1971-72	-33
1972-73	-46
1973-74	-
1974-75	-

Source : Memorandum Explaining the Provisions of the Finance Bill, Union Budget, Government of India

22. The most notable feature of the group-wise elasticities is that only three out of the ten groups have an elasticity of 1 or above. These are : Chemicals (1.12), petroleum products (1.03) and machinery and transport equipment (1.00). The average share of these groups in total excise revenue during the reference period was about 42.3 per cent. The groups that had elasticity values of 0.5 or less are food and beverages, tobacco, iron and steel and textiles. These groups accounted on an average for about 36 per cent of the total revenue, and they are the ones specially responsible for giving a lower bias to the overall income elasticity of excise taxes.

23. The elasticity estimates that we have obtained for the groups "food and beverages" and "tobacco products" are in fact not acceptable. In the former case, the tax base was rather narrow at the beginning of the period and so many additional items were brought into the tax net during the subsequent years that the entire structure of taxation on this group of products changed. Under such circumstances it becomes meaningless to measure the elasticity of a given basic structure. In the latter case, our methodology of adjusting for discretionary tax changes breaks down because of two reasons: first, the continuous increases in the rates of tax on tobacco products very clearly affected the automatic growth in revenue as is shown by the near stagnation in the volume of cigarettes sold since 1968-69 and even its decline after 1971-72. (In the absence of the tax hikes the automatic growth in revenue, and therefore, elasticity would have been higher). Second, for some of the years, Government's estimates of the yield of additional taxation were higher than the actual increases in the total tax on the products concerned. In such cases, the proportional adjustment method understates the automatic growth in revenue.

24. Table B below gives the indices of industrial production, prices, and value of proxy base for selected groups of excisable commodities together with the index of national income. The corresponding income elasticity co-officients are given alongside for ready reference:

TABLE B

Indices of Industrial Production and of Prices of Excisable Commodities

(Selected Groups)
1963-64 to 1974-75

	Elasticity* (1963-64 -to 1974-75)	1974-Index of Industrial production $=I_0$ (Base 1963 = 100)	1974: Index of Prices $= I_p$ (Base 1963 = 100)	1974: Index of Value $=I_v$ (Base 1963 = 100)	Index of NNP 1974-75 (Base I_y 1963-64 = 100)
				$I_v = I_o.I_p$	
11 commodities	0.75	158.0	281.4	444.6	342.5
Petroleum Products	1.03	257.4	261.4	672.8	342.5
Chemicals	1.12	220.0	224.0	492.8	342.5
Manufactures					
1) Textiles	0.38	97.9	234.4	229.5	342.5
2) Other manufactures	0.89	156.0	180.4	281.4	342.5
Machinery and transport equipments	0.99	185.5	212.1	393.4	342.5

Source: 1) Monthly Production of Selected Industries, C.S.O.

2) Monthly Abstract of Statistics, C.S.O.

3) Index Number of Wholesale Prices, Office of the Economic Adviser, Ministry of Industries and Civil Supplies

*Elasticity of Union excise duties with respect to National Income.

It is seen that the indices of value of output - which may be treated as a proxy potential base for the excise duties - rose faster than national income in the case of all groups other than manufactured goods. The value of output of all excisable goods increased much faster than income, namely by 344.6 per cent, and yet the elasticity of excise tax revenue as a whole was only 0.75, partly because of the prevalence of specific duties and partly because of downward bias given by the elasticities of duties on tobacco and food products referred to earlier. Chemicals and machinery and equipment have been subject to predominantly ad valorem rates of duty and we are able to see from the growth of their base how they could be fairly income elastic sources of revenue (elasticity nearly equal to 1). Petroleum products, on the other hand, were subject to specific duties and the higher than unit elasticity of these duties could only be explained by a possible increase in the weight of the higher taxed products (giving a higher value of the tax to base elasticity). The group "other manufactured goods" has an elasticity of nearly 0.9. Duties on them have gradually been converted from specific to ad-valorem. The value of their proxy base, however, did not increase as fast as national income. The progressive nature of the duties on these goods must have contributed to some extent to the elasticity becoming near unity.

25. The low value of elasticity of the yield from iron and steel products (see Table A) is to be largely explained by the fact that the production of the major items in this group such as plates and sheets, blooms, billets, pipes and tubes etc. had remained stagnant during the period 1965 to 1974.

26. We shall now consider the base data from 1970-71 to 1975-76 and comment on the behaviour of the groups in terms of the tax to base and base to income elasticities*. These are given in Table C below. The elasticity of base to income, except for vegetable oils and fats (0.6), is greater than one for all groups. The highest is that of petroleum products (3.11), followed by tobacco (1.99) and iron and steel (1.9). These are precisely the groups with the lowest tax to base elasticities-petroleum products (0.17), tobacco (-0.14) and iron and steel (-0.21). These groups have largely specific rates of duty and the results, therefore, seem quite plausible.

* These have been computed on the basis of the compound rates of growth of the concerned variables, as indicated earlier.

TABLE C

Tax and Base Elasticities of Union Excise Duties

(1970-71 to 1975-76)

		Elasticity of taxes to income E_{TY}	Elasticity of taxes to the base of the taxes E_{TB}	Elasticity of base of taxes to income E_{BY}
Total Union Excise Duties		0.78	0.51	1.52
A:	Food and beverages	0.34	0.31	1.09
B:	Tobacco	(-) 0.28	(-) 0.14	1.99
C:	Petroleum products	0.55	0.17	3.11
D:	Vegetable oils and fats	0.58	0.97	0.60
E:	Chemicals	1.37	0.86	1.59
F:	Metals:			
	a) Iron and Steel	(-) 0.40	(-) 0.21	1.89
	b) Non-ferrous metals	0.73	0.65	1.12
G:	Manufactures:			
	a) Textiles and jute	0.75	0.49	1.53
	b) Other manufactured goods	1.03	0.85	1.22
H:	Machinery and transport equipment	0.67	0.51	1.32

Source:
1) Memorandum Explaining the Provisions in the Finance Bill, Central Government Budget.
2) Explanatory Memorandum on the Budget of the Central Government.
3) National Accounts Statistics, 1960-61 to 1974-75, Central Statistical Organisation.

27. The highest tax to base elasticities are for vegetable oils and fats (0.97), chemicals (0.86), other manufactured goods (0.85) and non-ferrous metals (0.65). It is interesting that there is no group with tax to base elasticity of greater than one. The highest tax to base elasticity of nearly 1 for vegetable oils and fats is due to the fact that this group has predominantly ad valorem rates of duty. This reason is also valid in relation to chemicals to some extent.

28. The income elasticities of excises on these groups that are obtained on the basis of the tax and base data for 1970-71 to 1975-76 give us a somewhat different picture from the one that emerged from the calculations for the longer reference period. The income elasticity of excise tax revenue as a whole shows a moderate improvement; it stands at 0.78. Even though chemicals continues to have the highest elasticity (1.37) among all groups, the next in line are other manufactured goods (1.03), textiles and jute (0.76), non-ferrous metals (0.73) and machinery and transport equipment (0.67). The tax to income elasticity of petroleum products during this period turns out to be rather low at 0.55; the main reason for this seems to be that stiff increases in taxation towards the end of the period led to a fall in consumption.

29. The groups with the lowest elasticity of tax to income figures are iron and steel (-0.4), tobacco (-0.3) and food and beverages (0.3). Both iron and steel and tobacco, which have fairly impressive base to income elasticities have the lowest tax to income elasticities.

C. Factors Contributing to the Growth in Tax Revenues :

30. Finally, we shall attempt to separate out the increase in the tax yield due to the bringing in of new commodities into the tax net from that due to base increases and rate changes in relation to the commodities already subject to tax, with 1965-66 as the dividing year. Excise tax revenue increased from Rs. 897.2 crore in 1965-66 to Rs. 3823.62 crore in 1975-76, i.e., by Rs. 2925.70 crore. This increase can be attributed to three factors: (i) bringing in of new goods into the tax net. (ii) increase in the tax bases of commodities already subject to tax in 1965-66, and (iii) increases in the rates of taxes on these 'old' goods.

31. In order to identify the contribution of the three factors, we first substracted from each year's revenue collection, the yield from all the 'new' commodities taxed after 1965-66. The residual series represented the yield of the 'old' commodities. Applying the proportional adjustment method to this series, we obtained cleaned series that indicated the growth of revenue that would have taken place in the absence of rate changes in relation to 'old' goods. Thus we obtained three series as follows:

(In crores of rupees)

	1966/67	1967/68	1968/69	1969/70	1970/71	1971/72	1972/73	1973/74	1974/75	1975/76
1. Revenue from new goods	2.51	7.28	17.87	38.90	66.74	105.48	137.94	165.83	286.03	343.19
2. Growth in revenue due to rate changes	81.73	160.88	217.65	299.04	437.52	596.06	754.74	906.3	1200.72	1532.68
3. Automatic growth in revenue from old goods	81.61	82.44	304.71	288.45	389.26	479.69	558.3	649.8	884.64	1049.83

32. The last term in the first series gives us the contribution of new goods to the increase in revenue after 1965–66 and the last term in the second series gives the contribution of rate changes. Subtracting the last term in the third series from the total revenue in 1965–66, we obtain the contribution of the growth in base to the increase in revenue. Thus we have :

Contribution to increase in revenue from (1965–66 to 1975–76)

		Rs. crore	% of total increase
(i)	New goods	343.19	11.73
(ii)	Rate changes in relation to goods taxed in 1965–66	1532.68	52.39
(iii)	Growth of base of goods already taxed in 1965–66	1049.83	35.88
		2925.70	

Thus, the introduction of new items brought in only a rather small percentage of the increase in revenue between 1965–66 and 1975–76. It is significant that rate increase brought in as much as 52.4 per cent of the increase in revenue, while the growth of the basis brought in 35.9 per cent. Even assuming that the method of adjustment that we have used tended somewhat to underestimate the latter, it is clear that during the period under reference predoninent reliance was placed on rate increases for raising additional resources.

III. IMPORT DUTIES

A. Introduction :

33. India's customs duties have two components, viz., import duties and export duties, of which import duties are by far the more important. In 1974–75, customs duties yielded a revenue of Rs. 1333 crore of which Rs. 1194 crore, i.e., 90 per cent, were derived from duties on imports. The corresponding percentages for 1966–67 and 1970–71 were 79 and 75, respectively, which show that the importance of import duties has somewhat increased over the years.

34. Import duties are of two types, namely, revenue duties and protective duties. Of the revenue duties, machinery, ferrous and non-ferrous metals, chemicals and petroleum products constitute nearly two-thirds of the total. Apart from the purpose of protecting infant industries and earning revenue, import duties are also levied in order to influence the composition of imports, which is dictated largely by the needs and compulsions of the country's economy. It should be obvious, therefore, that the revenue collected from import duties, besides being dependent on the volume of imports, will also depend on the type of trade policies pursued by the country.

35. Imports into India have been subject to licensing throughout the post-Independence period. The proportion of licenses going to traders has gradually diminished from over 61 per cent of all licenses issued in 1951-52 to less than 3 per cent in 1970-71*. The proportion going directly to producers has now taken over the bulk of available imports.

36. In the last twentyfive years or so, the structure of imports has shifted in favour of capital goods, intermediate goods and raw materials, the only consumer goods imported in any significant quantity being foodgrains. Foodgrains, fertilisers and petroleum crude were the three major items that were exempted from import duties.

a) Quantitative restrictive regime:

37. The Second Five Year Plan period was characterised by a quantitative restriction (QR) regime which was generating import premia. From 1962-63 onwards import duties were used with increasing frequency to mop up the import premia generated by the QR regime.** Table 2 reflects this trend, showing that the average incidence of import duties rose steadly from 33 per cent in 1963-64 to 52 per cent in 1965-66. Most of the increases in import duties were selective and differential. In 1962-63 import duties were raised on some iron and steel items, silk yarn, copra, cars and machine tools. In 1963-64 import duties were raised on raw cotton, machinery, rubber, palm oil, iron and steel, manufactured mineral oils and dyes. In 1963-64 a surcharge was levied on all durable articles at a flat rate of 10 per cent of the existing import duty. Further, a general regulatory duty was levied at 10 per cent ad valorem which came into effect on February 17, 1965**. On the whole, the tariff structure lacked any clear rationale. This was not surprising because the premia resulting from the various degrees of import control pursued by the Government had no definite pattern as between different protected activities. The tariff structure, moreover, lacked stability, and it shifted with changes in premia resulting from the dynamic interaction of domestic and foreign supplies and demand. A measure of rationalisation of duties was brought about in the same year when importables were broadly classified into three categories, namely, raw materials, intermediate goods and fully processed goods. The rationalisation was arrived at by reducing the wide range of selectivity as well as the number of rates. Table D below shows the rates introduced:

Table D

Average Rates of Nominal Import Duty on Broad Classes of Commodities. Supplementary Budget

1965-66

Item	Percentage Rate of Import Duty*
Agricultural machinery	15

*See Bhagwati and Srinivasan (1976), pp. 76-80

**If the additional rate calculated at 25 per cent of the existing duty worked out to be higher, then this higher rate was applicable.

Item	Percentage Rate of Import Duty
Plant and machinery	35
Basic industrial raw materials	40
Processed industrial materials	60
Fully manufactured goods	100

*To these we must add the regulatory duty of 10 per cent

Source : Bhagwati and Desai (1970)

Original Source: Government of India, Ministry of Finance, Department of Economic Affairs, New Delhi

(b) Effective rate of protection :

38. Here we would like to draw a distinction between the above mentioned rates of duty and the effective rate of protection. The latter concept refers to the degree of protection of a particular process or economic activity as distinct from the 'nominal' tariff on output. The effective rate of protection on a process may be defined as the incremental value added (due to the tariffs) divided by the value added at c.i.f. prices*. In the short run, it is only the nominal tariff rate that determines the amount of import duties collected. However, in the long run it is the effective tariff rate that would be more relevant as a guide to the effect on the allocation of domestic resources and the relative outputs of different commodities. In the long run, therefore, it is the effective rate of protection that would determine which goods would be produced in what amounts, and how much of importables would be necessitated; the last would, in turn, determine the amount of import duties collected. Thus the long-run elasticity of import duties would be dependent on the effective rates of protection. We shall, however work only on the basis of the nominal rates of tariff.

(c) Import substitution :

39. Along with the maintenance of severe import restrictions, efforts have been made to encourage indigenous production of essential commodities, including raw materials and intermediates. An indication of the extent of import substitutions over the last few years is given by the substantial decline in the proportion of imports to total supplies of many of these commodities**. To the extent

*See Bhagwati and Desai (1970), p.336.

** See Economic Survey, 1964-65, Ministry of Finance, Government of India, P.36.

that import are substituted for by domestic production, the magnitude of import duties would go down and excise duties would go up, assuming that the relevant items are within the excise tax net.

B. Trends and Composition of Import Duties :

40. Revenue from import duties, which constituted about 24 per cent of the total central taxes in 1963-64 and 1966-67stood a little lower at 23 per cent in 1974-75. Import duties collected were Rs. 334 crore in 1963-64 and went up ' to Rs. 548 crore in 1965-66. The devaluation of 1966 and the recession of the next few years led to a declining yield from import duties for four successive years; and in 1969-70 the yield was only Rs. 306 crore. However, whithin the next two years the revenue from import duties had doubled; and by 1975-76, it had quadrupled over the level of 1969-70*.

41. The major groups of items which account for about 70 per cent of the import revenue collected are the following : (a) petroleum products (b) chemicals (c) iron and steel (d) non-ferrous metals (e) textiles (f) manufactured goods other than textiles and (g) machinery and transport equipment.

42. Import tax revenue earned from petroleum products, which formed about 15 per cent of the total duties collected in 1965-66, had declined in importance to about 8 per cent of the total by 1974-75. The revenue collected in absolute terms has inereased only a little over these years - in 1965-66 it was Rs. 83 crore, it went down to Rs. 30 crore in 1970-71 and gradually moved upto Rs. 96 crore by 1974-75. Note that petroleum crude was exempted from import duties**, so the items that earned the revenue were kerosene oil, high speed diesel oil and vaporising oil, motor spirit, individual fuel oils and lubricating oils,

43. 'Chemicals' is the only group for which the import duties in absolute terms did not go down after the devaluation of 1966. The duty collected in 1965-66 was Rs. 27 crore which had steadily moved up to about Rs. 35 crore by 1969-70 and to Rs. 182 crore in 1974-75, The share of chemicals in the total increased from around 5 per cent in 1965-66 to 15 per cent in 1974-75.

44. The share of iron and steel that was about 11 per cent of the total import duties in 1965-66 had gone up to about 18 per cent in 1974-75. However, it had tapered down to 12 per cent in 1975-76. In absolute terms the duties went down from Rs. 62 crore in 65-66 to Rs. 34 crore in 1969-70, but it had gradually increased to Rs. 211 crore by 1974-75. The importance of non-ferrous metals is much less than that of iron and steel; the share of the former moved up from about 2 per cent in 1965-66 only to 4 per cent in 1974-75.

45. Import duties from textiles and jute have never been very important because India is a net exporter of jute and cotton textiles. However, certain specific items pertaining to textiles that are mostly in the nature of raw materials and not domestically available*** are imported. The share of

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*See Table 1

**Import duties began to be levied on petroleum crude in 1975-76.

***These are certain varieties of raw wool, raw cotton, staple fibre (excluding yarn), artificial silk, yarn and thread, raw silk and artificial silk fabrics.

this group of items over the reference period* is 4 per cent of the total import duties. Among the manufactured goods other than textiles that contribute significantly to import duties are cinematograph films, rubber, pulp, paper and board, glass and glassware. The duties from these items, again, form hardly 2 to 3 per cent of the total. In absolute terms the import duty from both these groups was Rs. 31 crore in 1965-66. This went down to Rs. 13 crore in 1969-70 but it steadily moved up to Rs. 91 crore by 1975-76.

46. The most important revenue earning group is machinery and transport equipment. Its share in the total import duties has, however, fluctuated over the years. It increased from 28 per cent in 1965-66 to 39 per cent in 1968-69 but after that it fluctuated, and in 1975-76 it stood at 26 per cent. In absolute terms, import duty collections on this group dropped from Rs. 153 crore in 1965-66 to Rs. 105 crore in 1969-70 before moving up steadily to Rs. 326 crore in 1975-76.

47. The average incidence of import duties, that is, import tax revenue as a percentage of the value of importables has also been calculated. For this purpose the value of cereals and fertilisers has been excluded from the base because these items are exempted from import duties**. So in effect what is calculated is the ratio of import duties to the value of import trade minus the value of cereals and fertilizers. This ratio moved up from 33 per cent in 1963-64 to 52 per cent in 1965-66 at the pre devaluation rupee parity. With the post devaluation parity of the rupee, the ratio for 1965-66 was 34 per cent, which further went down to 25 per cent in 1969-70. This was due to the scaling down of import duties which accompanied the devaluation. But since the duties were raised in subsequent years, the ratio started to rise and was 39 per cent in 1975-76.

C. Buoyancy and Elasticity of Import Duties :

48. If imports into a country are allowed fairly freely, i.e., if there are no quota or quantitative restrictions, then total imports, and therefore, import duties, may be expected to respond positively to growth in national income. Since the middle 50's and right upto 1974-75, India was faced with acute foreign exchange shortage most of the time, and import of various kinds were subjected to different degrees of import control. Because of this fact and two other crucial factors, namely, the devaluation of 1966 and the oil price hike of 1973-74; one connot really expect to find a close relationship between import tax and national income during the period under reference.

49. We did, however, go through the exercise of computing the buoyancy and elasticity or total import duties and of import duties on the major groups of importables. As expected, the fit was not good. We obtained very low elasticities for the total as well as for most of the groups.

50. One further complication is that increases in import duties might themselves have affected the automatic growth in revenue. In such an event, as explained earlier in relation to excise duties on tobacco, the proportional adjustment method will give misleading results. However, given the data limitations, no other method of adjustment was possible.

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*i.e., 1963-64 to 1975-76.

**As pointed out earlier, crude petroleum was exempted from import duties uptil 1974-75, but subsequently it was brought under the tariff the next year.

51. Since the resulting elasticity estimate: xxx xplausible and are likely to mislead, we are not presenting them in relation to the period 1963-64 to 1974-75.

52. The buoyancy of total import duties and of the duties from five groups* of imports have been calculated (see Table E on the following page) with reference to (a) national income, (b) the value of total imports and (c) the value of non food imports**. The period covered is from 1963-64 to 1974-75. As pointed out earlier the buoyancy regressions do not display good fits with any of the above explanatory variables.

53. The buoyancy of total import duties with respect to the total value of importables works out to 0.93. The highest buoyancy is that of chemicals (1.73) and the lowest that of petroleum products. Machinery and transport equipment have a low buoyancy of 0.72.

54. As mentioned earlier the devaluation of 1966 had its reverberations right up till 1968-69. We have, therefore, separately analysed in Table F the trend of import duties from 1969-70 onwards till 1975-76. Because the number of observations are insufficient for a meaningful regression exercise, we have looked at the compound growth rates of the duties on the major groups as well as of the total import duties.

55. The compound rate of growth of total import duties during the period from 1969-70 to 1975-76 works out to 26.4 per cent. However, the automatic growth of revenue during the same period was at the compound rate of 19.6 per cent.

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*The groups are petroleum products, chemicals, iron and steel, manufactured goods other than textiles and machinery and transport equipment.

**The results obtained with (b) and (c) as the explanatory variables are quite close.

Table E

Buoyancy of Total Import Duties and of Certain Major Groups of Importables (1963-64 to 1974-75)

		Buoyancy	
Total import duties :	A*	0.86	0.5439
	B**	0.93	0.6045
	C***	0.96	0.6767
Petroleum products**		0.36	0.0770
Chemicals**		1.73	0.7525
Metals: iron and steel***		1.50	0.7562
Manufactured goods other than textiles***		1.25	0.7650
Machinery and transport equipment***		0.72	0.7049
Value of Imports		0.81	0.7054

* With respect to national income.

** With respect to the value of total imports.

*** With respect to non-food imports.

Sources:

(1) Memorandum Explaining the Provisions in the Finance Bill, Central Government Budget.

(2) Explanatory Memorandum on the Budget of the Central Government

(3) National Accounts Statistics, 1960-61 - 1974-75, Central Statistical Organisation.

(4) Monthly Statistics of Foreign Trade, Vol. II, DGCI&S, Calcutta.

Table F

Compound Rates of Growth of Total Import Duties and Duties on Major Groups of importables

(1969-70 to 1975-76)

	Compound Rates of Growth of the Actual Duties (percentage)	Buoyancy*	Compound Rates of Growth of the Hypothetical Series (percentage)	Elasticity*
Total import duties	26.38	2.31	19.64	1.72
Petroleum products	19.4	1.70	15.9	1.40
Chemicals	22.5	1.97	18.6	1.63
Metals (iron and Steel)	28.3	2.48	25.3	2.22
Manufactured goods other than textiles	32.1	2.82	29.1	2.55
Machinery and transport equipment	24.8	2.18	11.5	1.00

* Both buoyancy and elasticity have been calculated with the value of importables (excluding the value of cereals, fertilisers and petroleum products) as the explanatory variable.

Sources:

1. Economic Survey, Government of India 1969-70 to 1975-76.
2. Explanatory Memorandum Government of India 1969-70 to 1975-76.

With value of dutiable imports as the explanatory variable (which grew at the compound rate of 11.4 per cent) the buoyancy and elasticity work out to 2.31 and 1.72, respectively. The elasticity of import duties (I) with respect to national income (Y) may be decomposed into the product of the elasticity of import duties with respect to the value of importables (B) and the elasticity of the value of importables with respect to the national income. In symbols this may be written thus:

$$E_{IY} = E_{IB} \cdot E_{BY}$$

It turns out that the compound rate of growth of national income from 1969-70 to 1975-76 is 11.37 per cent. This makes the value of E_{BY} approximately equal to unity* which implies that the elasticities of import duties to national income and import duties to the value of importables are equal for the reference period.

56. In the groupwise analysis, 'manufactured goods other than textiles' with a compound growth rate of 32.1 per cent records the highest buoyancy of 2.82. The lowest buoyancy figure is recorded for petroleum products (1.7). Machinery and transport equipment which has generally accounted for about one quarter to one third of the import duties has a buoyancy of 2.18.

57. The group with the highest elasticity (as also the highest buoyancy) is manufactured goods other than textiles (2.55). Next to this is iron and steel with an elasticity of 2.22, which is in striking contrast to the elasticity of excise duties for this group - it was the lowest, and with a negative value (-0.16)** The elasticity values for chemicals and petroleum products are 1.63 and 1.4 respectively. With the buoyancy figures for the above four groups at 2.82, 2.48, 1.97 and 1.7 respectively, it appears that discretionary measures were not much relied upon to mop up import duties in these four categories. The elasticity for machinery and transport equipment works out to 1. Compared to the buoyancy estimate of 2.18 it seems that there was a significant growth in the inflow of new machinery and transport equipment in this period. Further, it should be noted that the rate of automatic growth in import duties from this group more or less kept pace with the growth rate of the value of dutiable imports.

58. Thus it may be concluded on the basis of data from 1969-70 to 1975-76 that import duties are elastic with respect to the value of dutiable imports, i.e. the value of elasticity is greater than unity. This implies that the structure of import duties is not inherently sluggish as it is in the case of excise duties. The major reason for this, as we have discussed earlier, is that whereas all of import duties are of the ad valorem type, a substantial part of excise duties is due to specific taxes, which have a built-in bias towards inelasticity.

IV Trends and Changes in the Composition Of Major State Indirect Taxes

59. The tax structure of the States has undergone perceptible changes over time, in terms of both the absolute and relative contributions of direct and indirect taxes. Direct taxes on income,

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*E_{BY} = 1 means that the compound growth rates of the value of importables and national income kept pace with each other during the reference period.

**The reference period, however, was from 1963-64 to 1974-75 and the explanatory variable was national income.

property and capital transactions accounted for over one third, or 34.6 per cent, of the total tax revenue of the States in 1960-61; this share has fallen to less than one sixth, or 18.8 per cent, in 1975-76. On the other hand, the share of indirect taxes on commodities and services has increased from 65.4 per cent to 86.4 per cent over the same period; in absolute terms there has been a ten-fold increase in their yield from Rs.295 crores to Rs.2955 crores. In terms of proportion of net national product, State indirect taxes constituted 2.2 per cent in 1960-61, 3.7 per cent in 1970-71 and 4.9 per cent in 1975-76.

60. Among the State indirect taxes, a certain structural transformation of the relative role of different constituents is evident from the statistical data. Sales taxes of course remain the most significant source of indirect tax revenue for the States. Four types of sales taxes, namely, the general sales tax, Central sales tax, sales tax on motor spirit and purchase tax on sugarcane together contribute more than half of the total indirect tax revenue of the States. Yet, over the period under study, the relative importance of these taxes in terms of percentage contribution to tax revenue has changed. Their combined contribution declined from 60.4 per cent of total indirect tax revenue of all States in 1970-71 to 54.2 per cent in 1973-74, but then improved significantly to 62.8 per cent in 1974-75. (Table 8)

61. Among the four sales taxes, the most important contribution is of the general sales tax, which accounts for about three-fourths of the sales tax revenue of all the States, with Central sales tax accounting for about one-fifth of the total sales tax revenue of the States (Table

62. An analysis of data over a longer time period from 1960-61 to 1974-75 given in Table I also brings out the dominating position of the general sales tax in the State indirect tax structure, even though there has been a nominal fall in its contribution in some of the years. Between 1960-61 and 1973-74, the contribution of the general sales tax to the total indirect tax revenue of the States declined from 42.3 per cent to 40.0 per cent, but then increased to 46.2 per cent the following year. In absolute terms, the yield of the general sales tax has increased very substantially from Rs.125 crores to Rs.1166 crores, that is, an increase of 933 per cent.

63. The contribution of State excises to State tax revenues is also quite significant, at about one sixth of their total indirect tax revenue. Over time, however, there has been some decline in its relative contribution from 18.2 per cent to 15.3 per cent (during 1960-61 to 1974-75). A similar decline in the relative share is also discernible in the case of tax on motor vehicles and electricity duty; however, while the decline is sharp for the former from 11.1 per cent of total State indirect tax revenue in 1960-61 to 7.4 per cent in 1974-75, it is nominal for the latter from 4.5 per cent in 1960-61 to 3.6 per cent in 1974-75.

64. The relative contribution of the tax on passengers and goods has, on the other hand, improved substantially from 1.5 per cent of indirect tax revenue in 1960-61 to 4.4 per cent in 1965-66 and 5.5 per cent in 1974-75. The contribution of entertainment tax has been fairly constant, varying only between 4.5 and 4.9 per cent.

65. The foregoing analysis of the trend in the yield of major State indirect taxes brings out the predominant significance of sales taxes, particularly the general sales tax, for the State exchequers. It is noteworthy that their relative importance has increased, inspite of the exploitation of other sources of revenue by the State Governments. State excises, though declining relatively to several others, still remain next in importance only to sales taxes. The changes in the relative shares of

the different indirect taxes have been the result of their differing rates of automatic growth and of the directions of additional resources mobilisations by the States. These factors can be analysed through the measurement of the buoyancy and elasticity of the major indirect taxes.

Buoyancy and Elasticity of State Indirect Taxes Methodology of Estimation and Limitations

66. Gross and net tax yields are regressed on State income at factor cost to estimate the buoyancy and elasticity coefficients. The tax yield data used in the study relate to 18 States, as some States like Sikkim, Manipur, Tripura and Meghalaya did not exist throughout the period and for some others, like Nagaland, consistent data are not available. Even though the number of States have increased over time, the increase is due to geographical breakup and can only nominally affect tax collection data at the aggregate or all States level. Income is taken as the single explanatory variable in the equation and the significance of coefficients is tested on the basis of the 't' test.

67. The methodology of estimation adopted for the study as well as the data used for estimation have certain inherent limitations:

i) data used in eliminating the effects of additional tax measures from the gross yield are generally ex-ante estimates; as such, any over estimation by States of the yield from the tax measures under-estimates the elasticity coefficient.

ii) Changes in arrears in tax collections limit the validity of annual data on the yield of taxes given in the budget. The total tax demand in any year consists of current demand and demand in relation to part or whole of arrears of earlier years, the yearwise break-up of which is not available. Similarly, tax collection in a year comprises realisation from the current demand and also a part of the backlog of arrears. This brings in distortion in the data because the realisation of arrears is very erratic, linked closely to administrative factors, responsiveness of assessees and general economic conditions. Studies on buoyancy and elasticity, therefore, have to assume that the problem of arrears does not unduly distort the normal rate of growth of tax revenue, i.e. that either arrears are negligible or that they are growing more or less at the same rate as collections.

iii) Gross tax yield is in reality a function of changes in State income, the rate schedule, changes in coverage through additions to, or omissions from, taxed items, changes in administrative efficiency, changes in the degree of compliance, evasion and avoidance. However, for lack of information and on account of difficulties in quantifying such intangible factors as compliance, we are forced to leave several of the factors out. The use of State income alone as an explanatory variable carries the implicit assumption that even additional tax mobilisation efforts are dependent on the growth of income. Again, the use of income as the independent variable in the function for each tax overlooks the fact of inter-dependence of the basis of different taxes. Thus, for instance, the imposition of a tax on one commodity changes consumer equilibrium resulting in a different pattern of consumer demand. This reduces the base of taxes on certain commodities and enhances that of some others. In a federal set up, the problem is even more pronounced as more than one authority operate on the same base to get more revenue.

(v) As explained in the companion paper, the proportional method of adjustment enables one to capture only the "average" of the elasticities of the different tax structures extent during the reference period and not that of a structure of any given year.

68. The above-mentioned limitations must be borne in mind in interpreting the results of the exercise. Although it is not possible to quantify the margin of error involved, on the basis of best judgement, it may be stated that the elasticity coefficients derived here give us a broad picture of the relationship between State indirect tax revenues and State incomes.

Buoyancy and Elasticity Of State Indirect Taxes - Aggregates for All States

69. Estimates of elasticity coefficients of individual taxes for different States reveal significant variations indicating that the responsiveness of individual taxes to changes in State income vary from State to State and also between different taxes within a given State. The variations in buoyancy coefficients are to be attributed also to an additional factor, namely, differences in policies regarding discretionary tax changes.

70. Buoyancy and elasticity coefficients have been computed at the all States level for a few specific State taxes, namely, the general sales tax (including the sales tax on motor spirit), the motor vehicles tax, the passengers and goods tax and the entertainment tax. The results of these computations presented in Table 1 indicate that the State tax systems on the average are not only buoyant but also elastic with reference to changes in State income.

71. The general sales tax, the most important source of revenue for State Governments, was highly buoyant; and it has also been income elastic. The elasticity coefficient of 1.15 indicates that a 1 per cent change in net national product (NNP) will lead to a 1.15 per cent change in the yield of the general sales tax. The value of elasticity coefficient shows that the State sales tax structures are such that even if there would have been no change in tax parameters in successive years, the tax yield would have grown faster than NNP. State sales tax systems have been highly buoyant because the States exploit this source to a large extent for additional resource mobilisation. However, it will be seen later that the degree of buoyancy and elasticity of the sales tax varies as between States.

72. The general sales tax (including sales tax on motor spirit) and the entertainment tax have the highest buoyancy co-efficient among the State taxes for which computations have been made; in both the cases, buoyancy is 1.43. In the case of the taxes on the motor vehicles and passengers and goods (together), buoyancy is lower at 1.27.

73. Not only were the general sales tax systems highly buoyant, but they have also been most elastic to changes in income, the elasticity coefficient at the all States level being 1.15. On the other hand, the elasticity co-efficients of entertainment tax and taxes on motor vehicles and on passengers and goods are much lower at 1.04 and 1.05 respectively. The earlier analysis in section II on the trend in revenue from various taxes had already shown that the relative contributions of the tax on passengers and goods had improved over time, but that of the tax on motor vehicles had declined very significantly.

74. The coefficient for the tax on motor vehicles and on passengers and goods which have been taken together relates to 18 States for the period 1963-64 to 1973-74, while the coefficients for the other two taxes (general sales tax and entertainment tax) relate to fewer States (14) but for a longer time period (1963-64 to 1974-75).

75. Buoyancy and elasticity coefficients have been computed for 16 States also for another, shorter period (1968-69 to 1975-76). These co-efficients have been computed for the general sales tax (including sales tax on motor spirit) and for the entertainment tax. In both the cases, the buoyancy and elasticity coefficients are higher than those presented earlier for fewer states but for a longer time period. While in the case of the general sales tax, the buoyancy coefficient for a smaller time period and larger number of states is 1.44 (1.43)earlier), the elasticity coefficient is 1.23 (1.15) and for entertainment tax the buoyancy coefficient is 1.54 (1.43) and elasticity coefficient 1.18 (1.04).

76. The preceding analysis thus shows that buoyancy and elasticity coefficients for State taxes are more effected by differences in time period than by differences in the number of States covered, provided the major States are included. The method of computation of elasticity and buoyancy does not significantly affect the values of the coefficients at the all-India (aggregate) level.

Inter-State Comparisons

77. Buoyancy and elasticity estimates at the aggregate level conceal inter-state variations. Due to the operation of various factors, there are significant inter-state variations in the buoyancy and elasticity of different indirect taxes. Among the influencing factors are consumer expenditure pattern, the degree of urbanisation, the rate of development of transport industry, the degree of movement of passengers and goods, the efficiency of tax administration, and the relative rates of growth of the volume of trade.

78. Inter-State comparisons of buoyancy and elasticity are confined to selected indirect taxes like the general sales tax, the sales tax on motor spirit, taxes on motor vehicles and on passengers and goods and the entertainment tax.

General Sales Tax

79. The range of variations in the buoyancy and elasticity of the general sales tax is quite wide among the 16 States for which estimates have been computed and are presented in Table 11. The general sales tax is the most buoyant in Jammu and Kashmir with buoyancy coefficient being 1.86, while the buoyancy of this tax is lowest in Bihar at 1.16. As against the average of 1.43 for all the States, eight States have above average buoyancy, these being Jammu and Kashmir, Karnataka, Utter Pradesh, Tamil Nadu, Assam, Haryana, Gujarat and Punjab. In none of the States is the buoyancy of the general sales tax less than 1.0, indicating that sales tax collections increased faster than State incomes in all the States.

80. In the case of elasticity, the range of variation is between 0.85 for West Bengal and 1.52 for Assam; in nine out of the 16 States elasticity coefficients are higher than the all-States average of 1.15. In Kerala, Jammu & Kashmir and West Bengal the elasticity of these taxes is less than unity, the lowest being 0.85. Thus the States having a low elasticity in their sales tax system are not only the under developed states but also industralized States like West Bengal.

81. A comparative examination of the buoyancy and elasticity coefficients indicates that highly buoyant State general sales tax systems are also highly elastic with respect to income. All the States having above average buoyancy, except Gujarat and Jammu & Kashmir, have above average elasticity, though even in the case of Gujarat the elasticity is more than unity (1.08) and in the case of Jammu & Kashmir it is slightly less than unity (0.98). Similarly, all States with above average elasticity have above average buoyancy except Andhra Pradesh, Rajasthan and Maharashtra. Even in these three cases the buoyancy is quite high ranging between 1.38 and 1.42. In other words, a high level of buoyancy is associated with a high level of elasticity and vice versa. Similarly, a low level of elasticity is associated with a low level of buoyancy as in the case of West Bengal, Kerala and Bihar.

82. While for all States taken together the difference between buoyancy and elasticity is only 0.28, for some individual States the differences are larger. They vary from 0.88 in Jammu & Kashmir to 0.05 in Haryana; in 5 of the 16 States for which the co-efficients have been worked out, the variations exceed the all India average of 0.28; these States are Jammu & Kashmir, West Bengal, Karnataka and Gujarat. In Madhya Pradesh it equals the all-India average.

83. In respect of the States that have low elasticities the additional mobilisation effort during the period 1964-65 to 1974-75 is given in Table A. It is evident that in these States

Table A

Extent of Additional Tax Mobilisation in Selected States

(1964-65 to 1974-75) (General sales tax)*

(In lakhs of rupees)

Year/States	Bihar	Gujarat	J & K	Kerala	Orissa	West Bengal
1964-65	1	15	-	-	-	-
1965-66	48	35	-	10	-	20
1966-67	73	440	10	40	20	785
1967-68	-	80	28	30	8	532
1968-69	-	553	20	-	-	180
1969-70	60	-	5	65	-	95

*including Central sales tax.

Year/States	Bihar	Gujarat	J & K	Kerala	Orissa	West Bengal
1970-71	90	287	-	100	84	-
1971-72	90	90	16	283	10	6
1972-73	34	207	10	300	-	245
1973-74	-	-	-	-	-	110
1974-75	225	270	45	700	200	600

Source: State Governments' Memoranda to the Finance Commissions.

either the magnitude of yield of additional taxation is quite high or the frequency of tax change is more, leading to higher tax yields over time. On the other hand, States like Assam, Punjab, Haryana, Karnataka, Uttar Pradesh and Tamil Nadu have a more elastic sales tax structure.

Sales Tax on Motor Spirit

84. Data on sales tax on motor spirit are available only for 10 of the 16 States, as in the case of the others these are merged with the revenue data for the general sales tax and the Central sales tax. The following analysis therefore relates only to these 10 States. The results are presented in Table 12.

85. Even though this tax is generally levied on a specific basis, it has shown a reasonable degree of elasticity in a number of States, with high, values being obtained for Punjab, Haryana, Uttar Pradesh and Tamil Nadu. In the case of Jammu & Kashmir and Orissa, the elasticity coefficients are negative. There must be some special reasons for these abnormal values of the coefficients but this have not been examined in the present study. In the case of West Bengal, Gujarat and Assam these taxes have exhibited low income elasticity, with charges in income explaining only between 11 per cent and 41 per cent of the total variation in the tax. The special reasons explaining these results have also not been examined in this study.

Taxes on Motor Vehicles and Passengers and Goods

86. The generally high level of buoyancy of this group of taxes and the differences between buoyancy and elasticity seen in most of the States indicate that during the period under reference these taxes were relied upon for additional mobilisation of resources. The tax on motor vehicles

is levied on a specific basis and on that score can be expected to be price-inelastic. On the other hand, the tax on passengers and goods should prove elastic with reference to income at current prices not only because it is often levied on an ad valorem basis but also because passenger and goods traffic tend to grow faster than income. This is inherent in greater industrialisation and geographical specialisation or division of labour. It is noteworthy that in all the relatively advanced (per capita income basis) or industrialized Sates, excepting Tamil Nadu, the elasticity of this group of taxes is higher than unity. The results are contained in Table 13.

87. We notice that the buoyancy and elasticity co-efficients in the case of motor vehicle & passenger and goods taxes (taken together) in Bihar are unusually high at 2.36 and 2.18 respectively. These were not due to any discretionary changes in tax measures or to a high degree of responsiveness but were presumably due to some administrative re-organisation in 1968-69, when the yield from the motor vehicle tax increased to Rs. 237 lakhs from Rs. 33 lakhs in the previous year. The Bihar figures for these taxes for the period 1963-64 to 1974-75 cannot therefore be taken to reflect a normal trend. We have therefore computed two other sets of figures. For a shorter time period, 1968-69 to 1974-75 buoyancy and elasticity co-efficients for Bihar for these taxes worked out to 1.30 and 0.76; these are not only more in consonance with similar co-efficients for other States but also have a better explanatory power (the R^2 being 0.94 and 0.81 and the statistic being 9.21 and 4.58, respectively). Another set of co-efficients using a dummy variable for the period 1963-64 to 1974-75, having a value 0 from 1963-64 to 1967-68 and 1 from 1968-69 to 1974-75, gives buoyancy of 1.02 (R^2 0.96) and elasticity of 0.76 (R^2 0.89). A similar exercise with a dummy variable was also carried out, which yielded the buoyancy coefficient for the motor vehicle tax only of 1.08 (R^2 0.99).

Entertainment Tax

88. In a number of highly industrialised states the entertainment tax system is inelastic to changes in income (Table 14). The elasticity coefficient of entertainment tax in West Bengal and Maharashtra is 0.93 and 0.95 respectively and in Gujarat 0.47. On the other hand, the elasticity coefficient is quite high and above the all State average of 1.04 in the case of under developed States like Uttar Pradesh Orissa, Jammu & Kashmir and Bihar. These findings are contrary to expectations as the general belief is that the revenue from entertainment tax would increase with industrialisation and the general improvement in economic conditions.

89. The buoyancy coefficients are unusually high in Karnataka and Haryana (2.07 and 2.04) which also have a very high elasticity coefficients (1.88 and 1.80). Elasticity coefficient is less than unity in the case of Gujarat, Madhya Pradesh, Maharashtra and West Bengal. There were no discretionary changes in Kerala indicated by the identical values of buoyancy and elasticity co-efficients.

Concluding Observations

90. It is often stated that the taxes at the disposal of the State Governments are inelastic relatively

to those at the disposal of the Central Government. The findings of this study contradict this general impression. While, as we showed in the companion paper, the elasticity of the major indirect tax levied by the Centre, namely, Union excise, is clearly below unity, we find that, taking the States as a whole, their major indirect taxes including the sales taxes, the taxes on motor vehicles and on passengers and goods and the entertainment tax, have elasticities greater than unity.

91. As indicated in the note on sources of data in Annexure II for estimating net yield, we have relied upon the cumulative yields of additional tax measures supplied by the State government to the Planning Commission and the Finance Commissions. Elasticity estimates are naturally sensitive to the estimates of the yield of additional tax measures. When all States are taken together, there is a chance that over-and under-estimates may at least partly, cancel each other. Also, we have not been able to look carefully into the relevant factors that effect the yield of every indirect tax separately in every individual State. Sometimes, fortuitous factors such as a High Court judgment or an administrative change leads to a spurt or fall in revenue, which in turn affects the estimated automatic growth. In the aggregate, this influence is not likely to be so important, but in the case of particular States the results might get distorted. Hence we would like to caution that the elasticity excercises for the individual State should be looked upon more as preliminary ones that yield only tentative conclusion and indicate the lines of further enquiry. Subject to this caveat, we might make the following observations:

92. Generally speaking, the change in the yield of the indirect taxes covered by the study was more than proportionate to changes in State income, i.e., the buoyancy of taxes in the different States exceeds unity. The exceptions are sales tax on motor spirit and the taxes on motor vehicles and on passengers and goods in Assam, the sales tax on motor spirit in Orissa, the tax on motor vehicles in Jammu & Kashmir, the taxes on motor vehicles and on passengers and goods in Kerala, Tamil Nadu and Madhya Pradesh. Thus in 4 out of the 16 States, the taxes on vehicles and on passengers and goods did not grow as fast as State income inspite of discretionary tax increases in most of them.

93. In a good majority of States (13 and 12 out of 16), the elasticities of the general Sales tax and the entertainment tax are greater than unity. The performance of the motor spirit tax and the motor vehicles, passengers and goods taxes has not been as good. In fact, the elasticity of the latter groups is less than unity in as many as 9 out of the 16 States; and in the case of the former, elasticity is less than unity in 3 out of the 10 States for which computations have been made, and in 2 others it is negative. As regards the performance of particular States in West Bengal and Jammu & Kashmir three of the four taxes studied have proved to be inelastic though in the fourth case (motor vehicles and passenger and goods in the former and entertainment tax in the latter) the elasticity coefficient is significantly higher than the average of all the States taken together. In the case of Kerala and Madhya Pradesh two of the three taxes studied have inelastic systems, the exceptions being the entertainment tax in Kerala and the general sales tax in Madhya Pradesh. For two of the four taxes studied, elasticity is less than unity in Assam, Gujarat and Orissa. On the other hand, all the 4 taxes are elastic in the case of Uttar Pradesh, Punjab and Haryana and all the 3 studied in Bihar. Three of the four taxes studied are elastic in Tamil Nadu and Maharashtra and two of the three studied in Rajasthan, Karnataka and Andhra Pradesh.

94. Some important questions suggested by our findings are; First, why have the taxes on motor vehicles and on passengers and goods proved to be income inelastic? Is it because of the specific nature of the motor vehicles tax or is it due to large-scale evasion? Second, what are the causes of low elasticity in some States of taxes that have proved to be quite elastic in other States? Lastly, in a case like West Bengal, there must be special reasons that have made for the inelasticity of most of the direct taxes considered. These and other questions could be studied in detail if the States could gather and preserve adequate information on the nature of discretionary tax changes and the yield thereof.

ANNEXURE I

SOURCES OF DATA

Data on additional yield due to discretionary changes introduced in the Union excise taxes and import duties have been obtained from the Memorandum Explaining the Provisions of the Finance Bill. The major limitation with these data is that the figures are supposed to be ex ante estimates, and hence may or may not be equal to the actual realised figures. The Reserve Bank of India Bulletin also publishes data on additional revenue collected due to discretionary changes but these data, too, are ex ante in nature. To our knowledge, no ex post data are available. Data on import duties and excise revenue collected from each excisable item are available in the Explanatory Memorandum. Data on the value of importables has been taken from the Economic Survey. We have adopted the same groupings for commodities as in the Explanatory Memorandum. Data on the quantity produced and cleared of all excisable items have been obtained from the Statistical Year Book, Central Excise, Vol. I, issued by the Directorate of Statistics and Intelligence, Central Board of Excise & Customs. Price data of all the excisable items from 1963-64 onwards are not easily available. The most well known price statistics are the Index Numbers of Wholesale Prices in India (New Series) published monthly by the office of the Economic Adviser, Ministry of Industry and Civil Supplies. However, the prices of not all the excisable items are available in the monthly bulletin. Data on the value base, or assessed turnover, of the excisable commodities were compiled for us by the Directorate of Statistics and Intelligence, Central Board of Excise and Customs. For the construction of the indices of industrial production we have made use of two publications of the Central Statistical Organisation, namely, Monthly Production of Selected Industries and the Monthly Abstract of Statistics. National income figures have been taken from the National Accounts Statistics, 1960-61 to 1974-75, also published by the Central Statistical Organisation.

METHODOLOGY OF DERIVING HYPOTHETICAL TAX REVENUE SERIES TO REFLECT AUTOMATIC GROWTH IN REVENUE

Two methods are usually adopted to adjust the actual revenue series for the effects of discretionary changes. The first method, which we call the proportional adjustment method consists in making suitable adjustments to the actual revenue collected each year to arrive at the so called cleaned series. This involves two steps:

1. Substract from the actual yield of each year the estimated amount attributed to the discretionary change in that year;

2. Refine the series thus obtained to get the final series which would exclude the continuing impact of each discretionary change in future years.

Define the following :

T_j :actual tax yield in year j. j = 1...n.

D_j :effect of discretionary change in the jth year on the jth year's revenue outturn.

$T_{1,j}$:jth year's actual yield adjusted to the tax structure that existed in year 1.

We have

$$T_{1,1} = T_1$$

$$T_{1,2} = T_2 - D_2$$

$$T_{1,3} = T_{1,2} + \frac{(T_3 - D_3 - T_2)}{T_2} \cdot T_{1,2}$$

$$= \frac{(T_3 - D_3)}{T_2} T_{1,2}$$

In general we have

$$T_{1,j} = T_{1,j-1} + \frac{(T_j - D_j - T_{j-1})}{T_{j-1}} T_{1\,j-1}$$

$$= \frac{T_{j-1,j}}{T_{j-1}} \quad T_{1,j-1}$$

$$= \frac{T_{j-1,j}}{T_{j-1}} \quad \frac{T_{j-2,j-1}}{T_{j-2}} \quad \cdots \quad \frac{T_{3,4}}{T_3} \quad \frac{T_{2,3}}{T_2} \quad T_{1,2}$$

If we have $i = 1$, then making use of the above procedure, we can obtain the series $T_{1,1}\ T_{1,2}\ \cdots\ T_{1,n}$. This cleaned series may then be regressed on national income or other base variables to obtain the corresponding elasticities.

It must be mentioned, however, that the proportional adjustment method suffers from certain important limitations. First, the hypothetical yield series does not give the tax yield based on the rate structure of a given year but rather a series based on an average rate structure of all the years in the reference period*. Secondly, if the ratio of the additional revenue due to discretionary changes and the total excise revenue collected has a wide variance, then the proportional adjustment method might break down. Thirdly, if increases in taxes themselves affect the automatic growth in revenue, then again, the method is likely to give misleading results.

The second method is called the constant rate base method. Under this method, an attempt is made to derive a series on the size of the tax base in the different years according to an unchanged legal difinition of the base of the tax. One of the years (usually the first) is chosen as the base year and that year's tax rate is then applied to the base series to derive the hypothetical revenue series to represent automatic growth. To apply this method in the case of excise duties, what we need to do is first to obtain the quantities cleared in each of the years of all the excisable items chosen for study. It is necessary that data on quantity cleared should be disaggregated according to rate categories. If such data are available then in the case of commodities subject to specific duties the legal rates in the base year could be applied to the respective quantities cleared. If the different qualities or types of products subject to different rates are lumped together in the data on quantities cleared, then one is forced to compute an average effective rate for different qualities of a product taken together, and such an average rate in the base year could be applied to quantities cleared of that product in other years. This procedure would be valid only on the assumption that the weights of the different varieties of products did not change during the reference period.

In case of commodities subject to ad valorem duties, it is obviously necessary to obtain the value of clearance of different excisable commodities. If this information is not available in the statistics published by the Department of Revenue (and this happens to be true in most cases of ad valorem duties), one has to collect data on ex-factory prices of the goods concerned to compute

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* Chelliah, Raja J, and Chand, Sheetal K. (1974) have proved that the estimate of elasticity will be the same whether we choose year 1, or n, or indeed any intermediate year j, as the base year.

the value bases. The ad valorem rates of the base year could then be applied to the estimated values of clearance. Here again, unless we are able to obtain or work out the value of clearance separately for each type of product subject to differential duties, the legal rates cannot be applied and we would have to make use of average effective rates in the base year.

If tax base data, i.e. data on the quantity or value of clearance, are available or can be computed, then we could calculate not only the elasticity of the tax with reference to national income, but also (a) the elasticity of the tax with reference to the base and (b) the elasticity of the base with reference to national income. In symbols, we have

Q_i^j : Quantity cleared of excisable item j in year i,
$i = 1 \ldots n, \quad J = 1 \ldots m.$

P_i^j : Price of the excisable item j in year i,

t_i^j : Specific tax rate on excisable item j in year i

a_i^j : ad valorem tax rate on excisable item j in year i.

Specific Tax

$$T_i^s = \sum_{j=1}^{K} t_i^j \quad Q_i^j, \quad i = 1 \ldots n:$$

Denotes the total revenue collected from a particular group, where k is the number of items in the group.

Ad Valorem Tax:

$$T_i^a = \sum_{j=1}^{k} a_i^j \; P_i^j \; Q_i^j, \quad i = 1 \ldots n,$$

Denotes the total revenue collected from a group, where k is the number of items in the group.

If a group consists of some items i...r having specific tax and the remaining items r+1..k having ad valorem tax then the revenue yield may be denoted thus:

$$T_1^{as} = \sum_{j=1}^{r} t_1^j \; Q_i^j + \sum_{j=r+1}^{k} a_i^j \; P_i^j \; Q_i^j \qquad i = 1 \ldots n$$

The tax yield in each of the above cases may be regressed on the value base, $\sum_{j=1}^{k} P_i^j \; Q_1^j$, and the value base, in turn, may be regressed on national income. In the event

of low elasticity of tax yield of a particular group to the national income, we would be able to determine whether the low rate of increase of tax yield is due to the low rate of increase of the base or whether it is due to an inherently 'regressive' tax structure. In a situation where most of the taxes within a group are of the specific type and we observe that the rate of increase of tax yield is very low compared to the rate of increase of tax base, then there is a good case for switching over to ad valorem taxes.

ANNEXURE - III

Method of Adjustments for Discretionary changes used in Relation to Planning Commission Data*.

The period covered in the study is 1963-64 to 1974-75. The data on the effect of discretionary changes are available according to sub-periods: 1964-65 to 1968-69, 1969-70 to 1973-74 and 1974-75 to 1976-77 on different base levels of taxation. We have to work out the hypothetical growth of the cumulative yield due to discretionary changes in the terminal year of one period over the years of the succeeding periods in order to obtain the series of tax yield due to discretionary changes with 1963-64 as the base year. If the cumulative yield due to discretionary measures undertaken in different years is deducted from the actual yield, the residual is the hypothetical yield adjusted to the rates and exemp tions structure of the base year.

Symbolically,

T_i = Actual tax yield in year i

D_i (J, M) = Effect of discretionary changes introduced from year J to year M in year i.

T_{ij} = Tax Revenue in year j and adjusted to the structure of year i.

The method of derivation of the hypothetical tax series is demonstrated in Table B. In column 1 yearly actual tax yields for the period 1963-64 to 1975-76, i.e., T_i (i=o.....12) are given. In columns 5, 4 and 3 respectively, changes introduce from year 1 to year 5 in year 5, from year 6 to year 10 in year 10 and from 11 to year 12 in year 12 are given along with the growth of cumulative yield due to discretionary measures, i.e. D_i (J, M) where J is the first year and M is the last year of the period. In column 2 the tax yields adjusted to the given base structure, i.e., $T_{5,j}$ and $T_{10,j}$ are given. In column 6 tax revenue in year j adjusted to the structure of year O(1963-64) is given.

The general formula for constructing the series of hypothetical tax yield adjusted to the structure of year O can be given as below:

The total period beginning from year O to n can be divided into m-sub-periods.

$$(1, M_1), (M_1 + 1, M_2) \ldots\ldots\ldots (M_{m-1} + 1, M_m)$$

Adjusted tax revenue for any year j ($T_{o,j}$) where the last series for cumulative effects of discretionary changes starts from year (M_k + 1) with $j \geq (M_k + 1)$ can be derived by

$$T_{o,j} = T_j - D_j (1, M_1) - D_j (M_1 + 1, M_2) \ldots\ldots\ldots\ldots D_j (M_k + 1, j)$$

*This method has been used in the case of taxes on motor vehicles and on passengers and goods.

TABLE B

METHOD OF COMPUTING THE HYPOTHETICAL TAX YIELD

Actual tax yield	Tax yield adjusted to given base year.	Cumulative Effect of Discretionary changes beginning year-			Hypothetical tax yield adjusted to the structure of year 0
		Year 11	Year 6	Year 1	
1	2	3	4	5	6
T_0					$T_{0,0}=T_0$
T_1				$D_1(1,1)$	$T_{0,1}=T_1-D_1(1,1)$
T_2				$D_2(1,2)$	$T_{0,2}=T_2-D_2(1,2)$
T_3				$D_3(1,3)$	$T_{0,3}=T_3-D_3(1,3)$
T_4				$D_4(1,4)$	$T_{0,4}=T_4-D_4(1,4)$
T_5				$D_5(1,5)$	$T_{0,5}=T_5-D_5(1,5)$
T_6	$T_{5,6}=T_6-D_6(6,6)$	$D_6(6,6)$		$D_6(1,5)=D_5(1,5).\frac{T_{5,6}}{T_5}$	$T_{0,6}=T_{5,6}-D_6(1,5)$
T_7	$T_{5,7}=T_7-D_7(6,7)$	$D_7(6,7)$		$D_7(1,5)=D_6(1,5).\frac{T_{5,7}}{T_6}$	$T_{0,7}=T_{5,7}-D_7(1,5)$
T_8	$T_{5,8}=T_8-D_8(6,8)$	$D_8(6,8)$		$D_8(1,5)=D_7(1,5).\frac{T_{5,8}}{T_7}$	$T_{0,8}=T_{5,8}-D_8(1,5)$
T_9	$T_{5,9}=T_9-D_9(6,9)$	$D_9(6,9)$		$D_9(1,5)=D_8(1,5).\frac{T_{5,9}}{T_8}$	$T_{0,9}=T_{5,9}-D_9(1,5)$
T_{10}	$T_{5,10}=T_{10}-D_{10}(6,10)$	$D_{10}(6,10)$		$D_{10}(1,5)=D_9(1,5).\frac{T_{5,10}}{T_9}$	$T_{0,10}=T_{5,10}-D_{10}(1,5)$
T_{11}	$T_{10,11}=T_{11}-D_{11}(11,11)$	$D_{11}(11,11)$	$D_{11}(6,10)=D_{10}(6,10).\frac{T_{10,11}}{T_{10}}$	$D_{11}(1,5)=D_{10}(1,5).\frac{T_{10,11}}{T_{10}}$	$T_{0,11}=T_{10,11}-D_{11}(1,5)-D_{11}(1,10)$
T_{12}	$T_{10,12}=T_{12}-D_{12}(11,12)$	$D_{12}(11,12)$	$D_{12}(6,10)=D_{11}(6,10).\frac{T_{10,12}}{T_{11}}$	$D_{12}(1,5)=D_{11}(1,5).\frac{T_{10,12}}{T_{11}}$	$T_{0,12}=T_{10,12}-D_{12}(1,5)-D_{12}(6,10)$

ANNEXURE IV

SOURCES OF DATA

Data on three items were needed for the study; State income, tax yield and yield due to additional tax measures. Various sources of data were examined to collect the necessary information.

The major sources of data on tax yield due to additional tax measures are the 'Forecast of Financial Resources' submitted by the State Governments to the Planning Commission and the 'Memoranda' submitted by the State Governments to the various Finance Commissions. The first document provides data on a cumulative basis relating to specified periods with different years as bases. Additional tax yield data are available for the period 1964-65 to 1968-69 with 1964-65 as the base, for the period 1969-70 to 1973-74 with 1969-70 as the base and for the period 1974-75 to 1976-77 with 1974-75 as the base. These forecasts, however, do not relate to all taxes and for all the years; hence some data gaps arise. These gaps were filled in through data from other sources, namely:

(i) Data provided by the States themselves on a cumulative basis for additional tax yield, period wise as well as year-wise.

(ii) Explanatory memoranda to State budgets and budget speeches of Finance Ministers.

(iii) Studies on State Finances in the Reserve Bank of India Bulletins.

Tax yield data were mainly obtained from State budget documents. State income data were obtained from Central Statistical Organisation, who in turn gather these data from the Directorates of Economics and Statistics in the States.

Table 1

Proportion of Union Excise Duties in Central Taxes and in National Income

(In crores of rupees)

Year	Union excise duty	Central taxes	National income at current prices	Union excise duty as % of central taxes	Union excise duty as % of national income
1950-51	68	405	9530	16.8	0.7
1960-61	416	895	13263	46.5	3.1
1965-66	898	2061	20636	43.6	4.4
1966-67	1034	2307	23883	44.8	4.3
1967-68	1148	2353	28102	48.8	4.1
1968-69	1321	2510	28729	52.6	4.6
1969-70	1524	2823	31770	54.0	4.8
1970-71	1759	3207	34476	55.8	5.1
1971-72	2061	3872	36535	53.2	5.6
1972-73	2324	4505	39573	51.6	5.9
1973-74	2602	5070	49148	51.3	5.3
1974-75	3231	6322	60120	51.1	5.4
1975-76	3824	7470	62525	51.2	6.1

Source: Indian Economic Statistics Part II, Public Finance, Government of India, Ministry of Finance, Department of Economic Affairs, September 1976.

Table 2

Trends in Excise Duty Collections from Major Groups of Commodities

(in crores of rupees)

Groups	1963-64	1965-66	1970-71	1975-76	Compound rate of growth of revenue between 1963-64 & 1975-76 (in percentage)
Total excise taxes collected of which	729.58 (100)	897.92 (100)	1791.44 (100)	3823.62 (100)	14.8
A: Food & beverages	69.94 (6.5)	73.01 (8.1)	161.93 (9.0)	270.90 (7.1)	11.9
B: Tobacco	80.66 (11.1)	98.88 (11.0)	202.41 (11.3)	307.52 (8.0)	11.8
C: Petroleum products	201.77 (27.6)	272.78 (30.4)	608.18 (34.0)	1030.00 (26.9)	14.6
D: Vegetable oils and fats	15.96 (2.1)	8.55 (1.0)	15.00 (.8)	21.50 (.6)	2.5
E: Chemicals	25.96 (3.6)	31.93 (3.6)	95.03 (5.3)	287.91 (7.5)	22.2
F: Metals:					
(a) Iron & steel	44.67 (6.1)	77.52 (8.6)	85.97 (4.8)	156.75 (4.1)	11.0
(b) Non-ferrous metals	2.27 (.3)	8.70 (1.0)	40.09 (2.2)	82.80 (2.2)	34.9
G: Manufactured goods:					
(a) textiles	99.17 (13.6)	108.48 (12.1)	218.13 (12.2)	485.84 (12.7)	14.2
(b) other manufactured goods	100.92 (13.8)	113.05 (12.6)	184.43 (10.3)	431.71 (11.3)	12.9
H: Machinery and transport equipment	33.69 (4.6)	42.54 (4.7)	80.36 (4.5)	218.25 (5.7)	

N.B. Figures in brackets denote the percentage to the total.

Source: Explanatory Memorandum on the budgets of the Central Government for various years.

Table 3

Estimated Values of Production of Excisable Commodities *

(In crores of rupees)

	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	Average annual compound growth rate per cent
All commodities	6612.80	7674.02	8492.24	9837.71	13585.82	19192.14	23.75
A: Food & beverages	936.06	1005.62	1096.98	1243.56	1395.22	1720.93	12.93
B: Tobacco	242.93	259.67	283.10	310.44	384.43	759.14	25.59
C: Petroleum products	314.36	436.26	509.49	754.31	1582.57	1774.50	41.36
D: Vegetable oils & fats	361.34	367.21	447.79	477.32	483.85	508.37	7.07
E: Chemicals	784.24	921.06	1070.65	1157.53	1615.81	1920.66	19.62
F: Metals:							
(a) iron & steel	451.55	618.16	705.76	789.08	1176.31	1258.81	22.76
(b) non-ferrous metals	159.95	167.75	174.02	193.19	203.43	297.43	13.21
G: Manufactured goods:							
(a) textiles & Jute	1943.98	2105.75	2209.60	2715.69	3742.43	4626.67	18.94
(b) other manufactured goods	753.07	842.79	950.13	1033.03	1439.90	1583.48	16.03
H: Machinery & transport equipment	665.32	949.75	1044.72	1183.56	1561.87	4742.15	48.11

* The figures given here do not include excise duties. Source: Central Board of Excise & Customs.

Table 4

Estimated Proportions Of Ad Valorem And Specific Taxes

(for 1965-66, 1970-71 and 1974-75)

	1965-66			1970-71			1974-75		
	Commodities subjected to ad valorem rates of duty.	Commodities subjected to ad valorem and specific rates of duty.	Commodities subjected to specific rates of duty	Commodities subjected to ad valorem rates and duty	Commodities subjected to ad valorem and specific rates of duty	Commodities subjected to specific rates of duty	Commodities subjected to ad valorem rates of duty	Commodities subjected to ad valorem and specific rates of duty	Commodities subjected to specific rates of duty
Total excise duties	15.8	4.1	80.1	37.0	3.6	59.4	36.4	1.7	61.9
A: Food and beverages	-	-	100.0	78.9	-	21.1	82.8	-	17.2
B: Tobacco	47.2	-	52.8	73.0	-	27.0	71.5	-	28.5
C: Petroleum Products	4.6	-	95.4	-	-	100.0	-	-	100.0
D: Vegetable oils and fats	-	-	100.0	92.8	-	7.2	93.6	-	6.4
E: Chemicals	69.2		30.8	92.7	-	7.3	96.3	-	3.7
F: Metals:									
(a) Iron and Steel	-	-	100.0	56.1	-	43.9	46.5	-	53.5
(b) Non-ferrous metals	26.1	-	73.9	83.7	-	16.3	75.1	-	24.9
G: Manufactures:									
(a) Textiles and jute	2.0	4.1	93.9	1.3	6.0	92.7	0.5	6.2	93.3
(b) Other manufactured goods	12.0	-	88.0	57.4	-	42.6	66.4	-	33.6
H: Machinery and transport equipment	45.5	46.8	7.7	64.9	35.1	-	100.00	-	-

Source: 1) Explanatory Memorandum on the Budget of the Central Government for various years.

2) Indian Customs and Central Excise Tariff, Volume-II, Department of Commercial Intelligence and Statistics, Calcutta.

Table 5

Estimated Values of Production Excisable Commodities for 1970-71 & 1974-75

(Classified by goods subject to specific and advalorem rates of duty)

(In crores of rupees)

	1970-71 5/			1974-75 5/		
	Commodities having ad valorem rates of duty	Commodities having specific rates of duty	All commodities	Commodities having ad valorem rates of duty	Commodities having specific rates of duty	All Commodities
All excisable commodities	2456.65 (37.1)	4180.80 (48.1)	6612.80	5140.19 (37.8)	6807.39 (50.1)	13585.82
A: Food and beverages	122.46 (13.1)	813.60 (86.9)	936.06	226.22 (16.2)	1169.00 (83.8)	1395.22
B: Tobacco	127.20 (52.4)	115.73 (47.64)	242.93	196.77 (51.2)	187.66 (48.8)	384.43
C: Petroleum products	-	314.36 1/ (100.0)	314.36	-	1582.57 1/ (100.0)	1582.57
D: Vegetable oils and fats	310.94 (86.1)	50.40 (13.9)	361.34	362.38 (74.9)	121.47 (25.1)	483.86
E: Chemicals	725.27 (92.5)	58.97 (7.5)	784.24	1501.33 (92.9)	114.48 (7.1)	1615.81
F: Metals						
(a) iron and steel	105.61 (23.4)	345.94 (76.6)	451.55	176.72 (16.0)	990.59 (85.0)	1176.31
(b) non-ferrous metals	102.57 (64.1)	57.38 (35.9)		112.64 (55.4)	90.79 (44.6)	203.43
G: Manufactured goods						
(a) textiles and jute	35.54 (1.8)	1169.65 (60.2)	1943.98 1/	44.70 (1.2)	2062.48 (55.1)	3742.43 2/
(b) other manufacture goods	498.20 (66.2)	254.87 (33.8)	753.07	960.55 (66.7)	479.35 (33.3)	1439.90
H: Machinery and transport equipment	428.86 (64.5)	-	665.32 3/	1561.87 (100.0)		1561.87

1/ Includes Rs.738.89 crores value of the commodities on which both specific and ad valorem rates of duty are applicable.
2/ Includes Rs.1635.25 crores value of the commodities on which both specific and ad valorem rates of duty are applicable.
3/ Includes Rs.286.46 crores value of the commodities on which both specific and ad valorem rates of duty are applicable.
4/ Includes Rs. the value of a few petroleum products on which ad valorem rates of duty are applicable.
5/ Figures in brackets give the percentage the value of commodities subjected to ad valorem and specific taxes to the value of all commodities in the group

Source: Central Board of Excise and Customs.

Table 6

Relative Share of the Major Groups in Import Duties Collected

(In crores of rupees)

	1963-64	1964-65	1965-66	1966-67	1967-68	1968-69	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76
Total import duties collected of which	334.25 (100)	404.64 (100)	547.69 (100)	462.37 (100)	392.9 (100)	343.08 (100)	306.29 (100)	391.95 (100)	611.51 (100)	755.88 (100)	895.16 (100)	1194.10 (100)	1949.05 (100)
Petroleum products	72.83 (21.79)	81.46 (20.13)	83.30 (15.21)	64.54 (13.96)	32.04 (8.37)	34.21 (9.97)	33.09 (10.80)	29.73 (7.59)	62.60 (10.14)	80.19 (10.61)	96.03 (10.73)	96.86 (8.63)	96.00 (7.69)
Chemicals	17.36 (5.19)	19.07 (4.71)	26.63 (4.90)	26.97 (5.83)	29.71 (7.76)	30.29 (8.83)	35.05 (11.44)	43.16 (11.01)	55.27 (9.04)	76.54 (10.13)	113.34 (12.66)	181.85 (15.25)	118.36 (9.48)
Iron and steel	27.76 (8.31)	37 47 (9.26)	62.31 (11.38)	48.58 (10.51)	46.84 (12.83)	37.91 (11.05)	33.62 (10.98)	56.01 (14.29)	117.99 (19.29)	122.95 (16.27)	138.60 (15.48)	211.18 (17.69)	150.00 (12.02)
Non ferrous metals	3.15 (0.94)	3.44 (0.85)	13.32 (2.43)	13.72 (2.97)	12.83 (3.35)	12.68 (3.70)	9.32 (3.04)	18.11 (4.62)	26.35 (4.31)	30.58 (4.05)	38.73 (4.33)	47.89 (4.01)	X
Textiles and jute	13.84 (4.14)	20.59 (5.09)	19.21 (3.51)	14.53 (3.14)	12.06 (3.15)	8.20 (2.39)	4.96 (1.62)	15.59 (3.98)	9.22 (1.51)	15.54 (2.06)	22.45 (2.51)	29.01 (2.43)	47.20 (3.78)
Manufactured goods other than textiles	5.96 (1.78)	7.21 (1.78)	11.84 (2.16)	11.43 (2.47)	10.48 (2.74)	6.73 (1.96)	8.23 (2.69)	8.59 (2.19)	11.45 (1.87)	18.59 (2.46)	21.51 (2.40)	36.04 (3.02)	43.70 (3.50)
Machinery and transport equipment	99.44 (29.75)	128.87 (31.85)	152.78 (27.90)	157.73 (34.12)	129.76 (33.89)	132.27 (38.56)	104.79 (34.21)	105.94 (27.03)	152.31 (24.91)	183.75 (24.31)	243.95 (27.25)	267.06 (22.26)	326.10 (26.13)

N.B.: Figures in brackets refer to percentage to total

Sources: Explanatary Memorandum, Government of India, 1963-64 to 1975-76.

Table 7

Average Incidence Of Import Duties, 1963-64 to 1975-76

(In crores of rupees)

Item	Pre Devaluation Parity			Post Devaluation Parity										
	1963-64	1964-65	1965-66	1965-66	1966-67	1967-68	1968-69	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76
Total Imports	1290.7	1349	1349	2218.4	2078.4	2007.6	1861.6	1582.1	1634.2	1884.6	1867.4	2955.4	4468.1	5157.8
Deduct non-dutiable imports of														
(i) Food	198.7	282.1	309.1	607.2	651	618.2	336.6	261	213	131.2	80.8	473.1	763.8	1338.3
(ii) Fertilisers	13.2	28.9	38.9	81.4	124.9	209.5	198.1	117.3	99.9	111.3	146.7	226.8	577.9	556.3
Dutiable imports (estimates)	1013.8	1038	1049	1629.8	1302.5	1279.9	1326.9	1203.8	1321.3	1582.0	1640.9	2255.5	3126.4	3263.2
Total net import duty revenue	334.25	404.64	547.69	547.69	462.34	352.90	343.08	306.29	391.95	611.51	755.88	895.16	1194.1	1218.05
Average import duty as dutiable imports, %	32.81	38.98	52.36	33.6	35.5	29.9	25.9	25.4	29.7	38.7	46.1	39.7	38.2	38.8

Sources: 1/ Explanatary Memorandum, Union Excise 1963-64 to 1975-76.

2/ Monthly Statistics of Foreign Trade DGC I&S

Table 8

Trends and Composition of Revenue from State Indirect Taxes (All States)
(1960-61 - 1974-75)

(in crores of rupees)

	General sales tax	Central sales tax	Sales tax on motor spirit	Purchase tax on sugarcane	State excise	Tax on motor vehicles	Tax on passen-gers & goods	Electricity duty	Entertain-ment tax	Other taxes & duties	Total taxes on commodities & services
1960-61	124.88*	-	11.41	4.43	53.68	35.06	4.51	13.26	13.35	34.99	295.57
	(42.25)		(3.86)	(1.50)	(18.16)	(11.08)	(1.53)	(4.49)	(4.52)	(11.84)	(100.00)
1965-66	276.87*	-	23.59	10.65	95.46	73.23	28.29	37.56	29.52	65.35	640.52
	(43.23)		(3.68)	(1.66)	(14.90)	(11.43)	(4.42)	(5.86)	(4.61)	(10.20)	(100.00)
1970-71	559.06	158.38	41.70	11.10	203.56	105.41	66.98	69.87	57.41	1.31	1274.58
	(43.86)	(12.43)	(3.27)	(0.87)	(15.97)	(8.27)	(5.26)	(5.47)	(4.50)	(0.10)	(100.00)
1971-72	639.41	159.25	45.26	10.89	233.73	113.10	84.37	75.10	69.93	128.03	1559.07
	(41.01)	(10.21)	(2.90)	(0.70)	(14.99)	(7.25)	(5.41)	(4.82)	(4.49)	(8.21)	(100.00)
1972-73	732.46	202.98	55.82	16.71	278.67	127.16	99.24	81.79	87.89	122.36	1805.08
	(40.58)	(11.24)	(3.09)	(0.93)	(15.44)	(7.04)	(5.50)	(4.53)	(4.87)	(6.78)	(100.00)
1973-74	842.51	212.21	67.64	18.43	352.64	148.04	118.41	81.82	97.78	162.50	2105.58
	(40.01)	(10.08)	(3.21)	(0.88)	(16.75)	(7.03)	(5.62)	(3.89)	(4.64)	(7.72)	(100.00)
1974-75	1165.79	300.77	88.51	30.30	386.36	185.54	138.93	91.30	117.75	20.62	2525.87
	(46.15)	(11.91)	(3.50)	(1.20)	(15.30)	(7.35)	(5.50)	(3.61)	(4.66)	(0.82)	(100.00)

Notes: 1. Figures in brackets are percentages to totals.
2. Figures of 'other taxes and duties' are not comparable year to year due to change in classification from time to time.
*includes Central Sales tax

Sources: (a) Budget of the State Governments;
(b) Reserve Bank of India Bulletins.

Table 9

Components of Sales Taxation

(in crores of rupees)

	General Sales Tax	Central Sales Tax	Sales Tax on Motor Spirit	Purchase Tax on Sugarcane	Total Sales Tax
1970-71	559.06 (72.58)	158.38 (20.56)	41.70 (5.42)	11.10 (1.44)	770.24 (100.00)
1971-72	639.41 (74.80)	159.25 (18.63)	45.26 (5.30)	10.89 (1.27)	854.81 (100.00)
1972-73	732.46 (72.67)	202.98 (20.14)	55.82 (5.53)	16.71 (1.66)	1007.97 (100.00)
1973-74	842.51 (73.85)	212.21 (18.60)	67.64 (5.93)	18.43 (1.62)	1140.79 (100.00)
1974-75	1165.79 (73.53)	300.77 (18.97)	88.51 (5.58)	30.30 (1.91)	1585.37 (100.00)

Note: Figures in brackets are percentages to totals.

Source: Same as for Table 1.

Table 10

Buoyancy And Elasticity Of Selected Indirect Taxes (All States)
(1963–64 to 1974–75)

	Buoyancy	R^2	Elasticity	R^2
General sales tax (including sales tax on motor spirit)	1.43 (1.44)	0.97 (0.93)	1.15 (1.23)	0.99 (0.99)
Entertainment tax	1.43 (1.54)	0.96 (0.94)	1.04 (1.18)	0.96 (0.92)
Taxes on motor vehicles and on passengers and goods.**	1.27	0.98	1.05	0.97

Note: All t values are highly significant.

* Relates to 14 major States, excluding Punjab, Haryana and Himachal Pradesh. Figures in Parenthesis relate to 16 States including Punjab and Haryana for the period 1968–69 to 1975–76.

** Relates to 18 States for the period 1963–64 to 1973–74.

Estimates of elasticity for General sales tax and Entertainment tax are based on the net yields derived from proportional adjustment method while estimates of elasticity for taxes on motor vehicles and on passengers and goods have been worked out using net yields derived from a variant of proportional adjustment method.

Table 11

Buoyancy And Elasticity of General Sales Tax For Individual States (1963-64 - 1975-76)

	Buoyancy	R^2	Elasticity	R^2
Andhra Pradesh	1.42*	0.97	1.26*	0.96
Assam	1.61	0.91	1.52	0.90
Bihar 1/	1.16*	0.94	1.01*	0.94
Gujarat 1/	1.48	0.94	1.08	0.93
Haryana 2/	1.53	0.93	1.48	0.92
Jammu & Kashmir 1	1.86	0.92	0.97	0.80
Karnataka	1.82*	0.97	1.40*	0.97
Kerala 1/	1.22*	0.98	0.99*	0.98
Madhya Pradesh	1.40*	0.94	1.12*	0.94
Maharashtra	1.40	0.99	1.18	0.99
Orissa	1.25	0.96	1.08	0.97
Punjab 2/, 3/	1.47	0.92	1.47	0.92
Rajasthan 1/	1.38*	0.93	1.19*	0.93
Tamil Nadu	1.67	0.98	1.40	0.99
Uttar Pradesh	1.70	0.94	1.46	0.94
West Bengal	1.33	0.96	0.85	0.83

Note All t values are highly significant.

* Figures include General Sales Tax, central sales tax and sales tax on motor spirit. In others, sales tax on motor spirit is not included.

1/ 1963-64 to 1974-75

2/ 1967-68 to 1974-75

3/ There were no discretionary changes.

The estimates of elasticity are based on the net yields derived from proportional adjustment method.

Table 12

Buoyancy and Elasticity of Sales Tax on Motor Spirit for Individual States (1963-64 to 1975-76)

State	Buoyancy	R^2	t	Elasticity	R^2	t
Andhra Pradesh*	-	-	-	-	-	-
Assam	0.85	0.62	4.24	0.50	0.37	2.52
Bihar*	-	-	-	-	-	-
Gujarat**	1.62	0.91	10.32	0.29	0.41	2.61
Haryana***	1.62	0.86	6.18	1.33	0.94	9.44
Jammu & Kashmir**	-0.14	0.02	-0.47	-0.30	0.09	-1.02
Karnataka*	-	-	-	-	-	-
Kerala*	-	-	-	-	-	-
Madhya Pradesh*	-	-	-	-	-	-
Maharashtra	1.23	0.98	20.89	1.08	0.96	23.23
Orissa	0.48	0.33	2.30	-0.95	0.57	-3.81
Punjab***	1.84	0.90	7.43	1.50	0.86	6.16
Rajasthan*	-	-	-	-	-	-
Tamil Nadu	1.77	0.98	21.95	1.16	0.91	10.77
Uttar Pradesh	1.63	0.95	14.33	1.21	0.91	10.36
West Bengal	1.29	0.94	13.46	0.26	0.11	1.16

Notes: * Included with general sales tax and central sales tax.

** 1963-64 to 1974-75

*** 1967-68 to 1974-75

The estimates of elasticity are based on the net yields derived from proportional adjustment method.

Table 13

Buoyancy And Elasticity of Taxes on Motor Vehicles and on Passenger And Goods For Individual States (1963-64 to 1974-75)

State	Buoyancy	R^2	Elasticity	R^2
Andhra Pradesh	1.34	0.92	0.99	0.91
Assam	0.50	0.80	0.25	0.56
Bihar	2.36	0.79	2.18	0.71
Gujarat 1/	1.32	0.91	1.16	0.91
Haryana 2/	1.86	0.91	1.32	0.93
Jammu & Kashmir 1/	0.98*	0.74*	0.39*+	0.34*
	1.59**	0.85**		
Karnataka 3/	1.00	0.95	0.92	0.94
Kerala 1/	0.73	0.90	0.48	0.84
Madhya Pradesh 1/	0.91	0.95	0.91	0.75
Maharashtra	1.31	0.99	1.04	0.99
Orissa 1/	1.16	0.94	0.83	0.95
Punjab 2/	1.69	0.94	1.16	0.89
Rajasthan	1.30	0.92	0.98	0.90
Tamil Nadu	0.97	0.96	0.68	0.91
Uttar Pradesh	1.38	0.96	1.02	0.94
West Bengal	1.63	0.52	1.53	0.48

Note

\+ In the case of motor vehicles tax t value not significant at 5 per cent probability level. All other t values are significant.

* Tax on motor vehicles.

** Tax or passengers and goods,

1/ 1963-64 to 1973-74

2/ 1967-68 to 1973-74

3/ 1964-65 to 1974-75

The estimates of elasticity are based on the net yield derived from a variant of proportional adjustment method.

Table 14

Buoyancy and Elasticity of Entertainment Tax for Individual States - (1963-64 to 1975-76)

State	Buoyancy	R^2	t	Elasticity	R^2	t
Andhra Pradesh	1.71	0.96	16.07	1.32	0.96	16.30
Assam	1.39	0.79	6.37	1.03	0.75	5.78
Bihar*	1.26	0.71	4.92	1.18	0.69	4.70
Gujarat*	1.54	0.91	9.89	0.47	0.41	2.66
Haryana**	2.04	0.94	0.86	1.80	0.94	9.80
Jammu & Kashmir*	1.70	0.78	5.88	1.25	0.06	4.26
Karnataka	2.07	0.99	29.21	1.88	0.99	32.62
Kerala *, ***	1.11	0.81	6.43	1.11	0.81	6.43
Madhya Pradesh	1.30	0.93	12.01	0.68	0.77	6.09
Maharashtra	1.47	0.98	25.84	0.95	0.95	13.86
Orissa	1.38	0.92	11.60	1.22	0.93	12.31
Punjab**	1.77	0.94	9.45	1.17	0.90	7.22
Rajasthan*	1.41	0.91	9.76	1.02	0.86	7.83
Tamil Nadu	1.36	0.98	25.33	1.20	0.99	31.67
Uttar Pradesh	1.61	0.95	14.16	1.06	0.90	10.02
West Bengal	1.48	0.92	11.40	0.93	0.89	9.13

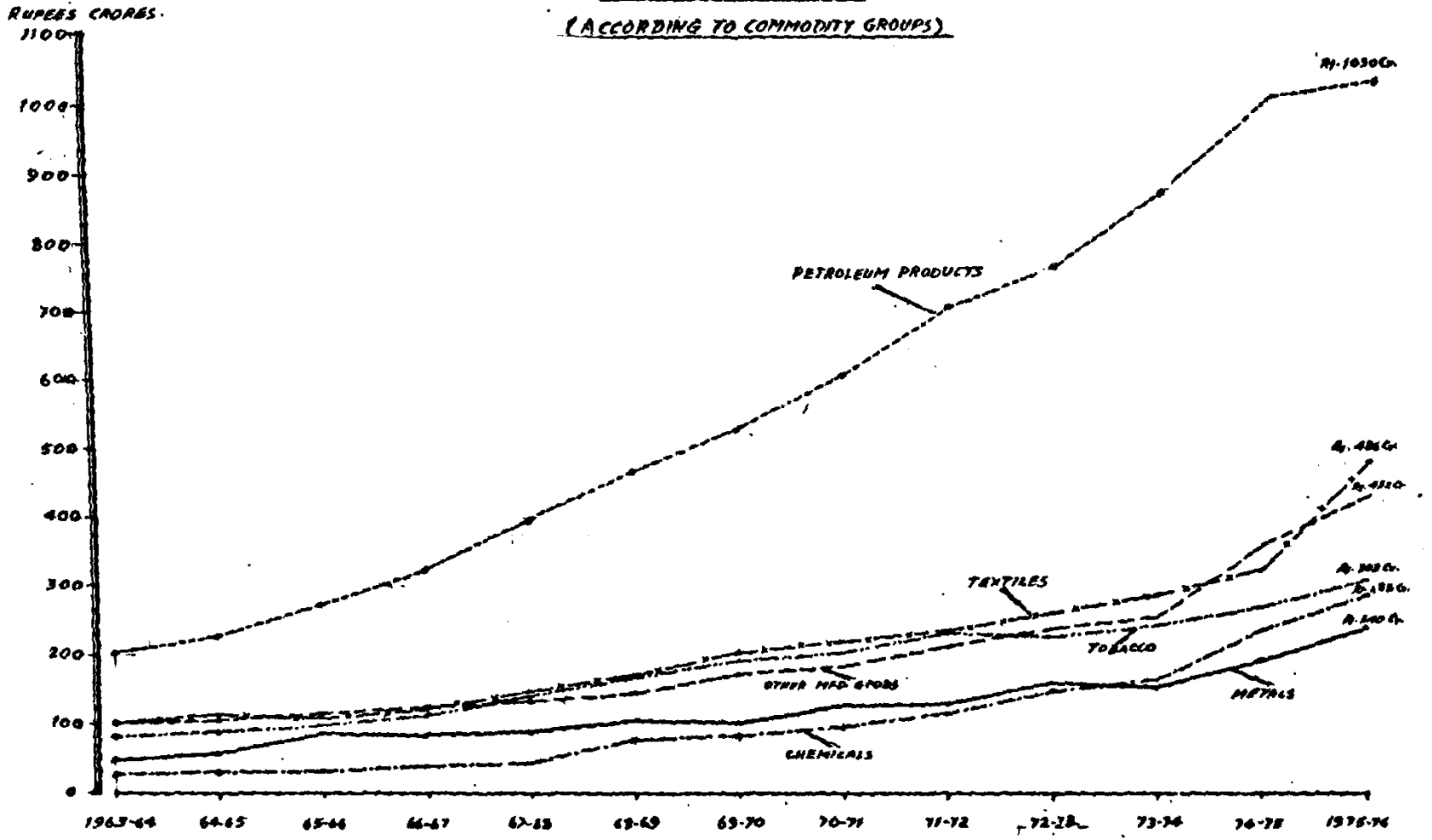
* 1963-64 to 1974-75

** 1967-68 to 1974-75

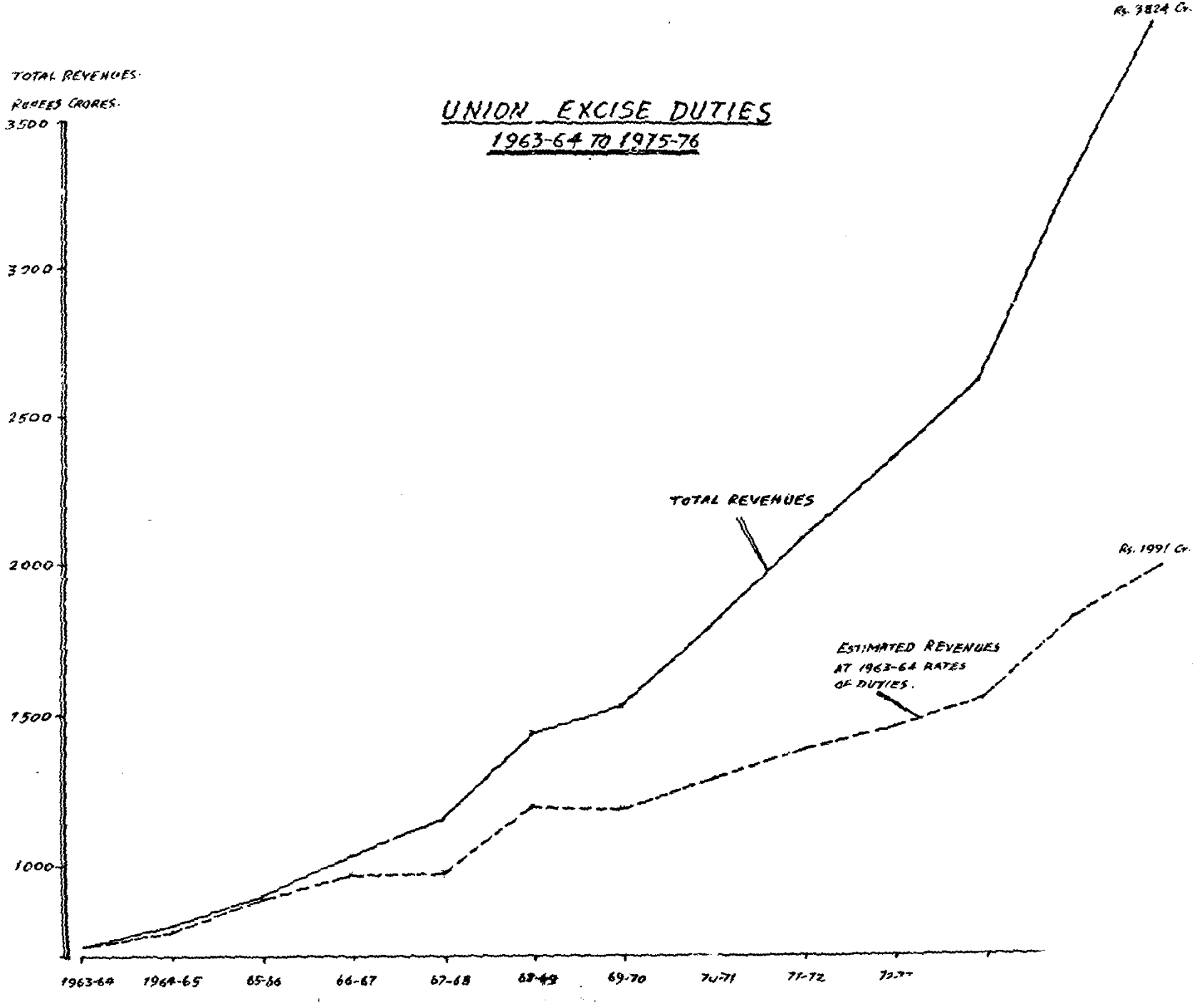
*** There were no discretionary changes of tax base and tax rate.

The estimates of elasticity are based on the net yields derived from proportional adjustment: method.

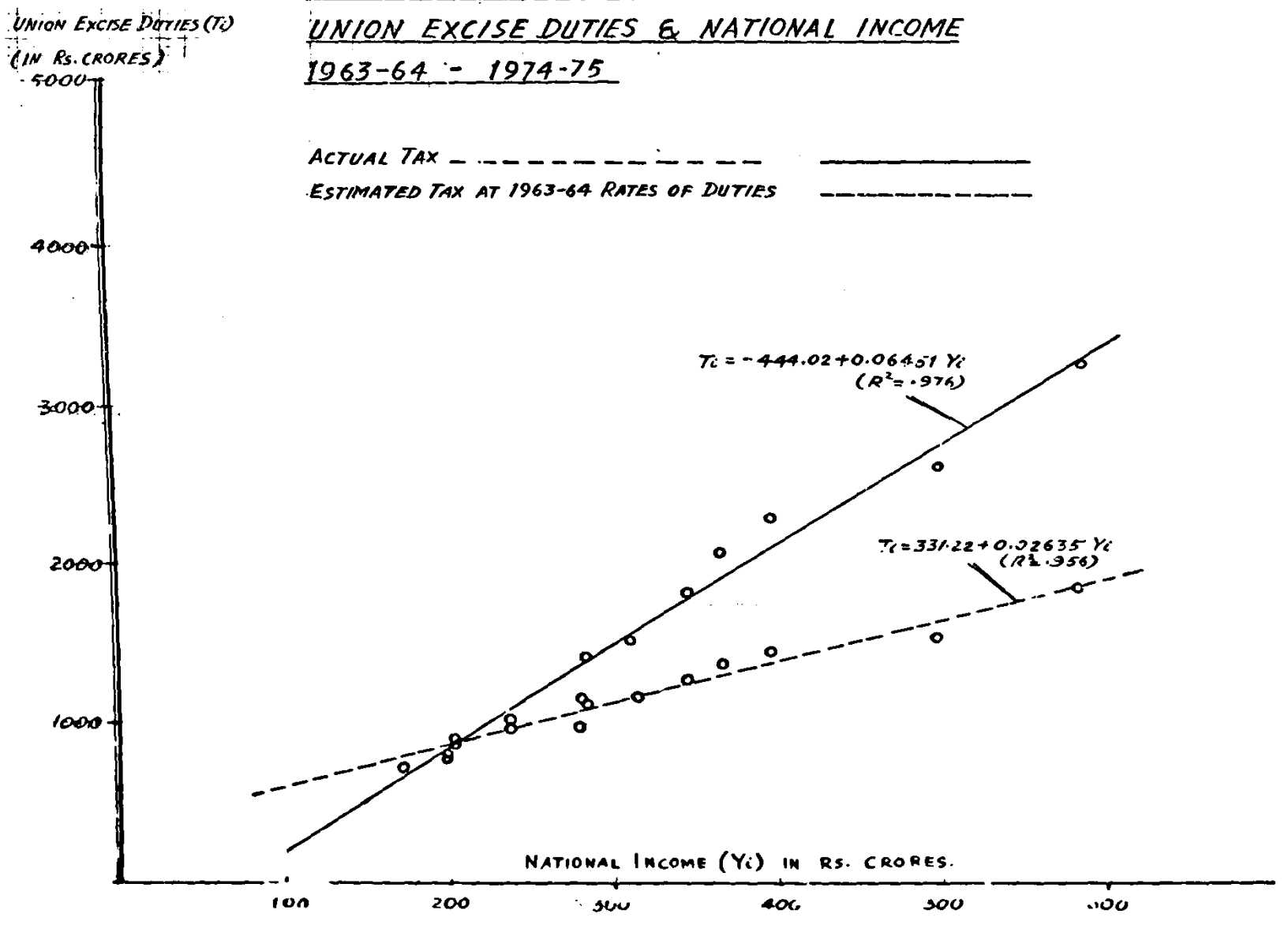
UNION EXCISE DUTIES
1963-64 TO 1975-76
(ACCORDING TO COMMODITY GROUPS)



UNION EXCISE DUTIES
1963-64 TO 1975-76



RELATIONSHIP BETWEEN UNION EXCISE DUTIES & NATIONAL INCOME 1963-64 - 1974-75



APPENDIX 6

STATEMENT SHOWING COMPARATIVE SALES TAX RATES FOR CERTAIN SELECTED COMMODITIES IN SOME OF THE STATES (AS OPERATIVE IN 1976-77)

Ad valorem
Rates in percent

S. No.	Name of commodity	Name of States							Remarks
		Maharashtra	Madhya Pradesh	Punjab	Rajasthan	Tamil Nadu	Utter Pradesh	West Bengal	
1.	Foodgrains	Nil	2, 4	4	2, 3, 4, 10	Nil	4	Nil, 6	
2.	Atta, Maida, Suji	Nil	2, 8	4	3, 4	2	2	Nil	
3.	Kirana	Nil, 5, $6\frac{1}{4}$, $8\frac{1}{4}$	8	6	N.A.	N.A.	6	6	
4.	Vanaspati	7	8	6	10	8	8	8	
5.	Edible Oils	3	2	N.A.	5	4	3	Nil, 6	
6.	Cooked food	N.A.	2	6	5	8	4	6	
7.	Cotton yarn	2	4	1	2	3	4	N.A.	
8.	Cement	6	8	6	12	8	7	6	
9.	Bricks	5	8	6	12	5	7	6	
10.	Kerosene Oil	3	7	6	7	$8\frac{1}{2}$	7	Nil, 6	
11.	Agricultural Implements	Nil, 3	Nil, 8	Nil	Nil, 5, 7	Nil	Nil, 5	Nil, 2	
12.	Bicycle and tricycle etc.	7	8	6	7	6	7	6	
13.	Iron and Steel	4	4	4	4	4	4	4	
14.	Steel furniture	15	12	10	12	10, 15	12	15	
15.	Articles of stationery	Nil, 3, $8\frac{1}{4}$	8	6	7	N.A.	7	6	
16.	Cosmetics	$15\frac{1}{4}$	12	10	10	12	12	6, 12	
17.	Wireless receiving sets	12	12	10	12	15	12	15	
18.	Tyres and tubes	3, 7, 12	8, 11, 12	10	7, 10	10	7, 12	3, 10	
19.	Drugs and Medicines	3	4	6	5	8	5	3, 8	
20.	Washing Soap	5	8	6		$5\frac{1}{2}$	5	8	
21.	Footwear	Nil, 5, 10, 15, 20	8, 10	6	7	4	7	6	

Note: Retail Sales Tax, levied on a registered retailer, @$\frac{1}{4}$% has been included against rates of sales tax of Maharashtra State against commodities at S. No. 3, 15 and 16.

APPENDIX - 7

RATES OF MOTOR VEHICLES TAX AND GOODS AND PASSENGERS TAX IN SOME STATES

STATE/UNION TERRITORY	MOTOR VEHICLES TAX PER ANNUM		GOODS TAX PER ANNUM	PASSENGER TAX PER ANNUM
	GOODS VEHICLES (Rs.)	PASSENGER VEHICLES (Rs.)	(Rs.)	(Rs.)
1. W. Bengal	3745	2490	Nil	N.A.
2. Bihar	N.A.	N.A.	20% of freight or 3000/-	25% on fares
3. Goa	2790	1715	5% on freight or 450/-	10% on fares or 5, 100/-
4. Kerala	5000	15, 360	Goods tax and passenger tax merged with Motor Vehicles Tax with effect from 1.10.1975.	
5. Madhya Pradesh	2978	N.A.	10% of minimum freight or*	25% of fare inclusive of tax or a composition fee.
6. Maharashtra	4130 (for general limits)	3300 (for general limits)	1350	17.5% of fare for mofussil areas
7. Nagaland	2400	2000	N.A.	N.A.
8. Punjab	N.A.	N.A.	1050	35% of fare
9. Rajasthan	2670	2750	1470 plus surcharge @ 10% Rs. 147	30% of value of fare (on pucca roads) 5% Surcharge
10. Tamil Nadu	5000	32160	Goods tax and passenger tax are merged with mrotor vehicles tax	
11. (a) Chandigarh	1000	3000	300	35% of fare
(b) Dadra Nagar Haveli	1550	-	Nil	NIL

NOTE: For goods vehicles RLW of 15500 kgs. has been assumed for passenger vehicles a seating capacity of 50 with 17 standees is assumed.

Source: Replies sent by State Government/Union Territories to questionnaires sent by the I.T.E.C.

Compsition Fee.

* according to the formula

$$\frac{\text{RLW-ULW}}{55 \text{ per month}}$$

Where RLW: Registered Laden Weight
ULW: Unladen in Kgs.

APPENDIX-8

TABLE SHOWING STATE-WISE ELECTRICITY TARIFF/ELECTRICITY DUTY

State	Domestic lights & fans As on 1.8.76 30 kwh/month				Commercial lights & fans 50 kwh/month				Agriculture 10 HP				Small Industry 10 KW				Large Industry 1000 KW			
	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Andhra Pradesh	40	-	3	40	75.00	-	-	75.00	19.67	-	-	19.67	32.00	-	-	32.00	25.77	-	-	25.77
Assam	45	-	3	48	57.00	-	3.00	60.00	18.00	-	-	18.00	22.00	-	1	23.00	21.70	8	0.08	29.78
Bihar	40	-	7	47	60.00	-	7.00	67.00	13.48	-	2	15.48	21.84	7.66	2	31.50	21.91	7.56	2.00	31.57
Gujarat	30.10	-	7.33	37.43	32.98	-	8.40	41.38	22.97	-	1.20	24.17	27.52	-	1	28.52	19.45	5.50	3.00	27.95
Kerala	38.33	-	2.50	40.83	38.00	-	3.80	41.80	11.22		1.12	12.34	15.00	-	1.50	16.50	12.90	-	3.87	16.77
Madhya Pradesh	30.00	-	6.50	36.50	40.00	-	8.00	48.00	16.00	-	-	16.00	22.00	-	1.50	23.50	15.54	5.70	1.50	22.74
Tamil Nadu	35.00	-	-	35.00	68.50	-	-	68.50	17.22	-	-	17.22	31.00	-	-	31.00	26.25	-	2.89	29.14
Maharashtra	31.00	-	5.00	36.00	35.00	-	15	50.00	20.00	4.67	-	24.67	20.00	4.67	1.00	25.67	12.86	4.67	1.00	18.53
Karnataka	38.33	-	4.50	42.83	57.50	-	4.50	62.00	16.22	-	1	17.22	18.04	-	4.50	22.54	10.60	-	2.25	12.85
Orissa	28.00	-	4.65	32.65	31.00	-	5.10	36.10	15.00	0.65	2.50	18.15	18.00	0.65	3.27	21.92	14.50	0.65	4.82	19.97
Punjab	27.50	-	10.25	37.75	40.00	-	8.80	48.80	20.86	-	-	20.86	18.50	-	3.70	22.20	15.51	-	3.88	19.39
Haryana	24.50	-	10.25	34.75	40.00	-	11.00	51.00	22.45	-	-	22.45	21.00	-	3.15	24.15	14.83	-	4.45	19.28
Rajasthan	38.00	-	5.00	43.00	50.00	-	-	50.00	21.00	-	-	21.00	21.00	-	1.00	22.00	18.00	0.40	1.00	19.40
Uttar Pradesh	41.00	-	2.00	43.00	51.00	-	2	53.00	18.36	-	-	18.36	24.00	-	1.00	25.00	16.98	7.17	1.00	25.15
West Bengal	45.00	-	3.00	48.00	55.00	-	3	58.00	32.00	-	6	38.00	32.00	-	0.33	32.33	21.67	4.60	1.50	27.77

(Note: 1 indicates electricity tariff and shows rate per kilowatt in paise
2 indicates fuel cost adjustment
3 corresponds to electricity duty in paise
4 indicates the total of 1, 2 and 3.)

APPENDIX 9

METHODOLOGY OF ESTIMATION OF INCIDENCE OF INDIRECT TAXES IN INDIA - 1973-74

As already explained, the study is confined to measuring the money burden of indirect taxes in India on different expenditure classes in the rural and urban sectors of the economy as a percentage of the aggregate expenditure of each class. The entire amount of indirect taxes collected has not been allocated to the households. The tax revenue attributable to purchases made by government administrative departments has been excluded from the total allocable yield from indirect taxes because it has been considered that the taxes collected on the purchase of goods by the government represent only an accounting transfer within the government sector and not a transfer to the government sector from the private sector. Purchases made by government departmental and non-departmental enterprises are, however, treated analogous to private sector purchases. A brief note on the method of arriving at the share of tax yield from government purchases is given in section IV.

For working out the incidence, two types of information are necessary: (i) data on total expenditure as well as expenditure on different consumption goods by different expenditure groups; and (ii) commodity-wise tax yield (exclusive of the share attributable to government purchases). We have already indicated in the Technical Note appended to Chapter VI the nature and sources of information as taxes and expenditure.

National Sample Survey (NSS) data on consumption expenditure are available in terms of quantity as well as value. Quantity data have not been generally used for working out the incidence due to the fact that in most cases while money expenditure data are given, quantity data are not given in the NSS report probably because sample households could not give dependable information on the quantity of consumption.

Taxes are levied not only on consumer goods but also on intermediate and capital goods. One of the major problems in the study of the incidence of indirect taxes is to trace the burden of taxes on these non-consumption goods. As indicated in the Technical Note, if we had a detailed input-output table for the economy we could have determined how different inputs are allocated for use in the manufacture of various kinds of final goods. Unfortunately, we could not get a detailed table and so we had to make use of the information obtained otherwise.

CENTRAL EXCISE

For measuring the incidence of excise as well as import duties, we have classified commodities into (A) mostly in the nature of consumption goods; (B) mostly in the nature of intermediate goods; (C) capital and partly capital goods and (D) components of capital and partly capital goods. We shall now proceed to indicate the methodology adopted in the case of these four groups of commodities.

A. Commodities Mostly in the Nature of Consumption Goods

There are a number of commodities which are mostly in the nature of consumption goods

which bear Central excise duties and also appear with more or less the same description as NSS items of consumer expenditure. In such cases the methodology of estimation of incidence is very simple. Tax yield (after allowing for government contribution) has been allocated to different expenditure groups in rural and urban sectors in proportion to their expenditure on such commodities. Difficulties arise, however, in cases where the commodities can be classified into grades or types and are subject to different tax rates in view of differences in quality, because tax categories often do not correspond to NSS categories. These cases are taken up after dealing with the simpler cases. The items for which the incidence can be worked out readily on the basis of consumer expenditures as made available in the NSS report are given below along with the NSS matching items:

	Items bearing taxes		NSS items of consumption
1.	Khandsari (Sugar)	1.	Khandsari (Sugar)
2.	Sugar	2.	Sugar, Sugar Candy Sugar (other)
3.	Confectioneries and chocolate.	3.	Biscuit, confectioneries
4.	Aerated water	4.	Drinking beverages other than tea and coffee
5.	Glucose dextrose and preparations thereof	5.	Baby food
6.	Vegetable oils and fats	6.	Vanaspati, groundnut oil, etc.
7.	Patent and proprietary medicines	7.	Allopathic medicine Homeopathic medicine Ayurvedic medicine Unani medicine other medicines
8.	Soap	8.	Toilet soap washing soap
9.	Cosmetic and toilet preparations	9.	Powder, snow cream, hair oil, hair cream, hair lotion and other toilet requisites
10.	Tooth paste	10.	Tooth paste
11.	Safety razor, baldes stainless steel	11.	Shaving blades, other shaving requisites
12.	Matches	12.	Matches (sticks)
13.	Gramophone and parts	13.	Other musical instruments (other than harmonium, radio and tape recorders)

	Items bearing taxes		NSS items of consumption
14.	Pressure cookers	14.	Pressure cookers
15.	Playing cards	15.	Amusement (other than cinema, theatre, mela, fair, sport goods, toys, etc.)
16.	Domestic electrical appliances	16.	Electric fan, iron, electric heater, etc.
17.	Rayon and art silk fabrics including synthetic fibres, nylon yarn and clothes	17.	Rayon and art silk fabrics
18.	Prepared or preserved food	18.	Bread
19.	Food products	19.	Salted refreshments, prepared sweets Jam and jellies Processed food and others
20.	Paper	20	News papers, journals, magazines, books, etc, taken together

For each of the remaining consumer goods subjected to excise taxes we have evolved a separate methodology for working out the incidence as indicated below.

1. Coffee

Production, clearance and tax yield data are available from the Statistical Year Book, Central Excise and Customs (henceforth termed 'Central Excise Year Book'). NSS data on consumption of coffee in quantity are available both in terms of number of cups consumed by the households and the quantity purchased in kilograms. Estimates of coffee powder purchased are given in terms of kilograms. From the publication, Indian Customs and Central Excise Tariff (hereafter termed 'Excise Tariff Book', we have the information on rates of duty in respect of different grades of coffee other than instant coffee.

Because of the difference in the price of coffee between the rural and urban sectors and also between different parts of the urban and rural sectors it has been considered desirable not to allocate the duty on this item on the basis of total expenditure on coffee by the different expenditure groups. Instead an attempt has been made in this case to allocate the tax yield on the basis of quantity consumed. As data on quantity are available in terms of both number of cups and kilograms, it is necessary to convert them into one standard unit. For this purpose, the quantity of powder purchased in kilograms was converted into quantity consumed in cups. On the basis of information available directly from the Coffee Board, it was assumed that 100 cups of coffee could be prepared from one kilogram of coffee powder. The tax yield on coffee, other than instant coffee, has been allocated to

different expenditure groups in rural and urban areas on the basis of the total number of cups consumed. The yield from instant coffee has been allocated on the assumption that it is consumed exclusively by the groups with per capita expenditure of Rs. 100 and above in the urban sector.

2. Tea

Information on production, clearance and tax yield is available from Central Excise Year Book; rates of duty from Excise Tariff Book and consumption data from the NSS. Production, clearance and tax yield data are available separately for loose leaf tea and package tea. Consumption data are available in terms of number of cups for tea and in terms of kilograms for loose leaf tea. Tax rates are available separately for loose leaf tea, package tea and instant tea. Duty on package tea is higher than on loose leaf tea. The rate of duty on instant tea is still higher.

As in the case of coffee, we have first tried to work out consumption in terms of cups of tea. For this purpose, the quantity of tea leaves has been converted into tea cups on the assumption that for one kilogram of tea 600 cups of tea could be prepared. This assumption is based on the estimates supplied by the Tea Board. In case of loose leaf tea, we have assumed that the consumption proportions (tea cups) found for urban and rural sectors and for different expenditure groups will hold good for the allocation of tax yield also. A difficulty is faced, however, in the allocation of yield from package tea. It is tea of a superior quality. In a similar exercise done by the Ministry of Finance (Incidence of Indirect Taxation, 1963-64, published in 1969), it was assumed that 57.2 per cent of the package tea was consumed in the rural sector and 42.8 per cent in the urban sector. In the absence of any statistical evidence it has been considered simpler to assume that the rural and urban sectors consume 50 per cent each. The difficulty arises in determining the proportion of package tea consumed by different expenditure groups in the two sectors. We have made an assumption here that the bottom four expenditure groups do not consume package tea and the next three expenditure groups consume 20 per cent, 30 per cent and 50 per cent, respectively, of total package tea. After this, the incidence of the tax on tea was worked out as follows.

First, the estimates of consumption of package tea (in cups) for different expenditure groups in the rural and urban sectors were worked out and accordingly, the incidence of tax yield attributable to package tea was estimated. Then from the total number of cups of tea consumed by different expenditure groups in the rural and urban sectors, the number of cups of tea prepared from package tea was deducted. The remaining number of cups have been taken as tea prepared out of loose leaf tea and accordingly, the tax yield from it was distributed.

The tax yield from instant tea has been wholly allocated to groups with per capita expenditure exceeding Rs. 100 per month in the urban sector.

3. Art silk, rayon and synthetic textiles

The data on consumption under this head relate to various items like dhoti, saree, cloth for shirt, pyjama, salwar, coat, suit, trousers, chaddar, headwear, lungi, bedsheet and knitted garments. There are marginal differences in the rates of duty on these items and the tax yield data

are not available separately. The total tax yield therefore has been allocated to different expenditure groups in the urban and rural sectors on the basis of total expenditure on all these items taken together for each category.

4. Tobacco (unmanufactured and manufactured)

Data on tax yields and the rates of duty on different kinds of manufactured tobacco are available from Central Excise Year Book and Excise Tariff Book, respectively. Similarly, data on consumption of different kinds of tobacco could be obtained from the NSS. Estimates of tax yields by kind of tobacco are as follows :

			1973-74 (Rs. lakhs)
1.	Cigarettes		23826.0
2.	Smoking mixtures		84.0
3.	Unmanufactured tobacco of which		9548.6
	(a) flue cured and used in the manufacture of smoking mixtures for pipes and cigarettes	7.7	
	(b) flue cured and used in the manufacture of cigarettes	1878.5	
	(c) flue cured and not otherwise specified	201.9	
	(d) other than flue cured used for the manufacture of cigarettes	867.0	
	(e) other than flue cured and not used for the manufacture of cigarettes of which	6593.7	
	(i) Snuffs	93.4	
	(ii) Hukkahs	499.8	
	(iii) Chewing	1129.9	
	(iv) Cigars and cheroots	299.6	

different expenditure groups in rural and urban areas on the basis of the total number of cups consumed. The yield from instant coffee has been allocated on the assumption that it is consumed exclusively by the groups with per capita expenditure of Rs. 100 and above in the urban sector.

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	(d) other than flue cured used for the manufacture of cigarettes	867.0	
	(e) other than flue cured and not used for the manufacture of cigarettes of which	6593.7	
	(i) Snuffs	93.4	
	(ii) Hukkahs	499.8	
	(iii) Chewing	1129.9	
	(iv) Cigars and cheroots	299.6	

(Rs. lakhs)

(v)	Biris	2647.5
(vi)	Goods of special importance	1499.8
(vii)	Others	423.9
TOTAL		33458.8

1. Cigarettes - In 1973-74, there was a uniform duty for all types of cigarettes (200 per cent ad valorem plus an additional duty of 100 per cent ad valorem). Hence, the tax yield has been allocated to the various expenditure groups in the rural and urban sectors on the basis of their expenditure on cigarettes.

2. Smoking mixtures - Smoking mixtures are used by the urban people and there is little use of them in the rural sector. The tax yield from this item is therefore attributed to the group with per capita expenditure of Rs. 100 and above in the urban sector only.

3. Unmanufactured tobacco - In the case of item 3(a), for the same reason as given above in (2), the entire revenue has been attributed to the group with per capita expenditure of Rs. 100 and above in the urban sector. This is a costlier product which is taken to be beyond the pockets of people belonging to groups with per capita expenditure of less than Rs. 100 in the urban sector. The rate of duty is as high as Rs. 40 plus an additional duty of Rs. 5.50 per kilogram.

Tax yields from items 3(b), 3(c) and 3(d) are attributed to different expenditure groups in the rural and urban sectors on the basis of their expenditure on cigarettes. The rates of duty in these three cases do not vary much.

In the case of the yields from items 3(e) (i) snuffs and 3(e) (ii) hukkah, the allocation has been done on the basis of NSS estimates of consumption of snuffs and hukkah tobacco, respectively; yields from chewing tobacco on the basis of expenditure on zarda, kimam and surti. The yield from tobacco used for cigars and cheroots of special importance has been allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector. The yield from biris has been allocated to different expenditure groups on the basis of proportions of expenditure on biris. The yields from others have been allocated on the basis of household expenditure on other tobacco products.

5. Cotton fabrics

There may be two methods of estimation:

1. We may work out the quantity of clearance of cloth and tax yield according to fineness

of cloth (superfine, fine, medium and coarse); make certain assumptions about the proportions in which different grades of cloth have been consumed (in quantity) by each expenditure group in the urban and rural sectors; and accordingly, allocate tax yield to different expenditure groups.

2. We may proceed from the expenditure side and work out the aggregate amount of expenditure on cotton cloth for the rural as well as urban sectors on the basis of NSS data; adjust the urban expenditures for price differential in the two sectors; make assumption about the proportions of expenditure on different grades of cloth by different expenditure groups in the rural and urban sectors; work out for each sector the total expenditure on cloth of each quality; and accordingly allocate the tax yield estimated to be derived from each type of cloth.

The second method has been adopted for mainly three reasons: (a) Data on the quantity of cloth cleared by types of cloth (according to fineness) are available for composite mill products but not for powerloom products. All units which have less than 49 looms installed paid a compounded levy based on the number of looms only and not on the quantity and grades of cloth produced. (b) Indian Textile Bulletins give data on the production of powerlooms and handlooms together. But separate data on the production flowing from powerlooms according to the quality of cloth are not available. Very crude estimates of cloth produced by powerlooms according to fineness can be worked out on the basis of yarn data but the conversion ratios of yarn into cloth may not be dependable. (c) The total quantity of cloth consumed as worked out on the basis of NSS data far exceeds the data on the total quantity produced and released. It may be pointed out that for 1973-74 NSS gives an estimate of 11410 million metres (exclusive of ready made cloth) while Central Excise Year Book and Indian Textile Bulletins give an estimate of 7770 million metres only. (d) In many cases quantity data on consumption are not given in NSS tables while for the corresponding expenditure groups value data are available. Basic assumptions that have been made can be explained as follows.

1. $C = {}^{R}C + {}^{U}C$

where C = total consumption expenditure

^{R}C = total consumption expenditure for the rural sector

^{U}C = total consumption expenditure for the urban sector

2. $^{R}C = {}^{R}C_1 + {}^{R}C_2 + {}^{R}C_3 + {}^{R}C_4$

where C_1 = consumption expenditure for the group with per capita expenditure of Rs. 0-28,

C_2 = consumption expenditure for the group with per capita expenditure of Rs. 28-55,

C_3 = consumption expenditure for the group with per capita expenditure of Rs. 55-100,

C_4 = consumption expenditure for the group with per capita expenditure of Rs. 100 and above.

3. $C_1^R = C_{1c}^R + C_{1m}^R$

where C_{1c}^R = consumption of coarse cloth in rural areas by the group with per capita expenditure of Rs. 0-28,

C_{1m}^R = consumption of medium cloth in rural areas by the group with per capita expenditure of Rs. 0-28.

C_{1c}^R is assumed to be equal to 0.5 C_1^R

and C_{1m}^R is assumed to be qual to 0.5 C_1^R

4. $C_2^R = C_{2c}^R + C_{2m}^R$

where C_{2c}^R is assumed to be equal to 0.4 C_2^R

and C_{2m}^R is assumed to be equal to 0.6 C_2^R

5. $C_3^R = C_{3m}^R + C_{3f}^R$, subscript f representing fine cloth

where C^{R}_{3m} is assumed to be equal to 0.6 C^{R}_{3}

and C^{R}_{3f} is assumed to be equal to 0.4 C^{R}_{3}

6 $C^{R}_{4} = C^{R}_{4m} + C^{R}_{4f} + C^{R}_{4sf}$, subscript sf representing superfine cloth

where C^{R}_{4m} is assumed to be equal to 0.2 C^{R}_{4}

C^{R}_{4f} is assumed to be equal to 0.2 C^{R}_{4}

C^{R}_{4sf} is assumed to be equal to 0.6 C^{R}_{4}

Similarly,

7. $C^{U} = C^{U}_{1} + C^{U}_{2} + C^{U}_{3} + C^{U}_{4}$

8. $C^{U}_{1} = C^{U}_{1c} + C^{U}_{1m}$

where C^{U}_{1c} is assumed to be equal to 0.5 C^{U}_{1}

and C^{U}_{1m} is assumed to be equal to 0.5 C^{U}_{2}

9. $C^{U}_{2} = C^{U}_{2c} + C^{U}_{2m}$

where C_{2c}^{U} is assumed to be equal to 0.3 C_{2}^{U}

and C_{2m}^{U} is assumed to be equal to 0.7 C_{2}^{U}

10. $C_{3}^{U} = C_{3m}^{U} + C_{3f}^{U}$

where C_{3m}^{U} is assumed to be equal to 0.5 C_{3}^{U}

and C_{3f}^{U} is assumed to be equal to 0.5 C_{3}^{U}

11. $C_{4}^{U} = C_{4m}^{U} + C_{4f}^{U} + C_{4sf}^{U}$

where C_{4m}^{U} is assumed to be equal to 0.4 C_{4}^{U}

C_{4f}^{U} is assumed to be equal to 0.3 C_{4}^{U}

C_{4sf}^{U} is assumed to be equal to 0.3 C_{4}^{U}

It may be noted that a separate treatment for cotton yarn is not necessary. Collection of duty for cotton yarn is done along with the cloth itself (according to fineness). Thus, the yield from yarn may be added to the yield from cloth to work out the incidence. The methodology adopted here (expenditure approach rather than quantity approach) takes care of ready- made cotton garments also.

Data on cotton yarn and cotton fabrics are available from the following sources: (1) Production and clearance data (in metres and square metres) are available for composite mills according

to fineness of cloth (superfine, fine, medium and coarse) in Central Excise Year Book, 1973-74. (2) Yield from basic duty according to fineness of cloth is also available from the same source. (3) Yield from additional duty and handloom cess according to grades of cloth could be obtained from the Directorate of Statistics and Intelligence (DSI).

In the following cases, information is not available in the needed detail. (1) Information on the yields from differential duty, according to fineness of cloth is not available; but it was suggested by DSI that they could be allocated to different grades of cloth in proportion to the yields from the basic duty. (2) The breakdown of yield from miscellaneous duties, according to fineness of cloth, is also not available; hence their yield has been allocated in proportion to the yield from the basic duty. (3) Non-availability of similar breakdown in respect of tax yield from embroidery in stripe and motifs and embroidery impregnated with cellulose has necessitated its allocation also in the same manner.

6. Footwear

Footwear was exempted from duty in the following cases: (1) the entire output of those factories (precincts) which employ less than 49 workers; (2) the output of those establishments in which the total of power used in the process of manufacturing footwear does not exceed the equivalent of two horse power; (3) footwear if made out of artificial or synthetic resins or plastic materials or both; (4) footwear made in Government Harness Factory and Saddlary Factory, Kanpur for consumption by the members of the armed forces, and (5) all samples (not exceeding 3 pairs of each variety) for exports. Because of these exemptions, we have been forced to make certain assumptions on the basis of judgement. We have assumed that (a) in the rural areas all the expenditure on footwear by groups with per capita expenditure not exceeding Rs. 75 per month is incurred on the purchase of footwear which is free of duty; (b) in the case of groups in the rural sector with per capita expenditure of Rs. 75 and above per month, only 25 per cent of the expenditure on footwear is on the kind which is free of duty; (c) for the urban sector in the case of groups with per capita expenditure not exceeding Rs. 75 per month, 50 per cent of the expenditure on footwear is on such footwear as is free from duty and (d) in the urban sector in the case of groups with per capita expenditure exceeding Rs. 75 per month, 75 per cent of the expenditure on footwear is on the kind which is subject to duty. On the basis of above assumptions, we have worked out the expenditure on footwear by each expenditure group in the rural and urban sectors which can be said to contain tax elements. These figures form the basis of allocating the tax burden on footwear.

7. Woollen fabrics and knitting wool.

The incidence in this case has been worked out on the basis of separate estimates of expenditure on woollen fabrics and knitting wools. It might be indicated that the NSS records no expenditure on wool by groups with per capita expenditure not exceeding Rs. 43 in the rural sector as well as by groups with per capita expenditure not exceeding Rs. 55 in the urban sector.

It has been assumed that even rural folk make most of their purchases of woollen fabric and knitting wool from urban shops and that hence the problem of price differential does not arise.

8. Mechancial lighters and vacuum flasks

The tax yield from vacuum flasks and mechanical lighters was Rs. 49 lakhs and Rs. 1 lakh, respectively. In both cases it has been decided to allocate the yield entirely to the group with per capita expenditure of Rs. 100 and above in the urban sector only. The tax on vacuum flasks is distributed in proportion to the expenditure on manufactured goods and that on mechanical lighters in proportion to the expenditure on cigarettes.

B. Commodities Mostly in the Nature of Intermediate Goods

As indicated earlier, more serious problems arise in estimating the incidence of taxes on intermediate goods because these goods are not directly used by consumers. One has therefore got to find out into what final goods and in what proportions each of the taxed intermediate products gets embodied.

1. Jute manufactures and yarn

Data on production, clearance and tax yield are available from Central Excise Year Book, Vol.I, 1973-74. The necessary breakdown of yield, according to different jute manufactures and yarn is available only in respect of the basic duty. Hence the tax yield from auxillary and miscellaneous duties has been allocated to hessian and others in the same proportions as the basic duty.

For working out the incidence we have made the following assumptions: (i) hessian is used for packing, etc., of manufactured goods and hence the tax yield from this item may be allocated to different expenditure groups on the basis of their expenditure on manufactured goods; (ii) sacking is used for transporting foodgrains, etc. and can therefore be allocated on the basis of expenditure on foodgrains by different expenditure groups in the urban sector; and (iii) tax yield from others may be allocated to different expenditure groups on the basis of their expenditure on manufactured goods only.

2. Fertilisers

Production, clearance and tax yield data are available in Central Excise Year Book. We have data on consumption of fertiliser according to type of crops for 1970-71 from the publication by National Council of Applied Economic Research (NCAER), entitled Fertilizer Use on Selected Crops in India (1974).

We have distributed the total quantity of clearance among the various crops on the basis of proportions obtaining in 1970-71, as given in the NCAER publication mentioned above. The yield of tax on fertilisers has been attributed to the different crops on the basis of the above proportions, as shown below.

TABLE 1

Crop-Wise Pattern Of Use Of Fertilisers, 1970-71

Crop		Consumption of fertilisers during 1970-71 ('000 tonnes)	Percentage of total consumption	Yield from excise tax during 1973-74 ('000 rupees)
1.	Rice	726.9	17.4	66193.4
2.	Wheat	443.3	10.6	49324.7
3.	Maize	92.3	2.2	8369.3
4.	Sugarcane	420.9	10.0	38042.2
5.	Cotton	181.7	4.4	16738.6
6.	Pulses	2314.1	55.4	210753.8
	TOTAL	4179.2	100.0	380422.0

3. Petroleum-domestic production

Data on tax yield (Central excise) from different petroleum products for 1973-74 are available from Central Excise Year Book.

TABLE 2

Tax Yields From Petroleum Products
(1973-74)

		Tax yields (Rs. lakhs)
1.	Furnace oil	3001
2.	Refined diesel oil and vaporising oil, diesel oil not otherwise specified	31406
3.	Asphalt bitumen and coal tar	1602
4.	Petroleum products not otherwise specified	4684
5.	Blended or compounded lubricating oils and greases	1737
6.	Calcined petroleum coke	120
7.	Motor spirit	30725
8.	Kerosene oil	14112
	TOTAL	87387

The publication, Indian Petroleum and Petro-Chemicals Statistics, issued by the Economics and Statistics Division of the Ministry of Petroleum, New Delhi (hereafter referred to as Petroleum Statistics), contains information on domestic production, imports, consumption and sales. It is possible to allocate the estimates of clearance (quantity) of different types of petroleum production to different broad uses on the basis of information contained in the above - mentioned publication. The methodology used in each case is explained below.

1. Furnace oil - We have obtained information about the broad uses of furnace oil from the Ministry of Petroleum. The estimates of the quantities used for different purposes in absolute terms as well as in terms of percentages are indicated in the following table:

TABLE — 3

Uses Of Furnace Oil In India

Sectors of use	Quantity '000 tonnes	Per cent of total
Transport of which	417	7.0
Road transport	2	Neg.
Railways	61	1.0
Waterways	354	6.0
Agriculture/plantation	222	3.7
Power generation	1648	27.8
Other industries of which	3138	53.0
Iron and steel	438	7.4
Textile fibre	650	11.0
Cement	204	3.4
Ceramics and glass	218	3.7
Chemicals and allied	795	13.4
Fertilisers	266	4.5
Aluminium	110	1.9
Sugar	59	1.0
Mining and quarrying	35	0.6
Engineering	363	6.1
Other miscellaneous	507	8.5
TOTAL	5932	100.0

In the NSS list of consumption items we have separate information on the expenditure of the households on road transport, railways and waterways. The tax yield attributable to transport has been distributed among the different expenditure groups in rural and urban sectors accordingly. We recognise that transport is also used for the carrying of goods. But since the amount involved is not large, the approximation we have used may not significantly distort the total picture.

The tax yield attributable to agriculture/plantations can be allocated to different expenditure groups on the basis of their total expenditure on the following items indicated in the NSS list of consumption items: (a) total cereals, (b) total pulses, (c) total vegetables, (d) fresh fruits, (e) tea and tea leaves, and (f) coffee and coffee powder.

For other items, the basis of allocation is as follows. (i) Power generation - total expenditure on consumption of electricity and manufactured goods with equal weight. (ii) Iron and steel - total expenditure on consumption of manufactured goods. (iii) Textile fibre - according to tax-yield from cotton and woollen fabrics allocated to different expenditure groups. (iv) Cement, ceramics and glasses - the total tax yield was divided into two broad categories: (a) residential buildings and (b) others on the basis of the aggregate value of construction obtained in respect of each of the two groups from the CSO. The share of residential building has been distributed on the basis of household expenditure on house rent as given in the NSS and the share of 'others' on the basis of expenditure on manufactured goods. (v) Chemicals - the method of allocation is the same as for the tax on chemicals to be discussed later. (vi) Fertilisers - as in the case of tax on fertilisers. (vii) Aluminium engineering, mining and quarrying and other miscellaneous - on the basis of total expenditure on manufactured goods. (viii) Sugar - according to the methodology used for sugar.

2. Refined diesel oil and vaporising oil diesel oil not otherwise specified - This group of petroleum products mostly consist of high speed diesel oil (H.S.D.) and light diesel oil (L.D.O.). The uses of these two products have been worked out by the Ministry of Petroleum as follows:

	High speed diesel	Quantity ('000 tonnes)
(a)	State transport	599
(b)	Other road transport (including agriculture)	3359
(c)	Railways	581
(d)	Bunkers	28
(e)	Miscellaneous	626
		5193

Similarly, for LDO the distribution according to end uses has been worked out as follows:

Light diesel oil

		Quantity ('000 tonnes)
(a)	Power	158
(b)	Bunkers	45
(c)	Rest (including agriculture and small scale industries)	1145
		1348

As no separate tax yield is available in respect of HSD and LDO, we have decided to club them together and classify their joint use as follows :

		Quantity of HSD and LDO used ('000 tonnes)
(a)	Road transport	3958
(b)	Railways	581
(c)	Bunkers (steamship)	73
(d)	Power	158
(e)	Others (agriculture and small scale)	1771
		6541

The tax yield has been allocated to various uses in proportion to the quantities consumed as given above. The yield attributed to items (a), (b) and (c) has been apportioned on the basis of expenditure on railways, road and steamship fares, respectively; and the yield attributed to item (d) on the basis of consumption of electricity. In the case of the yield attributed to item (e), 50 per cent is distributed on the basis of expenditure on manufacturing products and the remaining 50 per cent on that on agricultural products. The consumption of diesel oil for the purpose of transport (road, railways and steamship) would not be entirely for carrying passengers. A part would go also towards the transportation of goods. Hence, we made an alternative assumption that 50 per cent of the diesel oil was consumed for the transportation of passengers and the remaining 50 per cent forthe transportation of goods. The share of tax yield attributable to the transportation of goods was allocated on the basis of household expenditure on manufactured goods. Surprisingly, the results thus obtained were almost the same (only in the case of one or two expenditure groups the incidence came out to be different, but only at the second decimal point).

(3). Asphalt, bitumen and coal tar- These materials are used mainly in construction (including road making) activity. We can divide the total value of construction into (i) government construction, (ii) residential buildings (private), (iii) non-residential buildings, and (iv) roads and bridges.

We have obtained estimates in respect of each of the above categories of construction from CSO. The share of residential buildings can be distributed on the basis of rent on dwellings as given in NSS. The share of non-residential buildings is distributed on the basis of expenditure on manufactured items and the share of roads and bridges is distributed on the basis of expenditure on road transport.

(4) Petroleum products not otherwise specified - On the basis of information contained in Central Excise Year Book this item is split into:

		Quantity ('000 tonnes)
(a)	Liquified petroleum gas	263
(b)	Waxes	47
(c)	Other mineral turpentine oil	699
		1009

According to the information given by the Ministry of Petroleum, liquified petroleum gas is used almost entirely for domestic purposes. It is assumed that this is used entirely by the groups with per capita expenditure of Rs. 100 and above in the urban sector. In the case of waxes, about 50 per cent goes to candle manufacturing (e.f. Petroleum Statistics) and the remaining 50 per cent to water proofing, match industry, paper waxing and hard board industry. The latter part is apportioned to manufacturing and the tax on it is allocated on the basis of expenditure on manufactured goods.

(5) Blended or compounded lubricating oils and greases-From the publication Petroleum Statistics (1973), the following breakdown of the use of compounded lubricating oils and greases has been obtained for the year 1972-73

		Quantity ('000 tonnes)
(a)	Automotive oils (automotive),	211

		Quantity ('000 tonnes)
(b)	Railways oil/axle oil	19
(c)	Industrial lubricating oil	643
		873

The share of item (a) in the tax yield is attributed to road transport. Share of item (b) to railway transport and the remaining item (c) is attributed to manufactured items.

(6) Calcined petroleum coke - The whole of the tax yield has been distributed on the basis of expenditure on manufactured items.

(7) Motor spirit - The use of motor spirit is split into

		Quantity ('000 tonnes)
(a)	ATF (aircraft turbine fuel	798
(b)	Others (motor cars, etc.)	791
		1589

First, we have divided the total tax yield from motor spirit into two parts (i) 50 per cent is apportioned to use by aeroplanes, (ii) the remaining 50 per cent is apportioned to use in cars, motor-cycles, etc. Then, 70 per cent of the share attributable to item (i) is taken to be from commercial use of aeroplanes and is distributed among various expenditure groups on the basis of proportions in aggregate household expenditure; of the remaining 30 per cent, 10 per cent is attributed to governmental use of air-services, and 20 per cent is taken to be used by groups with per capita expenditure exceeding Rs. 100, per month, in the urban sector.

The share of tax yield attributed to motor spirit used for cars, motor-cycles, etc., is distributed as follows: Estimates of Capital Formation in India, 1969, published by the CSO gives the percentage shares of the number of cars used for industrial and commercial purposes and of those used for private purposes. We have assumed the same proportions. The share of tax on motor spirit assumed to be used for industrial and commercial purposes is distributed on the basis of proportion of expenditure on manufactured goods. The share attributable to private use of cars is entirely allocated to groups with per capita expenditure exceeding Rs. 100 per month in the urban sector.

(8) Kerosene oil - The estimates of use of kerosene oil have been obtained from Petroleum Statistics. The uses in 1973-74 were as follows:

	Quantity ('000 tonnes)	Per cent of the total
(a) Domestic	3328	96.3
(b) Industrial and commercial	129	3.7
	3457	100.0

The share attributable to domestic use is allocated on the basis of expenditure on kerosene oil by the households. The share attributable to industrial and commercial uses is distributed on the basis of total expenditure on manufactured items.

(4) Iron and steel - Central Excise Year Book gives the estimates of tax yield from the various categories of iron and steel being produced in the country. They are reproduced below:

		Rs. lakhs
(a)	Iron and steel in any crude from	602
(b)	Steel ingots	1141
(c)	Iron and steel products	15585+
(d)	Steel furniture	373
(e)	Others (include slotted angles and channels of steel wire-ropes)	82
		17783

Item (c) iron and steel products can further be broken into the following :

		Total yield	Basic duty	Auxiliary duty
(1)	Semi-finished steel (including blooms, billets, etc.)	4742	2710	2032
(ii)	Bars and rods, wires, etc.	3244	1854	1390
(iii)	Plates and sheets	3453	1973	1480
(iv)	Flats, skelps and strips	3579	2045	1534
(v)	Pipes and tubes	94	54	40
(vi)	Other steel castings	144	82	62
(vii)	Rails and sleepers	326	186	140
(viii)	Others	3	2	1
	Total	15585	8906	6679

On the use of steel, we were able to obtain two studies: (1) The Iron and Steel Industry of India (1964) by Mr. Choudhuri, and (2) an unpublished study by the Steel Authority of India (SAIL) for the year 1975. Choudhuri's book gives data on the demand for steel for the years 1956-57 to 1960-61 by different Industrial sectors. The information obtained from the SAIL is more up-to-date and, therefore, we have made use of the SAIL data.

SAIL have divided iron and steel products into eight major groups as against five major groups available in Central Excise Year Book. These major groups are (i) pig iron, (ii) semi-finished steel, (iii) railway materials, (iv) structures, (v) bars and rods, (vi) plates, (vii) sheets and (viii) skelp and H.R. strips. Each of the above iron and steel products has been apportioned by SAIL among twenty-nine uses; namely, steel and coal, defence, power, other government departments, railway wagon, ports (ship yards), Posts and Telegraphs; Public Works Department, auto-manufactures, bright bar electric manufactures, re-rollers, tube manufactures, wire drawings, basic metals main fabricators, furniture makers, drum, barrel, fastner industries, foundry corporate bodies and agro-industries, trade, etc.

First, we have tried to match SAIL's eight major groups of iron and steel with the five major groups of iron and steel given by Central Excise Year Book indicated earlier. This has been done in the following manner. Iron in any crude form given in Central Excise Year Book is taken to

represent pig iron. Similarly, steel ingots have been taken to include plates and sheets structures and iron and steel products; the remaining important groups given in Central Excise Year Book are taken to include the remaining groups of items in the SAIL report.

The many uses for each of the above metioned groups have then been reclassified into seven major uses: (i) Government services, (ii) furniture makers, (iii) irrigation, (iv) manufacturing, (v) power, (vi) transport and communication and (vii) others.

The share attributable to government services has not been allocated to households. Furniture makers, make steel furniture and structurals partly for permanent fitting in the buildings. This part is to be treated as capital formation and the remaining part as household consumption. Following the CSO estimates given in the Estimates of Capital Formation, 1969, 50 per cent is treated as part of capital formation in non-residential construction and 50 per cent as household consumption of furniture. The share going to non-residential construction has been distributed on the basis of household expenditure on manufactured goods. The share going to household consumption of furniture is distributed on the basis of expenditure on furniture by different expenditure groups. The share going to irrigation has been allocated on the basis of expenditure on agricultural goods. Similarly, shares of manufacturing and power have been distributed on the basis of expenditure on manufactured goods and electricity, respectively, Transport and communication has been broken up into Posts and Telegraphs, auto-manufacturers, railway wagons, trade and ports. The share of Posts and Telegraphs has been allocated on the basis of household expenditure on postage and telephone; the aggregate share of railway wagons, trade and ports on the basis of expenditure on manufactured goods; the share of item (vii) 'others' on the basis of expenditure on manufactured goods.

(5) Chemicals

(i) Paints and varnishes - on the basis of the information contained in Input-Output Table For India, 1963 prepared at the Gokhale Institute of Politics and Economics and published in Artha Vijnan, March 1972 (hereafter referred to as Input - Output Table For India, 1963) and in Draft Fourth Plan, Material and Financial Balances, published by the Planning Commission in September 1966, (hereafter referred to as Material and Financial Balances, 1966), we first allocated the total of this item among different uses, in the following manner.

		(Rs. crores)
(a)	Construction	32.6
(b)	Electrical equipment	2.9
(c)	Non-electrical equipment	1.4
(d)	Transport	5.7
(e)	Metal products	5.7

		(Rs. crores)
(f)	Glass and glass wares	2.4
(g)	Final consumption	1.1
	Total	51.8

For the purpose of estimating incidence, we had to compress the above into a smaller number of groups as given below:

		(Rs. crores)
(a)	Construction	32.6
(b)	Transport	5.7
(c)	Manufacturing	7.0
(d)	Domestic	6.5
	Total	51.8

Construction is broken down into (a) Government (b) residential and (c) others, on the basis of information obtained from the CSO. The tax yield from paints and varnishes attributable to Government construction has been excluded from the allocable pool. Residential construction is broken into rural and urban on the basis of estimates obtained from the CSO. The tax yield attributable to residential buildings in each sector is then apportioned among the different per capita expenditure groups in that sector in proportion to their expenditure on rent of (owned and rented) residential buildings. The amounts of tax yield attributable to 'others' is apportioned on the basis of expenditure on manufactured goods.

The share of tax yield attributable to 'transport' is allocated in the same manner as yield of other taxes attributable to transport (mentioned in earlier cases).

The share of manufacturing item (c) is allocated on the basis of expenditure on manufactured goods; and the share of domestic uses, item (d), has been allocated on the basis of expenditure on furniture.

(ii). Synthetic and organic dye stuffs - From the report of the Tariff Commission on the Review of Dye Stuffs Industry for the year 1974, we could get the following break-up of the uses of this chemical.

(a)	Textile industry	80 per cent
(b)	Leather, plastic and printing ink for paper and coir	20 per cent

The share of tax yield attributable to the textile industry has been allocated to different expenditure groups in the urban and rural sectors on the basis of their total expenditure on woollen, cotton and silk fabrics. The tax yield attributable to leather, plastic, printing ink for paper and coir has been allocated on the basis of total expenditure of the households on (i) leather (ii) plastic articles (iii) books and periodicals and (iv) coir ropes and coir mats.

(iii). Caustic soda and caustic potash - We have information about the end uses of these products from Indian Chemicals and Pharmaceutical Industry - A Survey, 1963-64 published by Indian Chemical Manufacturers Association.

The shares of the different end uses during the Third Five Year Plan have been assumed for the year 1973-74.

Industry	Demand (per cent of total)
(a) Paper and paper board	28
(b) Rayon and staple fibre	23
(c) Taxtiles	15
(d) Soap	14
(e) Aluminium	7
(f) Petroleum refining	2
(g) Vanaspati	1
(h) Dye stuffs	10
	100

The share of tax yield on caustic soda and caustic potash attributable to paper and paper board has been allocated on the basis of consumption expenditure on books and journals and news papers and periodicals; that attributable to rayon and staple fibre has been allocated on the basis of expenditure on artificial silk. The shares of textiles and dye stuffs have been allocated on the basis of expenditure on cotton and woollen fabrics.

The shares of tax yield attributable to soap and vanaspati have been allocated on the basis of NSS consumption expenditure on soap and vegetable oil, respectively. The share of yield attributable to caustic soda and caustic potash used in the production of aluminium has been allocated in the same fashion as the tax on aluminium.

(iv) Organic surface active agents - The yield from this item has been allocated on the basis of expenditure on manufactured goods.

(v) Calcium carbide, bleaching powder and sodium hydrosulphate - The yield from these items has been allocated on the basis of expenditure on manufactured goods.

(vi) Soda ash - Information about its uses is available from Indian Chemical and Pharmaceutical Industry - A Survey, 1963-64. For the Third Plan period, the uses have been indicated as follows:

		(per cent)
(a)	Laundry, dhobi and miscellaneous	37
(b)	Glass	31
(c)	Chemicals, caustic soda	12
(d)	Silicate	8
(e)	Paper	4
(f)	Textiles	3
(g)	Sodium bicarbonate	3
(h)	Bichromate	2
		100

The share of laundry, dhobi and miscellaneous have been allocated on the basis of expenditure by households on washerman, laundries, etc. of the total share of glass, 50 per cent has been allocated on the basis of expenditure of households on crockery and other utensils, and the remaining 50 per cent is attributed to construction. The distribution in regard to the tax yield of the share allocated to construction is the same as in case of other construction inputs.

The shares attributable to chemicals, caustic soda, silicate, sodium bicarbonate and bichromate have been allocated on the basis of expenditures on manufactured goods.

The share attributable to paper has been distributed on the basis of expenditure on books, journals and news papers etc., and that attributable to textiles on the basis of expenditure on cotton, silk and woollen fabrics.

(vii) Rubber processing chemicals - The entire yield has been allocated on the basis of expenditure on road transport because most of the consumption of rubber is used in the preparation of tubes, tyres, etc., for motor vehicles.

(viii) Carbon Black - This is used mostly in the preparation of tyres and tubes and hence the whole of it has been distributed on the basis of expenditure on road transport.

(ix) Optical bleacing agents - Expenditure of households on laundries has been taken as the basis allocation.

(x) Other Chemicals - The yields from the remaining chemical items like sodium silicate, cellophane, acids, camphor , menthol and glycerine, etc., have been distributed on the basis of expenditure on manufactured goods.

(6) Cement - Cement is used mainly for construction. Only a very small part of it goes to other uses like production of asbestos, which is also used in construction. The total value of construction consists of (i) construction covered by the commodity-flow approach and (ii) construction not covered by the commodity-flow approach. Cement is used only in construction works covered by the commodity-flow approach. The total value of construction covered by the commodity-flow approach and the break-up thereof in 1973-74 have been supplied by the CSO. These are as follows:

		(Rs. crores)
(a)	Total value of construction covered by the commodity-flow approach of which	4780
(i)	construction by and for government administration	1522
(ii)	departmental enterprises	1162
(iii)	non-departmental enterprises	816
(iv)	construction in the private sector	1280

First, the total tax yield has been distributed among the shares of construction of the items indicated above. The share going to government construction is excluded. The share attributable to departmental enterprises relates mostly to railways, Posts and Telegraphs and road transport. Hence, the share of the tax yield attributable to item (ii) can be distributed among the expenditure groups on the basis of their total expenditure on road and railway transport, and communication. The yield attributable to non-departmental enterprises has been allocated on the basis of expenditure on manufactured goods. Private construction can be broken up into private construction of residential buildings and others. On the basis of data published by the CSO it has been assumed that about 60 per cent of private construction goes for private residential buildings and the remaining part goes for non-residential construction. Hence, 60 per cent of the share allotted to private construction has been distributed among various expenditure groups on the basis of expenditure on residential rents and the remaining 40 per cent on the basis of expenditure on manufactured goods. No share has been allotted to agricultural goods because it is assumed that the nature of construction in the agricultural sector is mostly kutcha and there is very little use of cement in such construction works.

7. Coal and coke

This item is used in a number of ways. On the basis of information available in Material and Financial Balances, 1966, we could work out the percentage shares of different uses as follows: electricity thermal 25 per cent; railways 23 per cent; pig iron 12 per cent; soft coke 8 per cent; cement 7 per cent; brick burning 6 per cent; chemicals 2 per cent; paper and paper board 3 per cent; foundries 2 per cent; fertilisers 2 per cent; cotton textiles 2 per cent; engineering works 1 per cent; ceramics and potteries 1 per cent; glass 1 per cent; jute 1 per cent; others 4 per cent. The allocation of tax yield has been done in the following manner. In the case of electricity, 50 per cent on the basis of electricity consumption by households and 50 per cent on the basis of expenditure on manufactured goods; for railways on the basis of expenditure on railway fares; for pig iron on the basis of uses of pig iron discussed in the case of iron and steel; for soft coke on the basis of consumption of coke and coal given in NSS consumption data; for cement, as discussed in the case of cement; for brick burning, according to construction as discussed in the case of cement; for chemicals on the basis of expenditure on manufactured goods; for paper and paper board on the basis of expenditure on books, periodicals, papers, etc.; for foundries on the basis of expenditure on manufactured goods; for fertilisers on the basis of expenditure on agricultural goods; for cotton textiles on the basis of expenditure on cotton fabrics; for engineering works on the basis of expenditure on manufactured goods; for ceramics and potteries on the basis of expenditure on crockery; for glass, 50 per cent through construction as discussed in the case of cement and 50 per cent on the basis of household expenditure on "other utensils"; for jute, as in the case of jute manufactures; for others on the basis of expenditure on manufactured goods.

8. Tyres and tubes.

Production data in regard to automobiles are available in the annual report of the Directorate General of Technical Development (DGTD). The figures for 1973-74 are as follows:

			(Quantity (nos.)
1.	(a)	Commercial vehicles (buses and trucks)	40,580
	(b)	Passenger cars	36,756
	(c)	Jeeps	10,015
	(d)	Three wheelers	12,646
2.	Motor cycles		54,085
3.	Scooters		55,639
4.	Mopeds and scooterettes		29,212

The Transport Research Unit of the Ministry of Shipping and Transport supplied the figures of the total number of registered vehicles, on March, 1974, as follows:

		(Nos.)
(a)	Motor cycles	827906
(b)	Auto-rikshas and scooters	66718
(c)	Jeeps	79467
(d)	Private motor cars	573709
(e)	Taxis	82524
(f)	Buses	97738
(g)	Goods vehicles	319856
(h)	Scooters	2268135

The prices of tyres and tubes have been obtained from the Index Numbers of Wholesale Prices in India. The following were the prices in 1973.

	(Price per unit in rupees)	
	Tyres	Tubes
Dunlop C-49 giant (PV price)	1050.00	95.00

(Price per unit in rupees)

	Tyres	Tubes
Dunlop fort covers	210.00	30.00
Motor cycles	93.00	16.00
Scooter (two and three wheelers)	68.00	11.00

For the purpose of measurement, we have classified all the vehicles given above into the following categories:

	Name of the vehicles	Production	Registration	Price per unit in rupees Tyres	Tubes
(a)	Buses, trucks, etc.	40580	417594	1050	95
(b)	Cars, taxis, jeeps, etc.	46771	7356690	210	30
(c)	Motor cycles	54085	827906	93	16
(d)	Three wheelers	12646	66718)	68	11
(e)	Scooter, two wheelers including scooterettes	114851	220225)		

For working out the incidence, we have to divide the total number of registered vehicles into new and old. From the total number of registered vehicles we deduct the production data to get the number of old vehicles. The production data are taken to represent the number of new vehicles.

We have assumed that new vehicles absorb tyres and tubres (including the additional ones provided with the new vehicles) at the following rates: buses and trucks - 7, cars, taxis and jeeps - 5, motor cycles - 3, three wheelers - 4, scooters - 3.

We take the total consumption of tubes and tyres from two sides (i) production of new vehicles and (ii) demand for replacement for the old vehicles. Looking at the stock and flow figures of vehicles and assuming that a tube and tyre has an average life of not more than two years we deduce that 25 per cent of the tax yield can be attributed to new vehicles and 75 per cent to old vehicles. On the basis of information available about the number of new vehicles for each type, consumption of tube and tyre per vehicle and the prices of tubes and tyres, it has been possible to work out the value of each type of tube and tyre absorbed during the year by new vehicles. Similarly, we have worked out the value of total consumption of each type of tube and tyre for replacement purposes. We have assumed that

all the four wheelers consume twice the number of tyres and tubes as two wheelers and the number of old vehicles are euqal to the total stock minus the production of new vehicles. Then for each type of tyre and tube we have worked out the total expenditure in relation to new vehicles as well as that for replacement. The total tax yield has been divided among different categories of tubes and tyres on the basis of their share in total expenditure. The tax revenue shares thus arrived at have been distributed on the basis of expenditures of households on each type of transport services. The share attributable to trucks, however, has been allocated on the basis of expenditure on manufactured goods.

9. Copper and copper alloys

On the basis of information contained in Material and Financial Balances, 1966, and Input-Output Table for India, 1963, the different uses of copper and copper alloys have been classified into the following categories:

		(Share in per cent of total)
1.	Electrical goods	
	(a) Refrigeration	1
	(b) Telephone and telegraphs	6
	(c) Electric fans	2
	(d) Others*	55
2.	Non-electrical goods (including machinery and equipment)	
	(a) Automobiles	6
	(b) Railway equipment	Negligible
	(c) Food processing machines	2
	(d) Chemical industry equipment	12
	(e) Utensils (domestic)	10
	(f) Others**	6
	Grand total	100

* Includes electric motors, transformers, base copper conductors, PVC and VIR cables, paper insulated wires and cables, switch and control gear.

** Includes pumps and compressors, bolts, nuts, washers, diesel engines and metal products.

For the allocation of tax burden in regard to electrical goods, the methodology is as follows. According to proportions given in CSO's Estimates of Capital Formation in India, 1969, about 80 per cent of refrigeration products goes to households and the remaining 20 per cent to producer sectors. Thus 80 per cent of the total yield of tax on copper attributed to this item can be allocated to the group with per capita expenditure of Rs. 100 and above and the remaining 20 per cent on the basis of total expenditure on (a) allopathic medicines; (b) ice-cream and (c) jam and jellies. In the case of telephone and telegraphs, the tax yield has been distributed among various expenditure groups on the basis of household expenditure on telephones. The CSO assumes that 50 per cent electric fans are being used domestically and the remaining 50 per cent for commercial purposes. This assumption has been used here. The domestic share can be distributed on the basis of household expenditure on electric fans. The remaining 50 per cent can be allocated on the basis of expenditure on manufactured goods. The share attributed to the item 'others' under electrical goods has been allocated on the basis of expenditure on manufactured goods.

The share of non-electrical goods has been allocated in the following manner: (a) automobiles household expenditure on road transport; (b) food processing machines - household expenditure on processed food; (c) chemical industry equipment - in the same manner as for all chemicals indicated above; (d) utensils - household expenditure on manufactured goods.

10. Aluminium

We have the estimates of the uses of this item from Material and Financial Balances, 1966 and Input-Output Table for India, 1963.

		Per cent of total
1.	Electrical equipment of which	64
	(a) Fans	1
	(b) Refrigeration	1
	(c) Radios, etc.	Negligible
	(d) Others*	62
2.	Automobiles	11
3.	Food processing machinery	8
4.	Textile machinery	2
5.	Chemicals and pharmaceuticals	1
6.	Building construction and furniture fixing	5
7.	Domestic Utensils	9
	TOTAL	100

*Includes ACSR conductors and accessories, AA- conductors and accessories, other electrical manufacturing, PVC and BIR cables, paper insulated wires and cables.

Following the methodology of the CSO in regard to the estimation of capital formation, 50 per cent of the share attributable to fans and 80 per cent of the share attributable to refrigeration have been taken to be accounted for by domestic use. These portions can be allocated on the basis of expenditure on electric fans and on "other durable equipment".

The share of automobiles is allocated on the basis of expenditure on road transport. For others we have used the following methodology: food processing - expenditure on processed food by households; textile machinery - on the basis of expenditure on textiles; chemicals - on the same basis as the distribution of tax yield (aggregate) from chemicals; building construction and furniture fixing - on the same basis of allocation as for tax yield from cement for building construction; domestic utensils - expenditure on aluminium utensils.

11. Plywood

The pattern of use of plywood is not available separately. We have, however, information on the consumption pattern of wood. According to Material and Financial Balances, 1966, 78 per cent of the wood is used in construction and 22 per cent of it is used for manufacture of furniture and other purposes. Having no other basis, we have used the following proportions in respect of plywood; (i) 75 per cent for construction; and (ii) 25 per cent for furniture. Plywood is assumed to be used for permanent fixing and fitting in the construction of buildings. The share attributable to residential buildings is allocated to the construction of buildings for the group with per capita expenditure of Rs. 100 and above in the urban sector under the head "expenditure on rent on dwellings". The share attributable to non-residential buildings has been allocated on the basis of expenditure on manufactured goods. The share of the remaining 25 per cent has been allocated to different expenditure groups in the urban sector on the basis of expenditure on furniture.

12. Asbestos

The major part of this material is used in the construction of non-residential buildings like factory buildings, sheds, etc. A small part goes to the construction of residential buildings also. We assume that 75 per cent goes for non-residential buildings and 25 per cent for the construction of residential buildings. The share of tax yield attributable to non-residential buildings can be allocated on the basis of expenditure on manufactured goods and the remaining 25 per cent on the basis of expenditure on house rent by the households in the urban sector.

13. Mosaic tiles

These are taken to be used exclusively in the construction of residential buildings for the group with per capita expenditure of Rs. 100 and above in the urban sector. Hence the tax yield has been entirely allocated to this group.

14. Cinematograph films and projectors

Allocation has been done on the basis of household expenditure on cinemas.

15. Crown corks and pilfer proof caps

Allocation has been done on the basis of household expenditure on beverages (aerated water).

16. Lead unwrought

On the basis of information conatined in Material and Financial and Balances, 1966, we have allocated this material to different uses in the following manner: automobiles 35 per cent; electricity 30 per cent; paints and varnishes 16 per cent; printing metals and alloys 13 per cent; chemical plants and equipment 4 per cent; and construction 2 per cent.

Tax yield has been allocated in the following manner: (a) automobiles - on the basis of expenditure on road transport; (b) electricity - 50 per cent on the basis of household expenditure on electricity and the remaining 50 per cent on the basis of expenditure on manufactured goods; (c) paints and varnishes - on the same basis as for paints and varnishes; (d) printing metals and alloys - household expenditure on paper, periodicals and books; (e) chemical plants and equipment - on the basis of the distribution ratios used for all chemicals; (f) construction - as in the case of other construction inputs.

17. Electrical insulators, stamping wires, cables and others

50 per cent of the tax yield from these commodities has been allocated on the basis of expenditure on manufactured goods by households and the remaining 50 per cent on the basis of consumption of electricity by them.

18. Slides, zip and fasteners

The whole amount of tax yield from slides, zip and fasteners has been allocated on the basis of household expenditure on suitcase, attache and kitbag.

19. Rolling bearings, welding electrode and permanent magnet.

The total yield from rolling bearings, welding electrodes and permanent magnet has been allocated on the basis of total expenditure on manufactured goods.

20. Safes, strong boxes, etc.

The tax yield from safes, strong boxes, etc., made of hard metals has been allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector.

21. Rubber products (including synthetic rubber) other than tyres and tubes

There are three main uses of rubber products, namely, (i) leather footwear (4 per cent); (ii) jute textiles (5 per cent); (iii) household consumption (91 per cent).

The share of household consumption, i.e., item (iii) has been allocated to different expenditure groups on the basis of total expenditure on items like (a) rubber cushion and (b) footwear other than that of leather. The share attributable to leather footwear has been allocated on the basis of household expenditure on leather footwear which includes leather boots and shoes, leather sandles and chappals, and other leather footwear. In the case of jute textiles, the distribution has been made on the same basis as in regard to jute fabrics.

22. Chinaware and porcelain

These items are purchased by households as well as hotels and restaurants. As we do not have data on household expenditure on hotels and restaurants, we have allocated the entire yield on the basis of NSS household expenditure on crockery and chinaware.

23. Glass and glassware

Based on data contained in Material and Financial Balances, 1966 and Input-Output Table for India, 1963 , we have allocated the yield to different uses in the following proportions; construction - 17 per cent; electrical equipment 8 per cent; domestic purpose 42 per cent; and drugs and pharmaceutical 33 per cent. In the case of construction we have first divided building construction into urban residential and urban non-residential. The share allocated to urban residential has been distributed on the basis of rents (urban dwellings). In the case of the share of non-residential buildings, the allocation has been done on the basis of total expenditure on manufactured goods. The share of electrical equipment has been allocated on the basis of households expenditure on other non-durable electrical goods. The share attributable to domestic uses has been distributed on the basis of household expenditure on crockery and chinaware assuming that those who spend on crockery and chinaware spend on glassware also in more or less the same proportion. The share of drugs and pharmaceuticals has been allocated on the basis of expenditure on all types of medicines.

24. Typewriter ribbons

We have taken 50 per cent as being used by the government sector and the remaining 50 per cent by the private sector. The share of private use has been allocated on the basis of expenditure on manufactured goods.

25. Gases

Fifty per cent of the share has been allocated on the basis of expenditure of households on gases. The other 50 per cent has been allocated on the basis of expenditure on manufactured goods.

26. Synthetic resins and plastic materials.

The tax revenue collected from this item has been allocated on the basis of household expenditure on plastic goods.

27. Linoleum

Allocation has been done on the basis of expenditure on manufactured goods.

28. Tin plates

Based on information contained in Material and Financial Balances, 1966 and Input-Output Table for India, 1963, the tax yields have been distributed in the following manner: construction 44 per cent; electricity 12 per cent; manufactured goods 33 per cent; and domestic utensils 11 per cent.

29. Zinc

The allocation of the yield has been done on the basis of expenditure on (i) manufactured goods 85 per cent; and (ii) domestic utensils 15 per cent.

30. Iron ore

The same methodology as for iron and steel.

C. Capital Goods and Partly Capital Goods.

1. Internal combustion engines

Information about the uses of this item could be obtained from the Input-Output Table for India, 1963. It is used for (a) motor vehicles 80 per cent; (b) air and gas compressors, etc. 10 per cent; and (c) other industries 10 per cent.

The share of motor vehicles has been allocated in the same manner as done in case of motor vehicles discussed later. The share of air and gas compressors has been allocated on the same basis as for refrigeration because the compressors are used mostly in the production of refrigerators. The share of other industries has been allocated on the basis of expenditure on manufactured goods.

2. Electric Motors

According to the information contained in Input-Output Table for India, 1963, the uses are as follows: (i) agricultural use 89 per cent; (ii) textile machinery 2 per cent; (iii) machine tools 3 per cent; (iv) air-conditioners 2 per cent; (v) photographic and optical goods 2 per cent; (vi) construction and machinery 1 per cent; (vii) ships and vessels 1 per cent.

The share of item (i) is allocated to different expenditure groups on the basis of expenditure on agricultural goods; item (ii) on the same basis as the allocation of tax yield from cotton textiles; item (iii) on the basis of expenditure on manufactured goods; item (iv) on the basis of household expenditure on air-conditioners; item (v) on the basis of expenditure on cinema; and item (vi) and (vii) on the basis of expenditure on manufactured goods.

3. Office machines

The yield is distributed among different expenditure groups on the basis of expenditure on manufactured goods.

4. Power driven pumps

These pumps are used mostly in agriculture for the purpose of irrigation. The yield has been distributed on the basis of household expenditure on agricultural goods.

5. Fork lift trucks, platform.coated abrassive and grinding wheels

The aggregate yield from all these items has been allocated to different expenditure groups on the basis of expenditure on manufactured goods.

6. Partly capital and partly household goods

A part of such goods is purchased by households and the remaining by entrepreneurs. The part attributable to entrepreneurial use in each case has been distributed on the basis of expenditure of the households on manufactured goods. For the remaining shares the methodology is indicated for each item separately.

7. Photographic Cameras

According to the proportions in CSO's Estimates of Capital Formation in India, 1969, 50 per cent of this item is taken to be used for domestic purposes and the remaining 50 per cent for entrepreneurial purposes. Thus 50 per cent of the yield has been allocated on the basis of expenditure on manufactured goods and the remaining 50 per cent has been allocated on the basis of expenditure on "other durable goods".

8. Motor vehicles

50 per cent of the motor cars produced in the country have been taken to go for entrepreneurial purposes and the remaining 50 per cent for domestic use. This percentage is based on the information obtained directly from car manufacturers. The share of domestic use has been allocated to the households having monthly per capita expenditure of Rs. 100 and above in the urban sector. The remaining 50 per cent has been allocated on the basis of household expenditure on manufactured goods.

9. Steel furniture

50 per cent of the steel furniture produced has been taken by the CSO as going for household use. Thus 50 per cent of the yield has been allocated to different expenditure groups on the basis of expenditure on furniture. The remaining 50 per cent has been allocated on the basis of expenditure on manufactured goods.

10. Wireless receiving sets

10 per cent of the total value of output is taken to represent capital goods and 90 per cent to represent consumer durables. Thus, 90 per cent of the tax yield has been distributed among different expenditure groups in the rural and urban sectors on the basis of expenditure on radios; and the remaining 10 per cent on the basis of expenditure on manufactured goods.

11. Refrigerating and air-conditioning appliances

According to the CSO, 20 per cent is used by the entrepreneurs and 80 per cent by the households. But the latest information obtained directly from the manufacturers like Kelvinator of India, Ltd. and other indicates that about 70 per cent goes to households and 30 per cent for capital formation. We have used the latest information for working out the incidence. The tax

yield attributable to households has been allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector. The share going to entrepreneurs has been distributed on the basis of expenditure on manufactured goods.

12. Electric fans

50 per cent of the expenditure on them is taken to be by households. Thus 50 per cent of the yield has been distributed on the basis of expenditure on electric fans and the remaining 50 per cent on the basis of expenditure on manufactured goods.

13. Electric supply meters.

It is assumed that 50 per cent of the purchases is by households and the remaining 50 per cent by entrepreneurs. The share attributable to households is distributed on the basis of consumption of electricity, and the remaining share on the basis of expenditure on manufactured goods.

D. Components of Capital and Partly Capital Goods.

1. Motor vehicle parts and accessories

70 per cent of the tax yield has been allocated to households and has been distributed on the basis of expenditure on cars. The remaining 30 per cent of the tax yield is allocated to different expenditure groups in the rural and urban sectors on the basis of their expenditure on manufactured goods.

2. Electric batteries and parts thereof, tool tips, bolts, nuts, etc.

The total yield has been allocated to different expenditure groups on the basis of expenditure on manufactured goods.

3. Parts of wireless receiving sets

The same methodology as for wireless receiving sets.

II. IMPORT DUTIES

Imported items have been classified into the following groups for the purpose of working out the incidence:

A. Mostly in the nature of consumption goods;

B Mostly in the nature of intermediate goods;

C. Capital goods and parts thereof; and

D. Partly capital goods and parts thereof.

A. Import of Goods Mostly in the Nature of Consumption Goods

Most of these goods are consumed by the higher income groups. Therefore, the yield of import duties on them has been allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector. A list of such goods along with the value of tax yield in each is presented in the following Table.

TABLE 4

Imported Goods Assumed To Be Consumed By The Highest Per Capita Expenditure Group in the Urban Sector.

S. No.	Items	Revenue from the import duty in 1973-74 (Rs. lakhs)
1.	Ghee	2
2.	Other milk products	1
3.	Other meat (animal products)	308
4.	Fish fresh and dry	5
5.	Other vegetables	2
6.	Other fresh fruits	962
7.	Other drinking beverages	6
8.	Pickles and sauce	2
9.	Other processed food	230
10.	Betel nuts (supari)	3
11.	Cigarettes	1

Contd.

S. No.	Items	Revenue from the import duty in 1973-74 (Rs. lakhs)
12.	Leaf tobacco)	
	)	
13.	Hookah tobacco)	
	)	26
14.	Cheroot)	
	)	
15.	Other tobacco products)	
	)	
16.	Foreign liquor	274
17.	Cloth for shirt, pyjama, kurta, blouses etc.	136
18.	Cloth for coat, trousers, suit,overcoat, etc.	30
19.	Readymade garments	11
20.	Hosiery articles, stockings, banian and underwears	4
21.	Rugs and blankets	Negligible
22.	Cloth for upholstery, curtain,fabric cloth	7
23.	Cinematograph films	218
24.	Sports goods, toys, etc.	25
25.	Books and journals	1
26.	Tooth paste and tooth powder	Negligible
27.	Electric bulbs and tube lights	49
28.	Other toilet requisites	20
29.	Toilet articles	13
30.	Shaving blades	Negligible
31.	Other non-durable electrical goods	300
32.	Umbrella and rain coats	2

Contd.....

S. No.	Items	Revenue from the import duty in 1973-74 (Rs. lakhs)
33	Plastic goods	555
34.	Suitcase, attache and kitbag	3
35.	Foam rubber, cushion, (dunlop pillow type)	107
36.	Other musical instruments	27
37.	Jewels and pearls	329
38.	Enamel utensils	10
39.	Fountain pen	Negligible
40.	Spectacles	3
41.	Clock and watch	109
42.	Salt	1
43.	Homeopathic medicines	21
44.	Floor matting	11

There are some imported goods which cater for mass consumption. The methodology for each of these is given below:

1. Foodgrains and products like floor and starch

Allocation has been done on the basis of expenditure on foodgrains (rice, wheat, barley, jowar, maize, bajra) in the urban sector.

2. Babyfood and milk powder

From the publication 'Monthly Statistics of the Foreign Trade of India, we find that most of the imports under this head are in the form of milk powder. Out of an import of Rs. 525 lakhs worth of these goods, about Rs. 510 lakhs were spent on dry milk powder and the remaining on varieties of condensed milk. We have assumed therefore that most of these imports are sold in urban sector

as under government milk schemes. Thus, we have allocated the entire yield on the basis of expenditure on milk by households in the urban sector.

3. Linseed oil, refined oil or essential oil (all sorts) edible oils and oil seeds.

We have allocated the tax yields from these items on the basis of expenditure on these items by different expenditure groups in the rural and urban sectors.

4. Pepper, dry chillies and other spices

Allocation has been done on the basis of household expenditure on spices (pepper, dry chillies and other spices).

5. Paper - all sorts

We import various types of paper, Broadly, they can be devided into (i) news print and (ii) others. Others include all sorts of high strength and special grade paper which are used mostly for packing and accounting purpose and include carbon papers etc. Out of the total value of imports of paper, news print paper accounts for about one third. The remaining two thirds are accounted for by all other kinds of paper. Having no other basis we have allocated two third of the total tax yield among different expenditure groups on the basis of their expenditure on manufactured goods, one third of the yield is distributed on the basis of expenditure on periodicals and newspapers.

6. Allopathic medicines, other drugs and patents

Allocation has been done on the basis of expenditure on allopathic medicines.

B. Imports Mostly in the Nature of Intermediate Goods.

There are a large number of intermediate consumption goods which are imported from abroad but they are produced in the country also and their uses are more or less the same. The allocation of the import duty on all such imported intermediate goods as have supplementary domestic production is the same as indicated for intermediate goods domestically produced. A list of such goods is given below:

Imports	Domestic production
Chemicals products	
1. Manures, all sorts	1. Fertilisers
2. Paints and colours	2. Paints and varnishes
ii) paints, colours and painters' materials.	
3. Dye intermediaries	3. Synthetic organic dye stuff
ii) Coupling dyes	

Imports		Domestic production	
	iii) Dye from coal for fast colours		
	iv) Dye derived from coal tar		
	v) Dyeing and tanning substances		
4.	Sodium compounds	4.	Sodium silicate
Chemical products			
5.	Caustic soda	5.	Caustic soda and caustic potash
6.	Soda ash	6.	Soda ash
	ii) Nitrate of soda		
7.	Calcium carbide	7.	Calcium carbide, bleaching powder and sodium hydrosulphate
8.	Acids	8.	Acids
	i) Acetyle salicylic acid		
	ii) Acid olic		
	iii) Betaoxy Nephthoic acid		
	iv) Acid phospheric		
Petroleum products			
9.	Calcined petroleum coke	9.	Coal, coke and patent fuel.
10.	Asphalt, crude and refined coal tar	10.	Asphalt bitumen and coal tar
11.	All sorts of mineral and industrial oils:	11.	Furnace oil
12.	Diesel oil	12.	Refined diesel oil and diesel oil not otherwise specified.
	ii) High speed diesel oil		
13.	Lubricating oil	13.	Blended or compounded lubricating oils and greases
14.	Petroleum crude	14.	As in the case of petroleum products

Imports		Domestic production
15.	Kerosene	15. Kerosene oil
16.	Motor spirit	16. Motor spirit
Metals		
17.	Zinc white, zinc wrought and zinc sheets	17. zinc
18.	Steel	18. The total tax yield from imported steel has been classified into different groups from the point of view of uses and accordingly allocation has been made.
19.	Copper	19. Copper
	a) Copper wrought and manufactures of copper	Copper and copper alloys
	b) copper scraps	
	c) Copper unwrought ingots	
	d) Copper welding wires	
	e) Extended copper rods	
	f) Copper pipes and tubes	
	g) Copper wire	
20.	Aluminium	20. Alluminium
	a) Aluminium in any crude form	
	b) Aluminium conductors, sheets circles, strips and foils	Aluminium sheets
21.	Tin black	21. Tin plates
22.	Lead wrought, sheets, ingots, pigs and bead	

Imports		Domestic production	
Other goods			
23.	Rubber products	23.	Rubber raw
24.	Cork manufacture	24.	Crown corks
25.	Building and engineering materials	25.	Construction inputs
26.	Marbles and stones	26.	Mosaic tiles
27.	Glass and glass wares including sheet and plate glass	27.	Glass and glass wares
28.	Wood and timber	28.	Plywood
29.	Artificial and synthetic resins	29.	Plastic materials and synthetic resins
30.	Electric valves	30.	Electric valves and tubes
31.	Asbestos manufactures	31.	Asbestos

The yields from the following imported items can be apportioned among different expenditure groups in the rural and urban sectors on the basis of expenditure on the relevant or related items as indicated in each case. Where the treatment is different it is separately dealt with.

Imported goods		NSS matching consumption items	
1.	China clay	1.	China clay crockery-only in the urban sector for the groups with per capita monthly expenditure exceeding Rs. 55/-.
2.	Chalk, lime (special kind)	2.	Tooth paste, tooth powder
3.	Cement, not otherwise specified	3.	House rent in the urban sector only
4.	Hides and skins (raw and salted)	4.	Leather goods in the urban sector only for the per capita monthly expenditure groups of Rs. 75/- and above
5.	Coral, cowries and shells	5.	Ornaments
6.	Ivory manufactured	6.	Ornaments
7.	Seeds not otherwise classified	7.	Agricultural goods

Imported goods		NSS matching consumption items	
8.	Rubber seeds	8.	Rubber products
9.	Hops (agent for beer and medicines)	9.	50 per cent allopathic medicine and 50 per cent foreign liquor
10.	Barks and tanning	10.	Leather goods
11.	Cutch and gambier material (used by gold heaters)	11.	Ornaments
12.	Gums, resins and lac	12.	Plastic goods
13.	Plumbago and graphite	13.	Stationery articles
14.	Printers ink	14.	Books, periodicals and newspapers
15.	Essential synthetic oil	15.	Refined oil
16.	Fur skins	16.	For the per capita monthly expenditure group of Rs. 100 and above in the urban sector under the head woollen fabrics
17.	Wood pulp	17.	As in case of paper
18.	Silk worm cocoon	18.	Silk cloth
19.	Wool raw and wool tops	19.	Woollen cloth
20.	Raw cotton	20.	Cotton fabrics
21.	Raw flax, jute raw hemp	21.	Jute fabrics
22.	Sisal and aloe fibre	22.	Superfine cotton fabrics
23.	Staple fibre	23.	Cotton superfine fabrics
24.	Artificial silk yarn	24.	Artificial silk
25.	Yarn (excluding cotton yarn)	25.	Artificial silk
26.	Glass bead and false pearls	26.	Ornaments in the urban sector
27.	Gold and silver sheets and plates	27.	Gold and silver ornaments
28.	Brass rods brass wires	28.	Brass utensils

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Other goods			
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10.	Barks and tanning	10.	Leather goods
11.	Cutch and gambier material (used by gold heaters)	11.	Ornaments
12.	Gums, resins and lac	12.	Plastic goods
13.	Plumbago and graphite	13.	Stationery articles
14.	Printers ink	14.	Books, periodicals and newspapers
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16.	Fur skins	16.	For the per capita monthly expenditure group of Rs. 100 and above in the urban sector under the head woollen fabrics
17.	Wood pulp	17.	As in case of paper
18.	Silk worm cocoon	18.	Silk cloth
19.	Wool raw and wool tops	19.	Woollen cloth
20.	Raw cotton	20.	Cotton fabrics
21.	Raw flax, jute raw hemp	21.	Jute fabrics
22.	Sisal and aloe fibre	22.	Superfine cotton fabrics
23.	Staple fibre	23.	Cotton superfine fabrics
24.	Artificial silk yarn	24.	Artificial silk
25.	Yarn (excluding cotton yarn)	25.	Artificial silk
26.	Glass bead and false pearls	26.	Ornaments in the urban sector
27.	Gold and silver sheets and plates	27.	Gold and silver ornaments
28.	Brass rods brass wires	28.	Brass utensils

Imported goods		NSS matching consumption items	
29.	Yellow metal alloys	29.	Ornaments
30.	Plastic and rubber insulated wires	30.	Electricity
31.	Electrical accessories made of plastics	31.	Electricity
32.	Batteries	32.	50 per cent radios and 50 per cent torches
33.	Molasses	33.	Alcohol
34.	Batteries for motor vehicles	34.	Motor vehicles
35.	Articles made of stone or marble	35.	House rent in urban area in the per capita monthly expenditure group of Rs. 100 and above.
36.	Some other chemicals	36.	As in the case of chemicals as a whole for Central excise
37.	Saccharine alkaloids of opium and their derivatives and iodine in any crude form	37.	On the basis of expenditure on allopathic medicines
38.	Paints, solutions and compositions containing petroleum	38.	Paints and varnishes
39.	Silver wire, gold plates and gold leaf	39.	Gold and silver ornaments
40.	Stainless steel plates, sheets and strips	40.	Steel utensils
41.	Brass pipes, tubes and ingots	41	Fifty per cent on the basis of expenditure on manufactured goods and fifty per cent on that on brass utensils
42.	Earthenware pipes and sanitary ware	42.	50 per cent on earthenware and 50 per cent on residential rent both in the urban sector for the groups with per capita monthly expenditure of Rs. 75/- and above.

The yield from the following items has been allocated to different expenditure groups on the basis of their expenditure on manufactured goods.

Titanium dioxide; Ball bearings; Roller bearings; All articles otherwise not specified; Sulphur; Jute bailing hoops; Gums and stick on seed lac; Batteries not otherwise specified; Nickel pellets; Covered crucibles for glass making; All non-ferrous alloys not otherwise specified; Hardware iron mongering; non-ferrous nickel alloys; Packing, engine; Lithopone; Metallic ores all sorts; Twist and yarn of flax and jute; Nichrome and other electrical resistance wires; All non-ferrous metals; Cobalt chromium, tungsten, etc. Antimony ore in any form; Paste board, milk board and card board.

C. Imports of Capital Goods and Parts thereof

We can allocate only 10 per cent of the yield in 1973-74 assuming the average life of the assets to be 10 years. The basis of allocation in each case is indicated below.

Item		Basis of allocation	
1.	Iron and steel-railway track	1.	50 per cent on the basis of expenditure on manufactured goods, and the remaining 50 per cent on the basis of passengers' railway fares
2.	Cutlery all sorts (2)	2.	Allocated to the groups in the urban sector with per capita expenditure above Rs. 75/- on the basis of their expenditure on cooked food
3.	Metal furniture	3.	50 per cent on the basis of expenditure on manufactured goods, and the remaining 50 per cent on the basis of expenditure on furniture.
4.	Hurrican lanterns	4.	15 per cent (CSO estimate) is treated as capital formation and is allocated on the basis of expenditure on manufactured goods. The remaining 85 per cent is allocated to the per capita expenditure group of Rs. 100 and above in the urban sector.
5.	Zip fasteners	5.	As in the case of domestic production but allocated to the per capita expenditure groups Rs. 75-100 and above per month.
6.	Textile machinery	6.	As has been done in the case of cotton and woollen fabrics.
7.	Printing and lithographic presses	7.	Expenditure on books, newspapers, journals and periodicals.

Item		Basis of allocation	
8.	Agricultural implements	8.	On the basis of expenditure on agricultural goods.
9.	Dairy and poultry farming appliances	9.	Expenditure on milk products and poultry
10.	Knitting machines	10.	Expenditure on knitted garments including cotton millmade, cotton handloom, cotton khadi and wool, art silk and pure silk)
11.	Electric motors	11.	As in case of domestic production of electric motors
12.	Boot and shoe manufacturing machinery	12.	As in case of footwear
13.	Cinema projecting apparatus	13.	Household expenditure on cinema
14.	Oil crushing machinery	14.	Expenditure on all types of edible oils
15.	Petroleum gas well drilling equipment	15.	As in the case of petroleum products
16.	Refrigerating machinery	16.	As in the case of refrigerators
17.	Sound recording appliances	17.	Expenditure on cinema
18.	Sugar manufacturing machinery	18.	Expenditure on sugar
19.	Machine for carding, spinning wheel, cotton textile machinery, textile machinery and parts and looms of all kinds.	19.	On the basis of the proportions obtained in respect of the domestic production of textiles
20.	Power distribution transformers	20.	As in the case of electricity
21.	Electrical instruments apparatus and appliances	21.	As in the case of domestic production of electrical appliances
22.	Electric medical apparatus	22.	Expenditure on allopathic medicines
23.	Wireless transmission apparatus	23.	Expenditure on communication
24.	Tramcars and components	24.	Expenditure on conveyance in the urban sector

Item		Basis of allocation	
25.	Railway materials, components and parts	25.	As in the case of railway track
26.	Conveyance not otherwise specified	26.	Expenditure on other conveyance
27.	Carriage carts and parts thereof	27.	Expenditure on road conveyance
28.	Sparking plugs	28.	Expenditure on cars, motor cycles and scooters
29.	Single cylinder fuel injection pumps	29.	Expenditure on cars
30.	Nozzle holders	30.	Expenditure on motor vehicles
31.	Aeroplane parts	31.	Expenditure on hired conveyance other than road, water-ways and railways
32.	Optical instruments	32.	Expenditure on spectacles
33.	Photographic instruments	33.	As in the case of domestic production of such instruments
34.	Typewriters	34.	As in the case of domestic production
35.	Office machines	35.	50 per cent treated as government purchases; the remaining 50 per cent is allocated on the basis of expenditure on manufactured goods.

In the case of the following capital goods the allocation of the tax yield has been done on the basis of expenditure on manufactured goods:

Grinding wheels; Machinery like prime motors and boilers; Mining machinery; Carbon electric; Ships and other vessels; Components of machining; Passenger lifts; Machinery and parts; Instruments, apparatus and appliances.

D. Imports of Partly Capital Goods and Parts thereof

1. Other furniture

It is assumed that the whole of imported furniture is meant for private household consumption for the group with per capita expenditure of Rs. 100 and above in the urban sector. Thus the entire yield is allocated to this group.

2. Electric fan

The entire yield is allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector under the head ' electric fan '

3. Motor cycle, scooter and parts thereof

The entire yield is allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector under expenditure on scooters.

4. Motor car

Government import is taken to be negligible. The whole of the amount is allocated to the group with per capita expenditure of Rs. 100 and above in the urban sector under the head of expenditure on car.

5. Complete wireless receivers

Allocated to the groups with per capita expenditure of Rs. 100 and above in the urban sector under the head expenditure on radios.

6. Refrigerators and parts thereof

The allocation is the same as in the case of domestic production.

7. Sewing machines

Half of the yield is attributed to domestic use by the group with per capita expenditure of Rs. 100 and above in the urban sector and the remaining half is allocated to different expenditure groups on the basis of expenditure on cotton and woollen fabrics.

8. Bicycles and parts thereof

Allocated to the households in the urban sector on the basis of expenditure on cycles.

9. Accessories of motor vehicles

The treatment is the same as in the case of domestic production of motor vehicles.

10. Rubber products other than tyres and tubes

The allocation has been done in the same way as in the case of domestic products of rubber products other than tyres and tubes.

11. Brushes all sorts

The yield has been allocated to urban households with per capita expenditure of Rs. 100 and above under the head expenditure on toilet requisites.

12. Parts of shoe manufacturing machinery

Allocation has been done in the same way as in the case of shoes produced domestically.

13. Parts of electric medical appliances

Allocation has been done on the basis of expenditure on allopathic medicines.

14. Components and parts of amplifiers and loud speakers

The allocation has been done on the basis of expenditure on radios.

It may be noted that duties on some of the imported goods which were imported specifically for the government sector were ignored. These are mainly horses, animals, globes and uranium.

III STATES TAXES

A. Sales Taxes

As indicated in the text, we were able to obtain estimates of commodity-wise yield of sales tax (including Central sales tax) from 13 major States. On this basis, the commodity-wise yield of sales tax in all India (all States combined) was estimated.

The allocation of the burden of sales tax on commodities also subject to excise duties was done in the same manner as for the latter. The allocation of the burden of sales tax on other commodities did not raise any special problems as there were more or less corresponding entries in the NSS consumption data.

B. Electricity duty

Annual Statistical abstract of Indian Union, published by the CSO gives a detailed break-up of the uses of electricity in quantity for all the States and Union territories taken together and also for individual States and Union territories. The latest abstract available is for the year 1974 which contains data for 1972-73. According to this information, the share of each type of use in the total consumption of electricity is as follows:

		(Million kw)	(Percentage of total)
1.	Domestic	4309	9.78
2.	Commercial	2852	5.81

		(Million kw)	(Percentage of total)
3.	Industrial power at low and medium voltage	4546	9.26
4.	Industrial power at high voltage	27698	56.43
5.	Agricultural	5918	12.06
6.	Traction	1761	3.59
7.	Public lighting	520	1.06
8.	Public water works and sewage pumping	1094	2.23
9.	Miscellaneous	390	0.78
	TOTAL	49088	100.00

In the absence of any other information, the share attributable to public lighting, public water works and sevage pumping and miscellaneous (all taken together) has been distributed among various expenditure groups on the basis of rents paid (actual as well as imputed) by urban households. This allocation is based on the assumption that, in the final analysis, the urban house dwellers bear the burden according to the housing facilities enjoyed by them. The share for agricultural use has been distributed on the basis of household expenditure on agricultural goods. The share of traction has been allocated on the basis of expenditure on railway fares and expenditure on manufactured goods, each getting 50 per cent.

C. State motor vehicle tax

The Motor Vehicles Tax collections can broadly be classified under (i) motor cycle; (ii) private cars (including jeeps); (iii) taxis inclusive of autorikhsha; (iv) buses (P.S.V.); (v) goods vehicles; and (vi) miscellaneous.

The tax revenue figures for each of these groups are available from the CSO's annual publication, Statistical Abstract of Indian Union. The latest information related to the year 1970-71. The relative shares of the tax revenue of each of these groups obtaining in 1970-71 have been assumed for 1973-74 also. In the case of motor cycles, private cars and taxis, the distribution among the various expenditure groups in the rural and urban sectors has been done in accordance with the relative shares of expenditure on these items as given in the NSS. However, care has been taken to deduct 4 per cent of the total tax yield (share of Government vehicles) before the allocation. In the case of buses the allocation has been done on the basis of expenditure on household bus taxes. As regards goods and miscellaneous vehicles, 50 per cent of the tax yield has been distributed among the various expenditure groups on the basis of expenditure on agricultural goods and the remaining 50 per cent on the basis of expenditure on manufactured goods.

E. Goods and passenger taxes

The report of the Taxation Enquiry Committee, Uttar Pradesh (1974) gives data on the tax burden of the passenger tax (on 52-seated buses) and goods tax (on trucks with 9 tonnes RLW and

13 tonnes RLW) for 1972-73. The information is available for 8 States, namely, Uttar Pradesh, Karnataka, Kerala, Tamil Nadu, Andhra Pradesh, Bihar, Gujarat and Madhya Pradesh. Such data are also available for Maharashtra. Information regarding the number of vehicles registered in India with the above break-up is available from Statistical Abstract of Indian Union, 1974. The number of buses (52-seated) has been multiplied by the tax burden to get the total yield from the passenger tax. A similar exercise has been done for trucks (9 tonnes and 13 tonnes RLW) to get the total tax yield from goods tax. The proportions between the two tax yield figures have been applied to the all-India figure of passenger and goods tax yield in 1973-74 to work out the share of each of the items. The share allocated to passenger tax has been distributed among various expenditure groups on the basis of expenditure on bus fares; 50 per cent of the share of goods tax has been distributed on the basis of expenditure on agricultural goods and the remaining 50 per cent on the basis of expenditure on manufactured goods.

F. State Excise Duty

On the basis of the average of the figures obtained from Uttar Pradesh, Gujarat, Kerala, Madhya Pradesh, Maharashtra, Punjab, Rajasthan and West Bengal, we have broken down the aggregate tax yield into the following groups; (i) country spirit, (ii) country fermented liquor, (iii) opium and (iv) foreign liquor. The distribution has been done on the basis of expenditure on these items. Country spirit has been taken to represent country liquor and country fermented liquor has been taken to represent toddy.

G. Entertainment Tax

On the basis of data obtained for four States, namely, Uttar Pradesh, Karnataka, Maharashtra and Punjab, the aggregate tax collection figure is broken down into: (i) cinema theatre and (ii) 'fair'. The share of each group has been distributed among various expenditure groups on the basis of expenditure on the two groups of items.

H. Other taxes

They include mostly cess on sugarcane, tax on raw jute, tobacco duty and betting tax. Cess on sugarcane has been distributed on the basis of household expenditure on sugar and the raw jute tax has been allocated on the basis of expenditure on manufactured goods and agricultural goods as in case of intermediate consumption of jute. Tobacco duty has been allocated on the basis of expenditure on tobacco. Betting tax has been allocated on the basis of household expenditure on fair.

IV THE METHOD OF ESTIMATING GOVERNMENT SHARE OF INDIRECT TAXES

For the purpose of measuring the incidence of indirect taxation on households as discussed earlier, it has been decided that the share of the tax revenues attributable to general government consumption and capital formation should be excluded from the computation. The taxes paid by the Government on goods purchased for consumption or capital formation represent only accounting transfers and hence they need not be considered to result in a net burden on the private sector. It might be indicated that Government consumption is measured by the current expenditure on goods

and services and wages of only the government administrative departments including defence. Government capital formation is normally taken to include capital formation by the government administrative departments as well as by the departmental enterprises of the government. For the purpose of the present study, however, we have excluded capital formation by the departmental enterprises.

Full details of commodity-wise information on purchases made by the Central Government, State governments and the local authorities are not available. The Director General of Supplies and Disposal (DGS&D) publishes, annually, Directory of Government Purchases giving commodity-wise values of purchases made by the Governments. The DGS&D data, however, suffer from three main limitations. Firstly, the coverage of the data is partial because there are no statutory requirements for all the Central and State Government agencies to make purchases only through DGS&D. Secondly, government purchases of less than Rs. 20, 000 in the case of defence and Rs. 5000 in case of other ministries are made directly by Government departments and other government agencies, a greater part of which is not reflected in the purchases shown in the Directory. Thirdly, separate information on purchases made by the administrative departments of the Central and State Governments and those by departmental and non-departmental undertakings of the Central and State Governments are not available. The information contained in the Directory gives only a break-up into (a) purchases made through DGS&D, and (b) orders placed directly by the Government departments, government undertakings, etc. On the basis of this break-up, it is not possible to seggregate the share of purchases made by government administrative departments.

Information contained in the Input-Output Table for India, 1963, could not be used for the reason that the estimates relate to the year 1963 and since then the pattern of government consumption has undergone a great change.

Again, the estimates of fixed capital formation given in the Input-Output Table for India relate to the entire economy and separate information for the government administrative departments is not made available. For more or less the same reasons, we could not use also the information contained in the Material and Financial Balances, 1966 for drawing estimates of purchases of different categories of commodities by the government sector.

In the absence of any other source of information for the present study, reliance has been placed on the information on public consumption contained in the Technical Note of the Planning Commission (See A Technical Note on the Approaches to the Fifth Plan of India 1974-79, published in 1973). The Technical Note gives information on the value of purchases made by the government for consumption (public consumption) in 1973-74 at 1971-72 prices along with the value of total gross output in the economy and the total value of imports for a large number of commodities.

A list of goods purchased for public consumption along with the value of purchase in the year 1973-74 at 1971-72 prices for each item as contained in the Planning Commission's Technical Note is given below. It might be pointed out that the gross value of output includes the value of output used for intermediate consumption as well as for final uses. The value of intermediate consumption does not enter into the picture because such goods are purchased by entrepreneurial units of the economy (Government and non-government) which are in a position to pass on the incidence to households and government administrative departments through the sale of their output.

TABLE 5

Value of public consumption goods in 1973-74 (valued at 1971-72 prices)

(Rs. crores)

S. No.	Items	Public consumption	Gross output
1	2	3	4
1.	Animal husbandry	2.1	4065.0
2.	Forestry	16.4	686.3
3.	Coal	1.8	296.3
4.	Sugar and gur	0.6	762.1
5.	Vegetable oil	0.6	533.9
6.	Tea and coffee	1.2	391.5
7.	Other food products	25.4	2451.7
8.	Cotton textiles	27.4	2350.0
9.	Jute textiles	63.5	413.6
10.	Other textiles	38.9	588.6
11.	Miscellaneous textile products	14.5	688.4
12.	Wood products	45.9	381.2
13.	Paper and paper products	64.6	239.2
14.	Leather products	11.2	191.9
15.	Rubber products	25.7	354.0
16.	Plastics	1.8	152.4
17.	Cosmetic and drugs	2.5	492.5
18.	Other chemicals	4.4	720.8
19.	Petroleum products	27.6	297 9
20.	Other non-metal mineral products	1.3	725.0

1	2	3	4
21.	Bolts and nuts	0.9	53.4
22.	Metal containers	5.7	67.3
23.	Other metal products	29.9	916.0
24.	Office domestic equipment	4.7	56.7
25.	Electric wires	32.4	232.1
26.	Electronics	19.0	80.5
27.	Batteries	6.1	59.6
28.	Electrical household goods	8.0	98.6
29.	Telephone and telegraphs equipment	1.4	53.6
30.	Other electricals	57.1	260.7
31.	Motor cycle	0.4	120.6
32.	Motor vehicles	51.5	477.0
33.	Ship and boats	7.6	43.7
34.	Aircraft	4.5	40.5
35.	Rail equipment	12.0	352.5
36.	Other transport equipment	24.4	53.4
37.	Miscellaneous scientific instrument	7.8	37.3
38.	Other industries	6.2	433.8
39.	Printing	4.1	176.1
40.	Electricity	22.0	1025.3
41.	Construction	350.4	4856.7
42.	Railways	7.3	1203.0
43.	Other transport	25.0	1476.9
44.	Other services	3753.0	12454.3

We find three types of goods purchased for government consumption: (i) some goods mostly in the nature of consumption goods (ii) some in the nature of capital goods; and (iii) the remaining in the nature of services. Items 1 to 25 and 27 are consumption goods; item 26 and 28 to 38 and 41, capital goods and items 39, 40, 42, to 44, services. In the case of those goods which are mostly in the nature of consumption goods, the procedure of estimating the government share of indirect taxes is simple. We have the ratios of the value of government consumption to the total value of output plus import in respect of each item. This ratio has been applied to the total value of tax yield for each commodity (including sales tax) separately to work out the share of tax yield allocable to government consumption. In some cases, however the break-up of government consumption in the necessary detail is not available. In all such cases, many taxable items have been clubbed together to make them comparable to government consumption items.

Expenditure on goods of a capital nature for defence purposes only are treated as expenditure on consumption. The goods of a capital nature indicated in the above table under public consumption represent goods meant for defence purposes. Most of these goods are free from excise duties. Those which are subject to duties have been dealt with in the same fashion as we have done in the case of goods mostly in the nature of consumption goods.

The main difficulty arises in the case of capital formation. The estimates of gross fixed investment given in the Technical Note include capital formation in the government administrative departments. Item-wise information on fixed investment by Government administration, however, is not available. The methodology followed for estimating item-wise value of capital formation by the administrative departments is as follows.

In the case of construction, following the CSO practice, it is assumed that government construction falls into the category of those works which need material inputs. They are covered by the commodity-flow approach of estimation of capital formation in India by the CSO. We could obtain from the CSO value of construction falling into the category of commodity-flow approach broken up into government administration and the rest. The amount of tax yield worked out for construction inputs can be broken up into government administration and the rest on the basis of the ratio of the value of government construction in 1973-74 under the commodity-flow approach to the total value of construction under the commodity-flow approach.

For items of the nature of fixed capital investment in machinery and equipment, we do not have separate item-wise break-up into government administration and the rest. In the case of motor cars and motor cycles, however, the Directore General of Technical Development was in a position to give the percentage of total cars and motor cycles produced (4 per cent) going to government administrative departments of the Central and State Governments. Therefore, 4 per cent of tax yield from car and motor cycles has been taken as attributable to government administrative departments. The remaining items of capital formation in Government administration is taken to be negligible and hence ignored. Construction in the government sector and purchase of motor cars and motor cycles by the government cover a very large part of the value of capital formation by government administrative departments. According to the CSO, these two items cover above 95 per cent of gross fixed investment in government administration.

APPENDIX 10

STATISTICAL INFORMATION RELATING TO CONSUMPTION EXPENDITURE AND INDIRECT TAX BURDEN

The basic statistical information relating to per capita, per annum consumption expenditure, indirect tax burden in terms of percentages are presented in three tables as under:—

Table 1 - Per capita, per annum, Consumer expenditure, indirect tax burden and indirect tax burden as percentage of consumer expenditure (1973-74) .

Table 2 Total annual cash purchase expenditure as percentage of total annual expenditure.

Table 3 Expenditure on major items by urban households as percent of total consumer expenditure.

TABLE 1 OF APPENDIX 10

PER CAPITA, PER ANNUM CONSUMER EXPENDITURE, INDIRECT TAX BURDEN AND INDIRECT TAX BURDEN AS PERCENT OF CONSUMER EXPENDITURE (1973-74)[1]

Monthly per capita expenditure group (Rs.)	R U R A L							
	0-15	15-28	28-43	43-55	55-75	75-100	100 & above	All house holds
1	2	3	4	5	6	7	8	9
Total consumer expenditure Rs. per capita per annum	164.66	311.20	478.55	653.01	855.11	1146.46	1907.89	713.74
Amount of tax Rs. per capita per annum								
CENTRAL TAXES	2.76	5.80	12.36	24.04	36.37	72.48	196.45	35.58
1. Central excise	2.34	4.66	9.60	19.07	27.93	55.56	150.17	27.46
2. Import duty	0.42	1.14	2.76	4.97	8.44	16.92	46.28	8.12
STATES TAXES	2.03	4.57	8.92	16.30	21.02	42.38	111.99	21.72
1. State excise	0.37	0.83	1.52	4.10	3.18	10.63	34.80	5.22
2. Sales tax	1.04	2.55	4.66	7.57	10.46	18.99	46.22	10.01
3. Sales tax on motor spirit	0.06	0.10	0.24	0.43	0.73	1.26	3.37	0.64
4. Motor vehicles tax	0.25	0.48	0.94	1.45	2.14	3.51	7.82	1.88
5. Taxes on goods and passengers	0.17	0.31	0.76	1.29	2.03	3.60	8.21	1.78
6. Entertainment tax	0.00	0.00	0.18	0.29	0.73	1.33	3.67	0.61
7. Electricity duty	0.11	0.22	0.44	0.74	1.21	1.98	5.00	1.04
8. Other taxes and duties	0.03	0.08	0.18	0.43	0.54	1.08	2.90	0.54
ALL INDIRECT TAXES	4.79	10.37	21.28	40.34	57.39	114.86	308.44	57.30
Tax as percentage of consumer expenditure (percent)								
CENTRAL TAXES	1.68	1.86	2.58	3.68	4.25	6.32	10.30	4.99
1. Central excise	1.42	1.50	2.01	2.92	3.27	4.85	7.87	3.85
2. Import duty	0.26	0.37	0.58	0.76	0.99	1.48	2.43	1.14
STATES TAXES	1.23	1.47	1.86	2.50	2.46	3.70	5.87	3.04
1. State excise (on liquor)	0.22	0.27	0.32	0.63	0.37	0.93	1.82	0.73
2. Sales tax	0.63	0.82	0.97	1.16	1.22	1.66	2.42	1.40
3. Sales tax on motor spirit	0.04	0.03	0.05	0.07	0.09	0.11	0.18	0.09
4. Motor vehicles tax	0.15	0.15	0.20	0.22	0.25	0.31	0.41	0.26
5. Taxes on goods and passengers	0.10	0.10	0.16	0.20	0.24	0.31	0.43	0.25
6. Entertainment tax	0.00	0.00	0.04	0.04	0.09	0.12	0.19	0.09
7. Electricity duty	0.07	0.07	0.09	0.11	0.14	0.17	0.26	0.15
8. Other taxes and duties	0.02	0.03	0.04	0.07	0.06	0.09	0.15	0.08
ALL INDIRECT TAXES	2.91	3.33	4.45	6.18	6.71	10.02	16.17	8.03

Table I (contd.)

Statistical Appendix

PER CAPITA, PER ANNUM CONSUMER EXPENDITURE, INDIRECT TAX BURDEN AND INDIRECT TAX BURDEN AS PERCENT OF CONSUMER EXPENDITURE (1973-74)

Monthly per capita expenditure group (Rs.)	U			R	B	A	N	
	0-15	15-28	28-43	43-55	55-75	75-100	100 & above	All house holds
	10	11	12	13	14	15	16	17
Total consumer expenditure Rs. per capita per annum	166.73	329.49	497.05	671.74	879.75	1179.35	2164.41	971.86
Amount of tax Rs. per capita per annum								
CENTRAL TAXES	4.04	12.32	22.67	40.11	66.95	110.92	454.33	116.87
1. Central excise	4.04	10.25	18.65	33.18	55.00	91.68	363.12	94.54
2. Import duty	0.00	2.07	4.02	6.93	11.95	19.24	91.21	22.33
STATES TAXES	2.01	8.48	13.92	24.78	37.38	63.67	199.05	57.65
1. State excise	0.00	0.44	0.09	1.31	1.40	9.32	49.10	9.77
2. Sales Tax	0.50	5.14	8.85	14.88	21.60	32.55	89.02	28.86
3. Sales tax on motor spirit	0.00	0.23	0.41	0.88	2.05	2.99	8.73	2.56
4. Motor vehicles tax	0.00	0.82	1.25	1.84	2.86	3.75	17.95	4.72
5. Taxes on goods and passengers	0.00	0.55	0.87	1.40	2.55	3.46	8.60	2.94
6. Entertainment tax	1.51	0.55*	1.18	2.46	3.77	6.84	18.85	5.29
7. Electricity duty	0.00	0.49	0.86	1.44	2.16	3.14	7.43	2.62
8. Other taxes and duties	0.00	0.26	0.41	0.57	0.99	1.62	1.37	0.89
ALL INDIRECT TAXES	6.05	20.80	36.59	64.89	104.33	174.59	653.38	174.52
Tax as percentage of consumer expenditure (per cent)								
CENTRAL TAXES	2.42	3.74	4.56	5.97	7.61	9.41	20.99	12.03
1. Central excise	2.42	3.11	3.75	4.94	6.25	7.77	16.78	9.73
2. Import duty	0.00	0.63	0.81	1.03	1.36	1.63	4.21	2.30
STATES TAXES	1.21	2.57	2.80	3.69	4.25	5.40	9.20	5.93
1. State excise (on liquor)	0.00	0.13	0.02	0.20	0.16	0.79	2.27	1.01
2. Sales tax	0.30	1.56	1.79	2.22	2.46	2.76	4.11	2.97
3. Sales tax on motor spirit	0.00	0.07	0.08	0.13	0.23	0.25	0.40	0.26
4. Motor vehicles tax	0.00	0.25	0.25	0.27	0.33	0.32	0.93	0.49
5. Taxes on goods and passengers	0.00	0.17	0.18	0.21	0.29	0.29	0.40	0.30
6. Entertainment tax	0.91	0.17	0.24	0.37	0.43	0.58	0.78	0.54
7. Electricity duty	0.00	0.15	0.17	0.21	0.25	0.27	0.34	0.27
8. Other taxes and duties	0.00	0.08	0.08	0.08	0.11	0.14	0.06	0.09
ALL INDIRECT TAXES	3.63	6.31	7.36	9.66	11.86	14.80	30.19	17.96

Table I (contd.)

Statistical Appendix

PER CAPITA, PER ANNUM CONSUMER EXPENDITURE, INDIRECT TAX BURDEN AND INDIRECT TAX BURDEN AS PERCENT OF CONSUMER EXPENDITURE (1973-74)

Monthly per capita expenditure group (Rs.)	R U R A L & U R B A N C O M B I N E D							
	0-15	15-28	28-43	43-55	55-75	75-100	100 & above	All house holds
	18	19	20	21	22	23	24	25
Total consumer expenditure Rs. per capita per annum	165.75	312.91	481.29	656.57	860.75	1156.78	2006.09	765.13
Amount of tax Rs. per capita per annum								
CENTRAL TAXES	2.93	6.41	13.88	27.10	43.37	83.38	295.14	51.77
1. Central excise	2.43	5.18	10.94	21.76	34.13	65.80	231.67	40.82
2. Import duty	0.40	1.23	2.94	5.34	9.24	17.58	63.47	10.95
STATES TAXES	2.04	4.94	9.67	17.90	24.76	48.43	145.30	28.88
1. State excise	0.35	0.79	1.30	3.57	2.77+	10.26	40.27	6.12
2. Sales tax	1.02	2.79	5.28	8.96	13.01	22.84	62.80	13.76
3. Sales tax on motor spirit	0.05	0.11	0.27	0.51	1.03	1.75	5.42	1.03
4. Motor vehicles tax	0.34	0.52	0.99	1.53	2.31	3.58	11.70	2.45
5. Taxes on goods and passengers	0.16	0.34	0.78	1.31	2.15	3.56	8.36	2.01
6. Entertainment tax	0.08	0.05	0.33	0.70	1.43	2.89	8.71	1.54
7. Electricity duty	0.11	0.24	0.50	0.87	1.42	2.31	5.93	1.36
8. Other taxes and duties	0.03	0.10	0.22	0.45	0.64	1.24	2.31	0.61
ALL INDIRECT TAXES	4.97	11.35	23.55	45.00	68.13	131.81	440.44	80.65
Tax as percentage of consumer expenditure (percent)								
CENTRAL TAXES	1.72	2.05	2.88	4.13	5.04	7.21	14.71	6.77
1. Central excise	1.47	1.66	2.27	3.31	3.97	5.69	11.55	5.34
2. Import duty	0.24	0.39	0.61	0.81	1.07	1.52	3.16	1.43
STATES TAXES	1.24	1.58	2.01	2.73	2.88	4.19	7.24	3.77
1. State excise on (liquor)	0.21	0.25	0.27	0.54	0.51	0.89	2.01	0.80
2. Sales tax	0.62	0.89	1.10	1.36	1.51	1.98	3.12	1.80
3. Sales tax on motor spirit	0.03	0.04	0.06	0.08	0.12	0.15	0.27	0.13
4. Motor vehicles tax	0.15	0.17	0.21	0.23	0.27	0.31	0.58	0.32
5. Taxes on goods and passengers	0.10	0.11	0.16	0.20	0.25	0.31	0.42	0.26
6. Entertainment tax	0.05	0.02	0.07	0.11	0.17	0.25	0.43	0.20
7. Electricity duty	0.07	0.08	0.10	0.13	0.16	0.20	0.30	0.18
8. Other taxes and duties	0.02	0.03	0.05	0.07	0.07	0.11	0.12	0.08
ALL INDIRECT TAXES	2.96	3.63	4.89	6.85	7.92	11.40	21.96	10.54

1. (i) The aggregated value of consumer expenditure for the household sector calculated on the basis of NSS data is lower than the corresponding CSO estimate. The NSS estimates have therefore been blown up to match the CSO estimates.

(ii) The measurement excludes tax-revenue collected from Government purchases and taxes into account only one-tenth of the tax-revenue collected from capital goods. These two items account for about 14 percent of the revenue collected from indirect taxes.

+ The estimates of the consumption of liquor as per NSS data is less for the expenditure group Rs.55-75 compared to group-

x NSS consumer expenditure on contry liquor for the expenditure group Rs.28-43 is less than for the expenditure group Rs.15-28. Rs.43-55.

• NSS consumer expenditure on Cinema theatre etc. is less for the expenditure group Rs.15-28 than for the groups Rs.0-15 & Rs.24-43.

TABLE 2 of Appendix 10

Total Annual Cash Purchase Expenditure As Per Cent of Total Annual Expenditure.

Monthly per capita expenditure group (in rupees)	Rural	Urban	All India
	Total annual cash purchase expenditure as per cent of total annual expenditure.	Total annual cash purchase expenditure as per cent of total annual expenditure	Total annual cash expenditure as per cent of total annual expenditure
0-15	64	81	65
15-28	63	93	66
28-43	61	93	66
43-55	60	94	66
55-75	59	93	67
75-100	61	93	70
100 & above	72	96	82
All households	62	94	70

TABLE 3 OF APPENDIX 10

Expenditure on major items by urban households as percent of total consumer expenditure

Sl. No.	Items	0-15	15-28	28-43	43-55	55-75	75-100	100 & above	All households
	1	2	3	4	5	6	7	8	9
1.	Total food items of which	68.49	72.40	72.59	70.10	67.78	63.18	52.29	62.43
	1.1 Total cereals	41.52	47.89	43.53	37.64	32.47	25.78	13.59	26.84
	1.2 Milk & Milk Products	0.91	2.91	5.71	7.59	9.40	10.37	10.45	9.16
	1.3 Beverages & refreshment	13.33	4.41	4.11	4.47	4.96	5.96	10.99	7.10
	1.4 Edible oil	3.33	4.62	5.30	5.78	5.88	5.95	5.30	5.23
	1.5 Vegetables	4.24	4.29	4.88	4.90	4.85	4.89	3.61	4.42
	1.6 Meat, egg and fish	1.52	3.08	2.90	3.23	3.49	3.62	3.48	3.40
	1.7 Sugar	2.73	3.08	3.59	3.67	3.82	3.70	2.56	3.29
	1.8 Tea and Coffee	0.91	2.12	2.57	2.82	2.91	2.91	3.31	2.99
2.	Clothing	0.00	1.29	1.55	2.31	3.23	4.27	8.01	4.77
	(of which cotton fabrics)	0.00	1.29	1.52	2.12	2.96	3.45	4.93	3.44
3.	House rent*	0.74	0.67	0.66	2.25	2.59	3.72	5.05	3.44
4.	Fuel and light	7.88	7.86	7.20	6.78	6.64	6.06	4.73	5.97
	(of which kerosene)	0.91	1.12	1.24	1.35	1.31	1.23	1.01	1.19
5.	Transport	1.15	1.04	1.41	1.00	1.48	1.88	3.59	2.15
	(of which bicycle)	0.00	0.00	0.00	0.00	0.00	0.17	0.15	0.09
6.	Medicines	0.91	0.62	0.99	1.27	1.67	2.15	2.82	2.01
	Total (1 to 6)	79.17	83.88	84.39	83.71	83.39	81.26	76.49	80.75

Note: Total expenditure consists of cash and non-cash expenditure

* It includes rent for garage and residential land

SOURCE: National Sample Survey, 28th Round; October 1973. June 1974.

APPENDIX 11

TEXTILE - A FACTUAL STUDY

Clothing is one of the basic necessities of life, next only to food, As civilisation progressed and man made advances in other fields, the art of textile production also developed making use of cotton, wool, silk and finally man-made fibres and yarns. In India, the textile industry is one of the major industries giving vast employment and uses cotton, wool and silk as well as man-made fibres and yarn like rayon, viscose, acetate, polyester and nylon. Enclosed Statement 1 gives an idea of the trend of production of different yarns - natural and man-made since 1970.

2. Enclosed Statement 2 shows the production of woven fabrics of cotton, man-made fibres/ yarn and blends thereof in the mill sector as well as in the decentralised sector, during 1971-76. In this period, the production of cloth increased by about 3.3 per cent while the increase in population was of the order of 8.3 per cent.

3. The following table shows the pattern of consumption and per capita availability of different fabrics over the last 5 years:

TABLE

Year	Cotton	Per capita availability in metres		
		Blended/ mixed fabrics	Man-made fibres fabrics	Total
1972	13.18	0.36	1.59	15.13
1973	12.04	0.44	1.46	13.94
1974	12.88	0.36	1.36	14.60
1975	12.58	0.61	1.37	14.56
1976 (Provisional)	11.36	0.97	1.40	13.73

4. Over the years the per capita availability is showing a declining trend. The per capita consumption of all textiles in India is estimated at around 2 kgs. which is about 30 per cent of the world average consumption of about 7 kgs. We are predominently depending on cotton, almost to the extent of about 87 per cent as against the world average of about 50 per cent.

5. Textiles constitute a major group in the central excise tariff, comprising 16 items with a large number of sub-classifications. It is expected to contribute a revenue of about Rs.720 crores (about 16 per cent of the total estimated excise (net) during 1977-78. Enclosed Statements 3 and 4 show the item-wise estimated excise and customs revenues during 1977-78.

6. In the following paragraphs, we examine the tax structure on textiles under the following broad-heads:

1. Cotton textiles
2. Man-made fibres (including yarn and fabrics)
3. Woollens.

COTTON

7. Cotton textile industry in India is one of the largest in the world and caters to almost 87 per cent of the total clothing needs of the masses of India. The cotton mill industry has a weightage of as much as 17.43 in the index of industrial production. While, the mill sector provides employment to about a million workers, handlooms and power looms give jobs to several millions directly and many more millions indirectly. According to a study, handloom, which is the country's biggest cottage industry, provides jobs for about 10 million persons. It is estimated that Khadi provides employment to nearly one million persons (about 8.20 lakhs in only cotton fabrics). Further, a large number of small scale ancilliary and auxiliary industries depend on the working of this industry. The number of hosiery and garment manufacturers depending on this industry is very large.

8. The various sectors of the cotton textile industry can be broadly grouped in three categories - (1) Spinning Sector, (2) Weaving Sector and (3) Processing Sector. In the spinning sector, cotton yarn is spun either by independent spinning mills or by composite mills who do both spinning of yarn as well as weaving and processing of fabrics. The weaving sector consists of mills, power looms and hand looms and khadi. In the processing sector, apart from the composite mills, independent processors, process the cloth with or without the aid of power/steam.

9. The present capacity of the industry in various sectors has been shown in Statement 5. Statements 6 and 7 respectively show the production, consumption and deliveries of cotton yarn, and category-wise production of mill-made cotton fabrics, during the period 1972-76. While the consumption of cotton yarn in the decentralised sector (vide Statement 6) has increased considerably with a corresponding increase in production of cloth, share of mill-made cloth in the total production has declined to 48.9 per cent (as against 52.9 per cent in 1972). Further, within the mill-made cloth family, there is a rising trend of production of medium A, medium B and coarse fabrics vis-a-vis production of fine and superfine fabrics.

10. The production of mill-made cotton cloth during January-June, 1977 has come down to 1723.33 million metres as against 1996.32 million metres during the corresponding period of 1976. This is partly due to the multifibre policy introduced from 1st January 1977, under which it is mandatory on the cotton textile industry to use at least 10 per cent non-cotton fibres. The following Table gives the comparative figures of production of cloth in the mill sector.

TABLE

CLOTH WOVEN IN THE MILL SECTOR
(in million metres)

Six months January-June	Cotton cloth	Man-made fibres fabrics	Total	Percentage of 3 to 4
1.	2.	3.	4.	5.
1975	2005.94	97.76	2103.70	4.6
1976	1996.32	141.05	2137.37	6.6
1977	1723.33	301.30	2024.63	14.9

(The figures above indicate that the percentage of man-made fibre fabrics to the total quantity of fabrics has been increasing year after year).

DUTY STRUCTURE - COTTON YARN

11. The excise system in India may be said to have commenced in 1894 with the levy of duty on cotton yarn of finer counts. This was, later abolished in 1924-25. The duty was re-imposed in 1961, when in order to raise additional revenue and partly to tax hosiery and certain other fabrics which did not bear any duty, a duty was levied on cotton twist, yarn and thread. However, this duty was not applicable to yarn in hanks used by handlooms in weaving of fabrics such as dhoties, sarees etc. Enclosed Statements 8 and 9 give the details of tariff changes from inception till date. Statement 8 shows the changes in rates of duty applicable to yarn consumed by composite mills working under compounded levy procedure under which the yarn duty was discharged by them at the time of clearance of fabrics with reference to the category and area of fabric manufactured from such yarn. Statement 9 details the changes made in duty on other yarn (i.e. yarn other than that consumed for weaving of cotton fabrics by composite mills working under compounded levy procedure). The important changes made since the inception of the excise duty on cotton yarn are discussed below.

12. With a view to have some progression in the incidence of duty, instead of two-count groups, four-count groups were created in 1962 with higher duty rates for superior yarn. In 1964, the definition of 'manufacture' in relation to cotton yarn was enlarged to include sizing, beaming, warping, winding, reeling or conversion from one form to another. Simultaneously, duty on yarn (other than in hank) particularly, those on fine and superfine counts, was increased. This was done to raise additional revenue and also to transfer a large portion of the total incidence of duty from the fabric stage to yarn stage. An increase in duty on fine and superfine was also made in view of the high profits being made on such yarn spun from imported cotton. In 1966, again, to restrain the consumption of finer qualities of cloth, which required imported cotton, duty on yarn (other than

coarser counts of cotton) was increased. Since then many changes have been made in the duty to keep an appropriate margin of duty incidence in favour of powerloom vis-a-vis composite mill fabrics; to give relief to the industry in 1969 when it was passing through a bad time; to give protection to the handlooms; to raise additional revenues and to step up the ad valorem incidence of the specific rates of duty applicable to cotton yarn.

13. As a measure of rationalisation and to avoid assessment disputes, tariff description of the Item was amended in 1972 to restrict the levy under this only to such yarn which contained 90 per-cent or more by weight of cotton. But there was no change in the duty on cotton yarn.

14. In 1977, the duty structure of cotton yarn, now redefined as yarn in which cotton is predominant, has been changed completely and is given below. These rates are applicable to yarn consumed whether by composite mills or by others. (The compounded levy procedure for discharging duty liability on yarn consumed by composite mills has been withdrawn).

			Per kg.
(a)	Yarn containing more than 1/6th by weight of non-cellulosic fibre.		Rs. 18.00
(b)	Other—		
	(i)	of counts not exceeding 25s	1.5 paise per count
	(ii)	of counts exceeding 25s but not exceeding 35s.	40 paise plus four paise per count exceeding 25s.
	(iii)	of counts exceeding 35s but not exceeding 45s.	80 paise, plus 8 paise per count exceeding 35s.
	(iv)	of counts exceeding 45s but not exceeding 55s	Rs. 1.60 plus 14 paise per count exceeding 45s.
	(v)	of counts exceeding 55s	5.5 paise per count.

Note:- Single and multiple fold yarn in plain (straight) reel hanks has been wholly exempted. Further, duty on yarn in cross reel hanks is also reduced by 30 paise per kg. if yarn is purchased for the handlooms.

From the above rate structure it would be observed that the rate of duty changes with change of every count of the yarn.

15. The following table shows the ad valorem incidence of the specific rates of duty on cotton yarn of certain counts of a number of mills whose price schedule was studied.

TABLE

S. No.	Description	Ex factory prices Oct., 1977 Rs. per kg.	Duty Rs. per kg.	Ad valorem incidence expressed as percentage of Ex-factory price.
1.	2.	3.	4.	5.
1.	2/20s Grey Cotton yarn - Cross reel hanks	17.62	0.30	1.70
2.	4/20s Grey Cotton yarn - on Cones	21.60	0.30	1.38
3.	2/24s Grey Cotton yarn - Cross reel hanks	18.15	0.36	1.98
4.	2/30s Grey Cotton yarn - Cross reel hanks	21.37	0.60	2.80
5.	30s Grey Cotton yarn - on cones	21.80	0.60	2.75
6.	2/40s Grey Cotton yarn - on cones	22.80	1.20	5.21
7.	2/40s Grey Cotton yarn - Cross reel hanks	20.48	1.20	5.85
8.	2/40s Bleached Cotton - Cross reel hanks.	23.68	1.20	5.07
9.	40s in cones	17.60	1.20	6.81
10.	60s Carded on Cone	25.00	3.30	13.20
11.	60s Combed on Cone	29.00	3.30	11.38
12.	90s in Cones	35.20	4.95	14.06
13.	2/120s mercerised	67.05	6.60	9.84

It will be seen that even on yarn of the same count, the incidence of duty varies. This is due to the fact that the present rate structure ignores the factors, such as whether the yarn is grey, bleached, dyed, mercerised, or is carded or combed, or is on cones or beams etc.

16. Excise duty on cotton fabrics was first levied in the year 1896 to improve the competitive position of the Lancashire cloth in the Indian market. This duty continued till 1926 when it was abolished. Excise duty on cotton fabrics was reintroduced with effect from 1st January, 1949 by an Ordinance. To start with, duty was imposed on Superfine cloth at 25 per cent ad valorem, the rates in respect of Fine, Medium and Coarse Cloth being nil. From 1-3-1949, fine cloth was charged to duty at 6¼ per cent ad valorem and for Medium and Coarse cloth, a uniform rate of duty of 3 pies per yard was prescribed. In 1953, even for Superfine and Fine fabrics, specific rates of duty were prescribed. With effect from 1.3.1955, the basis of categorisation of fabrics into Superfine, Fine and Medium and Coarse was changed from the count of the warp yarn to the average count of both warp and weft yarn. Simultaneously, the unit of assessment was changed from linear yard to square yard which subsequently in 1960 was changed to square metre. In 1953, Handloom cess under the Khadi and Handloom Industries Development (Additional) Excise Duty Act, 1953 was levied on cotton fabrics, the present rate being 1.9 paise per square metre.

DUTY STRUCTURE - COTTON

17. In May, 1955, for smaller powerloom units, an alternate "Compounded levy procedure" was introduced. Under this, the duty liability is discharged on payment of an amount determined with reference to the number of powerlooms. The rates of compounded levy and the method of computation were changed several times. With the exemption of grey fabrics produced on powerlooms, the compounded levy procedure has been withdrawn from 18-6-1977, except in the case of 'unauthorised' powerlooms.

18. From 14-12-1957, additional excise duty in lieu of sales tax has been levied on cotton fabrics. In July, 1958, Medium category was sub-divided into Medium A and Medium B, increasing thereby the total number of categories to 5. Simultaneously, the effective rates for each of the five categories were fixed, according as the fabrics were grey, bleached shrink-proof or organdie processed, etc. As the rates of duty differed according as the fabric was grey or processed, the excise control was extended to the independent processors also. To meet the demand of the smaller processing units, specified quantity of fabric was allowed free of duty; this concession was ultimately withdrawn in 1968.

19. In 1960, the tariff description was amended to bring in handloom fabrics within the excisable category. However, through a notification such fabrics were exempted. Further a residuary category "Cotton fabrics N.O.S." was added to cover certain types of fabrics like non-woven Bonded fabrics and Malimo type of fabrics.

20. Since then the rates of duty have been changed several times. These changes are given in Statement 10 (enclosed). The important changes including those involving changes in classification and scope of levy are discussed below.

21. In 1961, the duty on Medium 'A' grey fabrics was increased by 25 per cent to reduce the wide gap between the rates of duty on Fine and Medium 'A' fabrics, which had resulted in a major shift in production from the former to the later.

22. The general structure of duty on cotton cloth and yarn was revised in 1962. Keeping in view the improvement in quality and price of cloth as a result of processing like mercerisation and shrink proofing/organdie processing as compared to bleaching, dyeing and printing, duty on such fabrics was stepped up. Alongside, to secure that the common man had not to make anything more than a marginal adjustment in his expenditure on Coarse and Medium cloth which he normally uses, duty on Coarse unbleached cloth was reduced.

23. In 1964, the duty on grey cotton fabrics was partly transferred to yarn and to the processing stage. Processing duty on cotton fabrics was rationalised by increasing duty on processed Superfine, Fine and Medium 'A' fabrics with a corresponding relief extended to shrink proofed/organdie processed Medium 'B' and Coarse fabrics. With the reduction of duty on grey fabrics compounded levy rates applicable to powerloom units were reduced and powerloom units having 50 looms or more were accorded a concessional duty of 80 per cent of the rates applicable to composite mills.

24. In the subsequent years, as in the case of cotton yarn, excise duty rates were changed on cotton fabrics too with a view to restraining consumption of finer qualities of cloth which required imported cotton; to increase the incidence of duty on sophisticated varieties of processed fabrics; to reduce the gap in duty between powerloom and composite mill fabrics; to give relief to the industry when it was in a bad shape in 1969; and to raise additional resources either for the Centre or for the States. While enhancing the rates of duty, care was taken that the increase was only on superior category of fabrics or fabrics subjected to the sophisticated processes and on the costlier fabrics. In the same year, i.e., 1969, the basis of levy of duty was changed from specific to ad valorem in respect of fabrics such as suitings, gaberdine, furnishings, coatings, tapestry, turkish cloth etc. which were then paying a low duty in relation to their price. Similarly, in 1973 duty was changed to ad valorem on the blended fabrics containing certain percentage of non-cellulosic fibres/filament yarn but still classifiable as cotton fabrics.

25. Prior to 15th March, 1976, rates of excise duty on most cotton fabrics were specific and their incidence did not depend on the price of the fabric. There were also considerable difficulties in administering the tariff in an industry with many differences of variety. Accordingly, the specific rates of duty were replaced by ad valorem duties in 1976. This step was also intended to "give relief to the weaker and more vulnerable sections of society who consume lower priced varieties of cloth" and to "shift the burden to those who have the ability to pay the higher prices for superior varities of cloth". In order to stimulate the use of long staple cotton, the definition of Superfine, Fine and Medium 'A' fabrics was revised so as to extend the coverage under the higher medium and fine categories. Although, the rates were changed to ad valorem, categorisation of fabrics based on the average count of yarn was maintained. The lower rates of duties were levied on coarser fabrics, mainly on the assumption that these were used largely by the poorer sections. To provide protection to the handloom industry, the compounded levy rates for powerloom units were increased.

26. In 1977, major changes in the tariff description and the duty structure on cotton fabrics were made. The tariff description was amended to levy duty under this Item only on such fabrics in which cotton is predominant or those fabrics which contain more than 40 per cent by weight of cotton and 50 per cent or more by weight of non-cellulosic fibre/yarn. The ad valorem rates of duty depending on the average count of the yarn used in the fabrics were replaced by a duty rate structure related to the value slabs of the fabrics irrespective of their category such as Superfine and Fine. The

composite mills were exempted from payment of yarn duty, the incidence having been transferred to the fabric stage. Non-power/steam processed fabrics were completely exempted and the duty on powerloom fabrics processed by independent power processors was fixed at 50 per cent of the duty applicable to mill-made fabrics. The powerloom units were exempted from the compounded levy duty. Subsequently, in view of the representations received from the various sectors of the industry, modifications have been made in the rates of duty as it was felt "that a sudden change in the long standing rate structure which was based on the counts of yarn rather than on the actual price of fabrics would create disturbances in the market and might result in increase in the cost of certain varieties of coarse and medium fabrics, while simultaneously bringing about some decrease in the case of cheaper varieties of fine and superfine cloth". The decentralised sector is also understood to have represented that the reduction in duty on fine and superfine fabrics based on value slabs would have a damaging effect on them. Keeping these factors in view, the following changes were made in July, 1977 at the time of consideration of the Finance Bill:

(a) the duty on yarn consumed by the composite mills was revived and charged separately at the rates applicable to yarn consumed by the decentralised sector ;

(b) the duty on fabrics having yarn of average count of 41s or more (i.e. fine and superfine fabrics) was fixed at 15 per cent irrespective of its value; and

(c) the duty on controlled cloth and drill was also reduced by 50 per cent of the normal duty.

27. The present rates of excise duty applicable to cotton fabrics are as under:—

(1) Cotton fabrics in which the average count of yarn is 41s or more — 15 per cent ad valorem

(2) Other cotton fabrics whose value per sq. metre - Rupees per sq. metre.

	Exceeds	does not exceed	Per cent ad valorem
(i)	-	4	2
(ii)	4	6	3
(iii)	6	7	4
(iv)	7	8	6
(v)	8	9	8
(vi)	9	10	10
(vii)	10	11	12
(viii)	11	12	14
(ix)	12		15

(a) In the case of handloom fabrics processed by approved independent processors, the appropriate rate of duty gets reduced to a prescribed extent; duty is nil if new fabrics are processed by a factory owned by a registered handloom cooperative society or any organisation set up or approved by the Government for the development of handlooms.

(b) In the case of powerloom fabrics or handloom fabrics not covered by (a) above and processed by an independent processor, the appropriate rate of duty gets reduced by 30 per cent subject to a prescribed maximum extent.

(c) In the case of price controlled cloth, namely, dhoti, sarees, long cloth, shirting and drill, the appropriate rate of duty is reduced by 50 per cent.

(d) In the case of drill, other than at (c) above, the appropriate rate of duty is reduced by 50 per cent.

(e) Inter alia, the following cotton fabrics are exempt:

(i) Unprocessed handloom fabrics;

(ii) Unprocessed cotton fabrics (excepting a few varieties) manufactured on authorised powerlooms;

(iii) Fabrics processed without the aid of power or steam;

(iv) Processed Khadi;

(v) Hosiery.

28. The above discussion of excise duty on cotton yarn and cotton fabrics brings out the following important facts:

(i) Duty on cotton yarn is specific and is dependent on its count and ignores other considerations.

(ii) Cotton yarn cleared in straight (plain) reel hanks, which is normally consumed by the handloom sector, is wholly exempt; duty on cross reel hank yarn is reduced by 30 paise per kg. if such yarn is for the handlooms.

(iii) Unprocessed handloom cloth is wholly exempt; handloom fabrics processed by specified category of processors either is wholly exempted or pays duty at a lower rate;

(iv) Unprocessed cotton fabrics (except a few varieties) manufactured on authorised powerlooms are exempted.

(v) Duty on cotton fabrics in which average count of yarn is 41s or more is 15 per cent ad valorem irrespective of the value of the fabric; on other fabrics rate of duty is related to the value.

(vi) There is a lower rate of duty on handloom or powerloom fabrics processed by an independent processor.

(vii) Duty on price controlled cloth and on drill is 50 per cent of the normal duty.

(viii) Khadi, hosiery and fabrics processed without the aid of power or steam are wholly exempted from fabric duty.

29. DUTY INCIDENCE The table below shows the production of cotton yarn and cotton fabrics and the excise revenue collected therefrom during the period 1972-73 to 1976-77 and also estimated revenue during 1977-78.

TABLE

Year	Production				Excise Revenue Rs. crores		
	Yarn million kg.	Cloth million metres			Yarn	Cloth	Total
		Mill-made	Handloom and powerloom	Total			
1972-73	972	4,224	3695	8026	33.65	81.65	115.30
1973-74	1,000	4,084	3863	8071	33.78	94.48	128.26
1974-75	1,025	4,450	3817	8409	55.94	109.15	165.09
1975-76	1,002	3,962	4129	8391	73.34	109.47	182.81
1976-77	963	3,739	3944	8107	72.40	118.10	191.26
1977-78 (Budget Estimate)					47.23*	160.93*	208.16*

*includes effects of 1977-78 Budget changes.

Source : Handbook of Statistics of Cotton Textile Industry, Indian Cotton Mills' Federation, Bombay and Directorate of Statistics and Intelligence, Central Excise & Customs, New Delhi.

It will be seen that on total cotton cloth production of 8107 million metres in 1976-77 excise duty collected on yarn was Rs.72.40 crores and on cloth it was Rs. 118.10 making a total of Rs. 191.26. Thus, while the impact of yarn duty on cloth was 8.92 paise per metre, the cumulative impact of yarn and cloth duties works out to 23.59 paise per metre. The market Research Wing of the Textiles Committee (Government of India, Ministry of Commerce) has estimated the average price of cotton textiles in 1976 as Rs.4.91 per metre. After making an allowance of 35 per cent, which is understood to be the normal difference between the ex-factory price and retail price, the average ex-factory price could be placed at Rs.3.41 per metre. The cumulative incidence of duty on cloth would, thus, be about 6.9 per cent of the average ex-factory price.

30. On the basis of the present rates of excise duties on cotton yarn and fabrics, cumulative incidence of excise duty on cotton fabrics will vary from about 3 per cent to about 25 per cent of the ex-factory price, depending on the price and category of fabrics. A sample study made reveals that even under the revised duty structure, the cumulative incidence of excise duty on different cotton fabrics can not be said to be equitable as can be seen from the following table. These anomalies, which exist not only between different categories of fabrics but also within the same category, are due to the specific rates of duty on cotton yarn.

TABLE

S. No.	Description	Ex-factory price Rs. per sq. metre	Duty in paise per sq. metre			Ad-valorem incidence of yarn & fabric duty expressed as % of ex-factory price	Rate of duty on fabric alone percent ad-valorem
			Fabric Duty	Yarn Duty	Total		
1.	2.	3.	4.	5.	6.	7.	8.
1.	Grey shirting (Med. B)	2.78	5.6	3.7	9.3	3.3	2
2.	Grey long cloth	3.27	6.5	7.1	13.6	4.2	2
3.	Bleached shirting (Med. B)	5.63	17.0	4.7	21.7	3.9	3
4.	Bleached Dyed shirting (Med. A)	8.08	65.0	13.3	78.3	9.8	8
5.	Mercerised Dyed fancy fabrics (Med. B)	9.22	92.0	8.0	100.0	10.1	10
6.	Mercerised dyed printed coating (fine)	10.19	153.0	37.0	190.0	18.6	15
7.	Mercerised dyed coating (fine)	9.93	149.0	37.0	186.0	18.7	15
8.	Grey Dhoties (Superfine)	4.44	66.6	44.1	110.7	24.9	15

1.	2.	3.	4.	5.	6.	7.	8.
9.	Mercerised dyed printed Full Voil (Superfine)	7.39	111.0	59.0	170.0	23.0	15
10.	Mercerised dyed (Rubia (Superfine)	11.59	174.0	67.0	241.0	20.8	15

Source - Ad hoc information collected by the Directorate of Tax Research, Ministry of Finance (Department of Revenue) from the Collectors of Central Excise.

ART SILK INDUSTRY

31.. From ancient times, natural fibres like cotton, wool and silk were being used for clothing, until by the end of the 19th Century, attempts began to be made to produce textile fibres by artificial means. Today there are two distinct groups in the man-made fibres growing in importance - (a) produced from natural cellulose base - known as cellulosic fibres, and (b) produced from synthetic petrochemical base - known as synthetic fibres.

32. In India, the man-made textile production started around 1920. Weaving units solely devoted to man-made fibre were established during the decade 1925 to 1935 when powerloom units manufacturing pure silk fabrics found the cost of yarn prohibitive and, as an alternative, turned their attention to the new fabrics which had the lustre and other properties of silk. The Government's decision to ban imports of Japanese rayon and fabrics to protect the cotton textile industry gave timely impetus to these units. For nearly 25 years, they remained entirely dependent on imports of yarn. The first plant to manufacture viscose rayon yarn in India was commissioned only in 1950. The commencement of production of nylon filament yarn, in the year 1962, provided the next landmark, resulting in a shift in the pattern of fabric production from cellulosics to non-cellulosics. The production of polyester fibre which began in 1965, further helped the growth of this industry, and its indigenous content began to rise with the production of basic raw materials such as DMT and Caprelactum.

33. Today, in India, the man-made textile industry consists of the fibre and spinning sector, and the weaving sector. The fibre and spinning sector consists of (i) units manufacturing cellulosic fibres and yarns i.e., viscose/polynosic fibre, viscose/acetate filament yarn and viscose spun yarn; (ii) units manufacturing non-cellulosic fibres and yarns, i.e., polyester fibre, nylon filament yarn and polyester filament yarn. Approximately 70 per cent of the production consists of cellulosic fibres and yarns and the rest, non-cellulosic fibres and yarns. (yarns are of two types - (a) continuous filament yarn, and (b) yarn spun from staple fibres). The weaving section consists of 1,36,000 powerlooms and 700 knitting machines. Eighty per cent of the looms are of units with 10 looms and below and are in the

decentralised sector. The total number of looms in the organised sector with 50 looms and above would be approximately 18,000. Statement 11 shows the particulars of production of cellulosic and non-cellulosic man-made fibres and filament yarns. Statement 12 shows yarn spun wholly or partly of man-made fibres.

34. In addition to domestic production, man-made fibres and yarn are also imported. In order to increase the production of man-made/blended fabrics and make them available at cheaper prices to the consumers, the imports of viscose/polynosic/polyester fibres have been placed on a free licensing basis. Statement 13 shows the extent of import of various man-made fibres and yarns.

DUTY STRUCTURE - MAN-MADE FIBRES AND YARN

35. Man-made fibres and yarn were brought within the excise net from 1.12.1956. Since then, there have been several changes in the rates of duty applicable to these fibres and yarn. The changes made have been shown in Statements 14 and 15. Important changes are discussed below.

36. In 1961, duty on fibres and filament yarn of cellulosic origin was increased by about 2/3rd as the rayon industry was in a "buoyant condition" and was earning "substantial profits". The Finance Act, 1962, brought about a marked change in the tariff by which man-made fibres and yarn made out of man-made fibres were included in the dutiable category. Simultaneously, rates of duty on fibres and yarn were stepped up partly to make good the loss in revenue due to exemption granted to the unprocessed art silk fabrics.

37. In view of the high margin of profit, the duty was substantially increased in 1967 on all rayon and synthetic fibres and yarn, except on filament yarn normally used in the manufacture of tyre cords, fishing nets and for other industrial purposes. It was expected that the producers would absorb the increase in the excise duties on rayon and synthetic fibres without any increase in the price charged to consumers. However, subsequently on representations received from the industry that it was not able to absorb the entire increase, the duty was reduced on certain denier groups of rayon and synthetic filament yarn. Simultaneously, in the case of manufacturers whose clearances of staple fibre of cellulosic origin and of rayon and synthetic yarn consisting entirely of cellulosic derivatives or regenerated cellulose or both, taken together, for home consumption during the financial year 1966-67 did not exceed 36.5 lakh kgs. a preferential duty treatment was accorded.

38. In 1969, with the objective of curbing the smuggling of nylon yarn, the duty on the lower deniers was reduced. To compensate for the loss in revenue there was an increase in duty on some of the higher denier yarns. The duty on polyester fibre upto 2 deniers was increased in 1970 without affecting other deniers, in order to raise the duty incidence on the costlier fibre. In 1971 after securing a release from the GATT binding imported staple fibres were subjected to an import duty of 100 per cent in view of the high margin of profit on imports.

39. In 1972, the tariff description of this Item was revised so as to clarify that besides man-made fibres and filament yarn, the item also covers "man-made metallic yarn". The other change made was to restrict the excise levy under this Item only to such spun yarn which contained 90' per cent or more by weight of man-made fibres. Special excise duties levied since 1963 were merged with the basic duty and rounded off. The excise duty on more expensive varieties of artificial

and synthetic fibres and yarn such as polyester fibre and synthetic filament yarn was also raised. As nylon yarn spinners began adjusting the denierage of yarn in a way that enabled them to pay lower duties, taking advantage of denier grouping system on the basis of which duty was levied, the denier groups were re-adjusted in 1973 to prevent this happening.

40. With the rise in prices of rayon and synthetic fibres and yarn, the incidence of duty based on specific rates had gone down. To step up this incidence, specific rates in respect of nylon filament yarn, staple fibre and filament yarn of cellulosic origin (other than acetate) were revised upward when supplementary Budget was presented in July, 1974. In 1975, the burden of excise duty on art silk fabrics was shifted from the fabric stage to the yarn, 'since collection of revenue at yarn stage is administratively easier and provides fewer loopholes'. An additional duty of Rs. 20 per kg. (since then reduced to Rs. 5/- per kg. in 1977) was also imposed on textured yarn.

41. As a result of changes in the tariff description (to further rationalise the tariff description of yarn items) made in 1977, spun yarn in which man-made fibre of cellulosic origin is predominently acrylic fibre is dutiable as woollen yarn, while the duty on yarn having predominently other non-cellulosic fibres, is Rs. 24 per kg. under a separate Tariff Item. In order to give relief to handloom sector, cellulosic spun yarn cleared in straight hanks has been wholly exempted. Similarly, duty on yarn cleared in crossed reeled hanks has been reduced by 30 paise per kg. if supplied to handlooms. With a steep fall in the international price of polyester fibre, import duty on it has been raised from 120 per cent to 160 per cent from 15-6-1977 to provide a regular protection to domestic producers.

42. Present rates of excise and customs duties on man-made fibres and yarn are given in Statement 16.

DUTY STRUCTURE-RAYON OR ARTIFICIAL SILK FABRICS.

43. Rayon or artificial silk fabrics were added to the list of excisable goods on 1-3-1954 with a specific rate of duty of one anna and six pies per yard. Excise on these fabrics was imposed as their use was increasing and they competed to some extent with cotton cloth which was subject to an excise duty. Certain fabrics, though commercially known as rayon or artificial silk fabrics, were excluded from the excise purview, e.g., stape fibre fabrics, handloom fabrics and fabrics produced by a manufacturer having less than 25 powerlooms. The subsequent changes in duty on rayon or artificial silk fabrics have been shown in Statement 17. The more important of these and other changes in the tariff are briefly discussed below.

44. In order to simplify the procedure for collection of revenue from a large number of manufacturers, a special procedure, known as compounded levy procedure was introduced on 27.5.1954, under which, manufacturers of rayon or artificial silk fabrics were given the option to pay a duty determined on the basis of number of looms installed. Subsequently, the duty was related to the number of looms/warp knitting machines employed, number of shifts worked and variety of fabrics manufactured.

45. From 12-12-1957, additional excise duty in lieu of sales tax has been levied on artificial silk fabrics. Effective from 1-3-1960 the tariff was amended to include staple fibre fabrics and to exclude fabrics containing 40 per cent or more by weight of silk. On 24-4-1962, the tariff was enlarged to bring handloom fabrics within the excise ambit. However, with a view to reduce the

administrative burden, all unprocessed rayon or artificial silk fabrics were exempted from excise duty and the revenue foregone was sought to be recovered by increasing the rates of duty on yarn, and by levying duty at half of the then existing rates only on fabrics processed with the aid of power or steam. All powerloom units manufacturing grey fabrics were freed from excise control. The compounded levy procedure was also consequently withdrawn.

46. In 1970, with the object of raising additional resources and to rationalise the rate structure so as to have an equitable incidence of duty on different varieties of rayon or artificial silk fabrics the basis of assessment was changed from specific to ad valorem with four value slabs - a lower duty on low priced fabrics and higher duty on costlier fabrics.

47. In March, 1972 the special excise duty, which has been in force since 1963, was merged with the basic duty and to raise additional revenue for the States the duty on costlier fabrics whose value exceeded Rs. 5 per square metre was stepped up by 5 per cent ad valorem. After considering the representations on account of the sharp increase in duty, Government revised the rates of duty and the four value slabs were replaced by nine value slabs. The lowest duty of 3 per cent was applied to the first value slab of fabrics upto Rs. 3 per square metre and the highest rate of duty of 15 per cent became applicable to the fabrics valued Rs. 10 or more per sq. metre. Simultaneously, the total exemption in favour of fents was also withdrawn. In 1973, duty on fents was increased and duty was also imposed on rags and fabrics processed with the aid of non-power operated machines.

48. From 1-3-1975, to make the collection of revenue administratively easier and to leave fewer loopholes, the burden of the basic excise duty was shifted from the fabric stage to yarn stage. Accordingly, artsilk fabrics valued upto Rs. 15/- per sq. metre were exempted from the basic duty. From 30-4-1975, this exemption from basic duty has been extended to all artsilk fabrics irrespective of the value. The earlier total exemption available to the processed knitted fabrics was also modified to make them liable to appropriate additional excise duty.

49. In the Budget of 1977, tariff description of this Item has been amended. The effect of this change is that only such fabrics in which man-made fibres/yarn are predominant are liable to additional excise duty under this Item (they continue to be exempted from basic duty). However, fabrics in which wool or cotton is 30/40 per cent or more, are excluded from the purview of this Item.

50. The present effective rates of duty on man-made fibre fabrics (rayon or artsilk fabrics) are given in Statement 18.

DUTY INCIDENCE AND IMPACT

51. We have seen that the rates of duty on man-made fibres/yarns are specific and related to count/denier of the yarn. On blended yarn containing more than 1/6th of non-cellulosic fibre (other than acrylic), the duty is Rs. 18/- per kg. This rate of duty is Rs. 24/- if such non-cellulosic fibre in the yarn is predominent. The ad valorem incidence of duty on some popular types of yarn is given in the table below.

TABLE

	Description	Duty (Rs./kg)	Ad-valorem incidence of duty as percentage of ex-factory price.
I.	Cellulosic spun Yarn		
	20s on cones	0.30	2.27
	20s cross reel hanks	0.30	2.25
	30s	0.60	4.00
	40s	1.20	6.00
II.	Viscose Filament Yarn		
	20-12 denier (d)	17.10	36.91,
	75-18 d	11.10	38.18
	120-33 d	6.60	26.28
	1650 d (tyre yarn)	2.50	10.72
III.	Nylon Filament Yarn		
	12-1-0 Semi-dull (SD)	58.80	85.16
	12-50	58.80	80.65
	12-1-0 SD	58.80	99.70
	20 SD	58.80	93.92
	40-10-0	51.80	88.53
	111-24-0 Bright	37.80	79.61
	152 SD	19.60	33.15
	162-32-0 SD	19.60	51.81

	Description	Duty (Rs./kg.)	Ad-valorem incidence of duty as percentage of ex-factory price.
IV.	Polyester Filament Yarn		
	67-24-0 SD	63.00	79.93
	80 SD	63.00	83.98
V.	Blended yarn containing more than 1/6th of non-cellulosic fibre		
	50s Polyester 67 x Cotton 33	24	37.85.
	2/80 S Polyester 67 x Cotton 33	24	27.30
	2/34 S Polyester 67 x Viscose 33	34	30.80
	Polyester 48 x Viscose 16 x Cotton 36	24	48.30
	40s Polyester 48 x Viscose 52	18	35.29
	60s Polyester 48 x Viscose 52	18	29.51

Source - Ad hoc information collected by the Directorate of Tax Research, Ministry of Finance (Department of Revenue) from Collectors of Central Excise.

From the above table, it will be seen that even within the same group of yarn, ad valorem incidence of the specific rates of duty varies considerably and sometimes even in respect of yarn of the same denier. In the case of blended yarn containing more than 1/6th of non-cellulosic fibre (other than (acrylic), duty is either Rs. 18.00 or 24.00 per kg., irrespective of the value of yarn, giving different ad valorem incidence.

52. The cumulative excise levy on spun yarn is seen to be much more if the fibre duty, which is Rs. 1.50 per kg. on cellulosic fibres and Rs. 36 per kg. on polyester fibre, is also reckoned. For example, ad valorem incidence of yarn duty on 20s viscose spun yarn is only 2.25 per cent whereas inclusive of fibre duty, this would be 14 per cent. As against this, the cumulative levy on cotton yarn of the same count is only 1.38 per cent though the duty at yarn stage on both is the same.

53. The table below shows the nominal rates of excise duty and cumulative levy of excise on some selected man-made fibre fabrics:

TABLE

S. No.	Description of goods.	Ex-factory price per linear metre.	Excise duty		Fibre and yarn duty	Cumulative duty : col. 5+6	Cumulative duty expressed %age to the ex-factory price.
			Rate %	Amount Rs.			
1.	2.	3.	4.	5.	6.	7.	8.
1.	100% Polyester dyed shirting 91cm.	29.0	5.5	1.60	6.33	7.93	27.34
2.	-do-	33.0	5.5	1.82	7.44	9.26	28.06
3.	74/26 Polyester-Viscose suiting 137 cm.	60.0	5.5	3.30	14.63	17.93	29.88
4.	67/33 Polyester cotton shirting 91 cm.	15.5	5.5	0.85	5.27	6.12	39.48
5.	49/51 Polyester-acrylic suitings 139 cms.	42.65	5.5	2.35	13.58	15.93	37.35
6.	100% Nylon dyed fabric 114cm	12.54	5.5	0.69	2.70	3.39	27.03
7.	100% Nylon dyed chinon 114 cm.	17.04	5.5	0.94	2.98	3.92	23.00
8.	100% Nylon printed sarees	11.50	5.5	0.63	2.47	3.10	26.96
9.	100% Nylon American Georgette printed.	13.30	5.5	0.73	2.94	3.67	27.59
10.	110% Nylon crimped Georgette printed.	15.16	5.5	0.85	2.34	3.19	21.04
11.	100% Cellulosic filament yarn dyed fabrics	5.75	3.87	0.22	0.53	0.75	13.04
12.	100% Cellulosic spun yarn fabric.	5.35	3.64	0.19	0.29	0.48	8.97

Source : Ad hoc information collected from the Collectors of Central Excises

Note : In the above calculation, only fabrics using indigenous fibre/yarn have been taken into account. In fabrics containing imported fibre/yarn, the cumulative duty will increase corresponding to the import duty.

Though the nominal rate of excise duty on man-made fibre fabrics (col. 7) is very low, the cumulative excise (fabric + fibre + yarn) duty is very high. Further, the cumulative excise duty on fabrics of cellulosic yarn is 13.04 per cent (8.97 per cent in case of spun yarn). As against this the cumulative levy on comparable cotton fabrics is around 4 per cent (vide S. No. 3 of Table under para 30).

54. On an average the impact of duty on polyester fibre and blended yarn spun out of it (67 per cent polyester and 33 per cent cotton or viscose) works out to about 33 per cent of the ex-factory price of the fabrics manufactured. On fabrics of nylon filament yarn this would be nearly 25-30 per cent and about 10 per cent ad valorem on fabrics of cellulosic yarn.

55. The excise duty collections from man-made fibre/yarn and fabrics during the year 1976-77 were about Rs. 296.25 crores on an estimated production of about 1200 million metres, inclusive of blended fabrics. This amount, however, does not include duty collected on blended yarn, but includes the duty collected on man-made fibres used in the manufacture of woollen or cotton fabrics. Taking these two factors as balancing ones, the average incidence of excise duty per metre of man-made fibre textiles works out to Rs. 2.46 per metre. If the average incidence of duty on cellulosic fibre fabrics is separated from Rs. 2.46, the average incidence on synthetic fabrics will be substantially higher. Some Associations have made calculations to show that the average duty on cellulosic fibre fabric is 58 paise per metre and on synthetic fabrics it is Rs. 5.60 per metre. We have not been able to verify these calculations but it is certain that the average incidence on man-made fibre fabrics particularly synthetic fabrics is very high as compared to the average incidence of 23.59 paise per metre on cotton cloth.

WOOLLENS

56. The Indian woollen textile industry consists of two sectors (a) the organised sector which includes : combing ; worsted woollen and shoddy spinning and manufacture of worsted woollen and shoddy goods; machine made carpet manufacturing and readymade garments and knitting yarn, and (b) decentralised sector which is made up of a very large number of small units producing tweeds, blankets, shawls, hosiery, carpets, hand-knitted fabrics from yarns supplied by the organised sector. In addition, there is decentralised dyeing of grey hand-knitting yarn produced by the organised sector of the woollen industry.

57. Statement 19 shows the number of functioning units in the organised sector, installed capacity in the different sectors of the woollen industry and production of woollens in 1974-75, 1975-76 and 1976-77.

58. According to the information available with us, domestic wool is used for the weaving of carpets, certain types of blankets and coarse fabrics, and for meeting the defence requirements. Imported wool is mainly used for making most of the wearable fabrics including handloom fabrics as well as for handspinning and knitting. In the past due to paucity of foreign exchange imports of raw wool were subject to fairly stiff restrictions by value/volume. With effect from 17th February, 1977, the import of raw wool has been placed on free licensing basis.

59. Central excise duty on woollen yarn was imposed on 1-3-1961. This duty was levied as a measure of revenue and also to bring within the excise net hosiery and certain other fabrics which did not bear any duty. The duty on worsted yarn was 15 per cent ad valorem and on other woollen yarn it was only 5 per cent ad valorem.

DUTY STRUCTURE - YARN, TOPS AND WOOL

60. The manufacturers were, however, given an option to pay duty at specific rates based on weight instead of at ad valorem rates. The changes in the rates since then may be seen in Statement 20, the more important of which are discussed below.

61. In 1962, to partly make good the loss in revenue on account of the total exemption granted in favour of unprocessed woollen fabrics, tariff rates as well as the alternative specific rates of duty on woollen yarn were increased by about 50 per cent. Exemption available in favour of shoddy wool yarn was also withdrawn. In 1964, for raising additional resources and to make costlier varieties of worsted yarn to bear higher tax burden, duty on worsted yarn of 48 counts and above was revised upward to 20 per cent ad valorem . Simultaneously, the alternative specific rates of duty were also withdrawn. In 1972, the definition of woollen yarn was amended to include only such yarn as contained 90 per cent or more of wool by weight and the special excise duty levied since 1-3-1963 was merged with the basic excise duty.

62. As the rates of duty on worsted yarn had always been higher than on other types of woollen yarn, there was a tendency on the part of some of the manufacturers to misdeclare worsted yarn of lower counts as woollen yarn to claim its assessment at the lower rate of duty. To reduce such evasion it was decided to transfer a part of the duty from worsted yarn to wool tops which were made excisable for the first time in 1969. In the subsequent years, whenever duty on worsted yarn was to be raised, a part of the increase was transferred to wool tops. From 30th August, 1976, the duty on wool top was raised to Rs. 10 per kg.

63. In the Budget of 1977, the tariff description of woollen yarn has been revised. Now, yarn in which wool and/or acrylic fibre predominates is taxable as woollen yarn. But the woollen yarn (including acrylic spun yarn) has been wholly exempted provided the non-cellulosic fibre (other than acrylic fibre) content in it by weight is not more than 1/6th. If it exceeds this limit, duty is leviable at the rate of Rs. 18/- per kg. Woollen yarn has been exempted from excise duty on the ground that excise duty on yarn, which is manufactured in small sector, had led to evasion and other malpractices. The loss in revenue has been made good by an increase in the customs duty at the stage of import of raw wool, waste wool and rags. Simultaneously, with the same objective, duty on wool tops was also reduced to Rs. 5 per kg. and the loss in revenue being made good by the increase in the import duty on raw wool. It has been stated that both these measures should result in making fabrics using indigenous wool cheaper. The present import duty on raw wool is 75 per cent ad valorem as against the pre-Budget rate of 45 per cent ad valorem.

64. "Woollen fabrics", were subjected to excise duty in 1955. In the Finance Bill, the rate of duty proposed was 10 per cent ad valorem which was reduced to 6¼% per cent during the passage of the Bill. Production of fabrics by factories with less than 5 looms and coarse blankets not exceeding Rs. 10 in value (value was enhanced to Rs. 12/- in 1961 when duty was levied on woollen yarn) were exempted. The changes made since the inception of levy on

DUTY STRUCTURE - WOOLLEN FABRICS

woollen fabrics are given in Statement 21. In June, 1956, the exemption based on number of looms was extended to equivalent number of looms of bigger manufacturers also.

65. While the production of composite mills continued to be assessed on ad valorem basis, an optional compounded levy scheme was evolved in 1961 for woollen fabrics manufactured on powerlooms which provided for total exemption in respect of factories having only one loom and a differential lower duty on factories having more than one but not more than five looms.

66. In 1962, tariff description was amended to bring handloom fabrics within the excise net but with a view to release a large number of powerlooms from excise control, all unprocessed (grey) woollen fabrics were wholly exempted. Loss in revenue was made good partly by an increase in duty on yarn and partly by a duty on processed fabrics. Fabrics processed by independent processors became chargeable at 3-1/3 per cent ad valorem if such fabrics were produced on powerlooms or handlooms and 5 per cent ad valorem if in composite mills. Processed handloom fabrics made out of hand spun yarn were exempted. Special excise duty imposed in 1963 at 20 per cent of the effective basic excise duty was merged with basic duty in 1972.

67. In 1977, the tariff description of woollen fabrics has been revised to include fabrics in which wool content is predominant or fabrics having wool 30 per cent (as against the previous limit of 40 per cent) or more of wool and 50 per cent or more of non-cellulosic fibre/yarn. Under the Additional Duties of Excise (Goods of Special Importance) Act, 1957 woollen fabrics are also subject to additional excise duty, which is in lieu of sales tax.

68. Handloom cess at 9 paise per square metre, which was originally 3 pies per square yard, is payable on woollen fabrics under the Khadi and other Handloom Industries Development (Additional Excise Duty on Cloth) Act, 1953.

69. The present effective rates of duty applicable to woollen fabrics are given in column (13) of Statement 21 (Part II).

70. Statement 22 shows the excise revenue collected from woollen yarn, woollen fabrics and wool tops during the last five years.

71. The following table indicates the cumulative burden of customs and excise duties on some woollen fabrics and hand knitting yarn. The estimate of total cumulative tax burden will go up if the sales tax on woollen yarn is also added.

TABLE

Sl. No.	Description of goods	Input duties/taxes as percentage of ex-factory price			Nominal excise duty on finished products. Percent ad-valorem	Total cumulative duty as %age of ex-factory price.
		Customs	Excise or countervailing	Total		
1.	2.	3.	4.	5.	6.	7.
1.	All wool worsted suiting	23.85	1.40	25.25	11	36.25

1.	2.	3.	4.	5.	6.	7.
2.	80/20, wool/polyester suiting	16.26	9.55	25.81	11	36.81
3.	45/55 wool/polyester suiting	7.52	10.44	17.96	11	28.96
4.	Pure merino wool worsted Fancy suiting	14.79	0.03	14.82	11	25.82
5.	Pure merino wool worsted Gaberdine	18.65	0.40	19.05	11	30.05
6.	Terewool suiting plain	11.20	11.12	22.32	11	33.32
7.	Hand knitting yarn	28.07	3.89	31.96	Nil	41.43

STATEMENT 1

TREND OF PRODUCTION OF DIFFERENT YARN - NATURAL AND MAN-MADE SINCE 1970

(In million Kgs.)

Year	Cotton	Man-Made	Wool	Silk	Total
1970	965	117	19	2	1103
1971	881	117	24	3	1025
1972	972	131	22	3	1128
1973	998	125	38	3	1159
1974	1007	135	39	3	1184
1975	989	131	39	3	1162

Source - 1. Handbook of Statistics on Cotton Textile Industry (10th edition) published by the Indian Cotton Mills' Federation (ICMF), Bombay.

2. Economic Times, New Delhi (13th October, 1977)

STATEMENT - 2

PRODUCTION OF WOVEN FABRICS OF COTTON, MAN-MADE FIBRE/YARN AND BLENDS THEREOF IN THE MILL AND DECENTRALISED SECTORS

(In million metres)

Year	100% Cotton cloth			100% Man-made yarn (spun/filament) Fabrics (viscose & non-viscose)			Mill made Blended/Mixed Fabrics						Blended/ Mixed Fabrics by decentralised sector	Total production of cloth
	Mills	Decentralised sector	Total	Mills	Decentralised sector	Total	Polyester/ cotton	Polyester viscose	Polyester/ other fibres except cotton and viscose	Cotton/ viscose	Cotton other fibres except poly. & viscose	TOTAL		
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
1972	4245	3777	8022	1	918	919	60	7	1	21	9	98	101	9140
1972	4169	3602	7771	1	836	887	73	6	1	32	17	129	121	8908
1974	4316	3968	8284	Neg	849	849	63	5	3	32	21	124	87	9344
1975	4032	4002	8034	1	845	846	118	11	6	83	16	234	133	9247
1976	3881	4064	7945	1	900*	901*	142	24	13	156	9	344	253	9443*

*Provisionally estimated.

Source -- Handbook of Statistics on Cotton Textile Industry (10th edition) ICMF, Bombay.

STATEMENTS - 3

EXCISE REVENUE FROM DIFFERENT TEXTILE ITEMS

S.No.	Tariff Item No.	Description of goods	Revenue Estimated (1977-78) (Rs. lakhs)
1	18	Man made fibre & filament yarn etc.	30,767
2.	18A	Cotton yarn, all sorts	4,723
3.	18B	Woollen & acrylic, spun yarn	171
4.	18C	Silk yarn	-
5.	18D	Jute Twist Yarn thread rope & twine, all sorts	315
6.	18E	Non-Cellulosic spun yarn	7,385
7.	19	Cotton Fabrics	16,093
8.	20	Silk Fabrics	-
9.	21	Woollen Fabrics	1,250
10.	22	Man made fabrics	5,720
11.	22A	Jute Manufacture	4,550
12.	22AA	Textile Fabrics NES	2
13.	22B	Textile Fabric Impregnated	10
14.	22D	Ready made garments	
15.	22F	Mineral Fibres & Yarn	360
16.	43	Wool Tops	668
		Total	72,014

i.e. 16 per cent of the net estimated excise revenue in 1977-78

Source - Directorate of Statistics and Intelligence, Central Excise & Customs, New Delhi.

STATEMENT 4

ESTIMATED CUSTOMS REVENUE FROM TEXTILE ITEMS DURING 1977-78

S. No.	Description	Estimated Revenue Rs. crores
1.	Yarn of man-made fibres	13.06
2.	Man-made fibres & filament tow	30.00
3.	Wool, raw and wool tops	26.37
4.	Cotton, raw	0.40
5.	Raw silk and silk manufacture	0.65
	Total	69.83

i.e. about 5% of total import duties (net)

Note: With liberalisation of import policy and increase in import duty on polyester fibre, revenue collections from textile items are likely to exceed the above estimate.

Source: Directorate of Statistics & Intelligence, Central Excise & Customs, New Delhi.

STATEMENT 5

CAPACITY IN THE VARIOUS SECTORS OF THE COTTON TEXTILE INDUSTRY

As on 31.3.1977

No. of Spinning Mills	412
No. of Composite Mills	290
No. of Spindles installed	19.75 million
No. of looms installed	2.08 lakhs.
No. of Handlooms (Cotton)	3.5 million.
No. of Powerlooms (Cotton)	2.11 lakhs.
No. of registered independent power processors.	265 (approx)

Source: 1. Report (1976-77) of Ministry of Commerce, Government of India.

2. Directorate of Statistics and Intelligence, Central Excise & Customs, New Delhi.

STATEMENT 6

PRODUCTION, CONSUMPTION AND DELIVERIES OF COTTON YARN
(in million kg.)

Year	Spindle point Production.	Consumed in mills for weaving cloth.	Free yarn availability (2 minus 3)	Consumed in mills for other manufactures* (included in col. 4)	Deliveries For Exports.	civil consumption
1	2	3	4	5	6	7
1972	972	524	448	16	19	416
1973	998	540	458	18	13	405
1974	1007	537	470	19	11	438
1975	989	513	476	16	3	438
1976	1006	523	483	18	15	449

*Such as hosiery, sewing thread and tyre cord.

Source Handbook of Statistics on cotton textile industry (10 edition), ICMF, Bombay

STATEMENT 7

PRODUCTION OF COTTON CLOTH BY MILLS CATEGORY-WISE

(In million metres)

Calendar year.	Coarse	Lower medium	Higher medium	Fine	Superfine	Total
1972	590	1192	1917	205	341	4245
	(13.9)	(28.1)	(45.2)	(4.8)	(8.0)	(100.0)
1973	605	1279	1559	368	358	4169
	(14.5)	(30.7)	(37.4)	(8.8)	(8.6)	(100.0)
1974	554	1272	1957	277	256	4316
	(12.8)	(29.5)	(45.4)	(6.4)	(5.9)	(100.0)
1975	558	1125	1829	252	268	4032
	(13.8)	(27.9)	(45.4)	(6.2)	(6.7)	(100.0)
1976	553	1130	1788	164	246	3881
	(14.2)	(29.1)	(46.1)	(4.2)	(6.4)	(100.0)

Figures in brackets indicate percentages to total.

Source — Handbook of Statistics on Cotton Textile Industry (10 edition), CIMF, Bombay.

STATEMENT - 8

COTTON YARN CHANGES IN THE RATES OF COMPOUNDED DUTY IN RESPECT OF YARN CONTAINED IN FABRICS PRODUCED BY COMPOSITE MILLS WORKING UNDER SPECIAL PROCEDURE.

Rates of compounded duty

Category	1961-62	1962-63	1963-64	1964-66	1966-67	1967-68	1968-69	1969-70	1974-75	1975-76	1976-77	1977-78
					(In paise per square metre)							
I-Sound Fabrics												
Superfine	1.20	2.00	2.67	8.40	12.00	22.00	22.00	20.00	30.00	40.00	40.00	*
Fine	1.20	2.00	2.67	7.20	9.00	15.00	14.00	12.00	20.00	27.00	30.00	*
Medium-A	1.20	1.80	2.16	5.50	6.60	6.60	6.60	6.60	10.00	10.00	13.00	*
Medium-B	1.20	1.80	2.16	4.40	4.40	4.40	4.40	4.40	4.40	4.40	4.40	*
Coarse	1.20	1.20	1.44	2.20	2.20	2.20	2.20	2.20	2.20	2.20	2.20	*
Fabrics of 191(1)	-	-	-	-	-	-	-	-	5.00	5.00	5.00	*
II-Fents of					(Paise per kilogram of fabrics)							
Superfine	15.0	27.0	36.0	80.0	120.00	120.0	120.0	200.0	400.0	540.0	620.0	*
Fine	15.0	18.0	26.0	60.0	90.0	90.0	90.0	80.0	140.0	190.0	405.0	*
Medium-A	10.0	13.5	16.2	33.0	44.0	44.0	44.0	45.0	70.0	70.0	110.0	*
Medium-B	10.0	13.5	16.2	33.0	44.0	44.0	44.0	30.0	30.0	30.0	30.0	*
Coarse	10.0	10.0	12.0	16.5	16.5	16.5	16.5	15.0	15.0	15.0	15.0	*
Fabrics of 191(1)	-	-	-	-	-	-	-	-	30.0	30.0	30.0	*

* w.e.f. 18.6.77 composite mills were exempted from cotton yarn duty. However, from 15.7.77 they have to pay duty on cotton yarn consumed by them at the rates applicable to such yarn used by the decentralised sector (of statement 9)

STATEMENT - 9

Tariff Item 18A
Year of levy - 1961

Cotton yarn- changes in the standard effective rates of duty for yarn used by other than composite mills

Count (N.E.S.)	Group	Changes with effect from																
		1-3-1961	24-4-1962	1-3-1964	17-4-1964	1-3-1966	30-4-1966	26-5-1967	24-7-1967	1-3-1968	1-3-1969	29-4-1969	1-5-1970	1-3-1974	1-8-1974	1-3-1975	16-3-1976	18-6-1977
		2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18
	Yarn																	
80 (98.2)	-	15	17	50	50	90	90	90 (108)	90 (108)	90 (108)	90	90	90	90	90	90	-	
69 (81.1)	84	15	17	50	50	90	90	90 (108)	90 (108)	90 (108)	90	90	90	90	90	90	-	
59 (60.2)	69	15	17	50	50	90	90	90 (108)	90 (108)	90 (108)	65	65	65	65	65	65	-	
40 (47.2)	51	15	17	25	25	65	65	65 (78)	65 (78)	65 (78)	40	40	-	-	-	-	-	
34 (40.2)	40	15	8	10	10	40	40	40 (48)	40 (48)	40 (48)	-	-	-	-	-	-	-	
29 (34.2)	34	-	8	10	5	25	5	5 (6)	5 (6)	-	-	-	-	-	-	-	-	
22 (26.0)	29	-	3.5	5	-	5	-	-	-	-	-	-	-	-	-	-	-	
14 (16.5)	22	-	3.5	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
6 (7.1)	14	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
-	6	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	

Nil (w.e.f 13/6)

(w.e.f. 18/3/61)

Contd...

1		2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18
II- Other yarn																		
84 (99.2)	-	15	27	108	108	150	150	110 (620)	110 (520)	110 (350)	150	150	150	250	375	500	500	
69 (81.4)	84	15	27	108	108	150	150	110 (620)	110 (520)	110 (350)	150	150	150	200	340	450	500	*
51 (60.2)	69	15	27	108	108	150	150	110 (620)	110 (520)	110 (350)	125	125	125	175	315	425	400	
40 (47.2)	51	15	27	72	72	120	120	110 (620)	110 (520)	110 (350)	110	110	110	150	285	385	300	
34 (30.0)	40	15	18	54	54	90	90	70 (240)	70 (240)	70 (145)	80	80	80	100	125	170	200	
29 (34.2)	34	15	18	54	48	72	72	70 (240)	70 (240)	70 (145)	70	70	70	90	110	150	100	*
22 (26.0)	29	10	13.5	38.5	33	44	44	40 (44)	40 (44)	40 (44)	40	32	32	40	60	60	60	
14 (16.5)	22	10	13.5	27.5	27.5	27.5	27.5	25 (28)	25 (28)	25 (28)	25	20	20	20	20	20	20	
6 (7.1)	14	10	10	16.5	16.5	16	16.5	13 (15)	13 (15)	13 (15)	13	10	10	10	10	10	10	
-	6	10	10	11	11	11	11	13 (15)	13 (15)	13 (15)	13	10	10	10	10	10	10	

* see note 3 below

Note:— (1) Hank yarn presently means single yarn and multiple fold yarn in plain (straight) real hanks.

(2) Figures in brackets under columns 8, 9 and 10 respectively show the duty payable on sized yarn.

Contd...

(3) w. e. f. 10.6.77 tariff description of cotton yarn has been amended to include all yarn in which cotton predominates. The present effective rates of duty on cotton yarn are as under

(a) Yarn containing more than 1/6th by weight of non-cellulosic fibre Rs. 18.00 per kilogram

(b) Other —

(i)	of counts not exceeding 25s	1.5 paise per count
(ii)	of counts exceeding 25s but not exceeding 35s	40 paise plus four paise per count exceeding 25s
(iii)	of counts exceeding 35s but not exceeding 45s	80 paise, plus eight paise per count exceeding 35s
(iv)	of counts exceeding 45s but not exceeding 55s	Rs. 1.60 plus 14 paise per count exceeding 45s
(v)	of counts exceeding 55s	5.5 paise per count.

Per Kg.

Duty is reduced by 30 paise per Kg. on single or multiple fold yarn of (b) type, if cleared in cross real hanks for handlooms.

(4) Figures in brackets under column. (1) indicate the corresponding British count of the yarn.

STATEMENT - 10

COTTON FABRICS - CHANGES IN RATES OF DUTY

YEAR OF LEVY - 1949
TARIFF ITEM No. 19

S. No.	Description	Rates of duty in Advalorem			Paise per square metre								Advalorem	
		1.1 49	1.3 49	1.2 50	26.6 65	1.3. 66	26.5 67	1.3 68	2.5 68	1.3 69	29.5 71	1.3 74	16.3 76	18.6 77
1	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
I-	SUPERFINE													
	(i) Grey-unprocessed	25%	25%	20%	22.00 / 15.5	NC	12.00 / 15.5	7.00 / 15.5	NC	NC	7.00 / 25.00	NC		
	(ii) Grey - Printed	25%	25%	20%	22.00 / 15.5	NC	12.00 / 15.5	7.00 / 15.5	NC	12.00 / 15.5	12.00 / 25.00	NC		
	(iii) Bleached or/and dyed but not printed	25%	25%	20%	32.00 / 15.5	NC	22.00 / 15.5	NC	NC	NC	22.00 / 25.00	NC		
	(iv) Bleached or/and dyed and printed	25%	25%	20%	32.00 / 15.5	NC	22.00 / 15.5	NC	NC	27.00 / 15.5	27.00 / 25.00	NC	12.5% / 2.5%	
	(v) Mercerised or/and water proofed (including Rubberised) but not printed	25%	25%	20%	42.00 / 15.5	52.00 / 15.5	42.00 / 15.5	NC	NC	NC	42.00 / 25.00	51.00 / 25.00		
	(vi) -do- and printed	25%	25%	20%	42.00 / 15.5	52.00 / 15.5	42.00 / 15.5	NC	NC	47.00 / 15.5	47.00 / 25.00	56.00 / 25.00		
	(vii) Processed in any other manner including shrink proofed or organdie processed but not printed	25%	25%	20%	52.00 / 15.5	67.00 / 15.5	57.00 / 15.5	NC	NC	NC	57.00 / 25.00	74.00 / 25.00		
	(viii) -do- and printed	25%	25%	20%	52.00 / 15.5	67.00 / 15.5	57.00 / 15.5	NC	NC	62.00 / 15.5	62.00 / 25.00	79.00 / 25.00		

Contd...

1	2	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
2.	FINE													
	(i) Grey unprocessed	-	6¼%	5%	16.00 / 9.6	NC	10.00 / 9.6	6.00 / 9.6	NC	NC	6.00 / 15.00	NC		
	(ii) Grey - printed	-	6¼%	5%	16.00 / 9.6	NC	10.00 / 9.6	6.00 / 9.6	NC	11.00 / 9.6	11.00 / 15.00	NC	12.5% / 2.5%	*
	(iii) Bleached or/and dyed but not printed	-	6¼%	5%	26.00 / 9.6	NC	20.00 / 9.6	21.00 / 9.6	NC	NC	21.00 / 15.00	NC		
	(iv) Bleached or/and dyed and printed	-	6¼%	5%	26.00 / 9.6	NC	20.00 / 9.6	21.00 / 9.6	NC	26.00 / 9.6	26.00 / 15.00	NC		
	(v) Mercerized or/and water proofed (including Rubberised) but not printed	-	6¼%	5%	36.00 / 9.6	46.00 / 9.6	40.00 / 9.6	41.00 / 9.6	NC	NC	41.00 / 15.00	60.00 / 15.00		
	(vi) -do- and printed	-	6¼%	5%	36.00 / 9.6	46.00 / 9.6	40.00 / 9.6	41.00 / 9.6	NC	46.00 / 9.6	46.00 / 15.00	55.00 / 15.00		
	(vii) Processed in any other manner including shrink proofed and or/organdie processed but not printed	-	6¼%	5%	46.00 / 9.6	61.00 / 9.6	55.00 / 9.6	56.00 / 9.6	NC	NC	56.00 / 15.00	73.00 / 15.00		
	(viii) -do- and printed	-	6¼%	5%	46.00 / 9.6	61.00 / 9.6	55.00 / 9.6	56.00 / 9.6	NC	61.00 / 9.6	61.00 / 15.00	76.00 / 15.00		
3.	MEDIUM - A													
	(i) Grey - (unprocessed)	-	3 pies per yd.	NC	5.00 / 4.8	NC	NC	NC	2.5 / 4.8	nil / 4.8	Nil / 6.00	NC	2.0% / 2.0%	*
	(ii) Grey - printed	-	-do-	NC	5.00 / 4.8	NC	NC	NC	2.5 / 4.8	NC	2.5 / 6.00	NC		
	(iii) Bleached or/and dyed but not printed	-	-do-	NC	15.00 / 4.8	NC	NC	NC	10.00 / 4.8	2.5 / 4.8	2.5 / 6.00	NC		

Contd...

1	2	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
(iv)	Bleached or/and dyed and printed	-	-do-	NC	15.00 4.8	NC	NC	NC	10.00 4.8	5.00 4.8	5.00 6.00	NC		
(v)	Mercerised or/and water proofed (including Rubbered) but not printed	-	-do-	NC	25.00 4.8	35.00 4.8	NC	NC	27.5 4.8	20.00 4.8	20.00 6.00	25.00 6.00	2.0% 2.0%	*
(vi)	-do- and printed	-	-do-	NC	25.00 4.8	35.00 4.8	NC	NC	27.5 4.8	22.5 4.8	22.5 6.00	27.5 6.00		
(vii)	Processed in any other manner including shrink proofed and or/organdie processed but not printed	-	-do-	NC	35.00 4.8	50.00 4.8	NC	NC	42.5 4.8	35.00 4.8	35.00 6.00	47.00 6.00		
(viii)	-do- and printed	-	-do-	NC	35.00 4.8	50.00 4.8	NC	NC	42.5 4.8	37.5 4.8	37.5 6.00	49.50 6.00		
4.	MEDIUM - B													
(i)	Grey (unprocessed)	-	3 Pie per Yd.	NC	3.00 4.8	NC	NC	NC	1.5 4.8	nil 4.8	nil 6.00	NC		
(ii)	Grey - printed	-	-do-	NC	3.00 4.8	NC	NC	NC	1.5 4.8	2.5 4.8	2.5 6.00	NC		
(iii)	Bleached or/and dyed but not printed	-	-do-	NC	8.00 4.8	NC	NC	NC	6.5 4.8	- 4.8	- 6.00	NC		
(iv)	Bleached or/and dyed and printed	-	-do-	NC	8.00 4.8	NC	NC	NC	6.5 4.8	2.5 4.8	2.5 6.00	NC	1.0% 1.0%	*
(v)	Mercerised or/and water proofed (including rubberised) but not printed	-	-do-	NC	13.00 4.8	18.00 4.8	NC	NC	16.5 4.8	10.00 4.8	10.00 6.00	NC		
(vi)	-do- and printed	-	-do-	NC	13.00 4.8	18.00 4.8	NC	NC	16.5 4.8	12.5 4.8	12.5 6.00	NC		

Contd..

1	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
	(vii) Processed in any other manner including shrink proofed and or/organdie processed but not printed	-	-do-	NC	23.00 4.8	33.00 4.8	NC	NC	31.5 4.8	25.00 4.8	25.00 6.00	NC	1.0% 1.0% *	
	(viii) -do- and printed	-	-do-	NC	23.00 4.8	33.00 4.8	NC	NC	31.5 4.8	27.5 4.8	27.5 6.00	NC		
5.	COARSE													
	(i) Grey (unprocessed)	-	3 Pie per Yd.	NC	1.00 3.6	NC	NC	NC	NC	nil 3.6	nil 3.6	NC		
	(ii) Grey - Printed	-	-do-	NC	1.00 3.6	NC	NC	NC	NC	2.5 3.6	NC	NC		
	(iii) Bleached or/and dyed but not printed	-	-do-	NC	6.00 3.6	NC	NC	NC	NC	nil 3.6	NC	NC		
	(iv) Bleached or/and dyed and printed	-	-do-	NC	6.00 3.6	NC	NC	NC	NC	2.5 3.6	NC	NC	0.5% 0.5% *	
	(v) Mercerised or/and water proofed (including Rubberised) but not printed.	-	-do-	NC	11.00 3.6	16.00 3.6	NC	NC	NC	10.00 3.6	NC	NC		
	(vi) -do- and printed	-	-do-	NC	11.00 3.6	16.00 3.6	NC	NC	NC	12.5 3.6	NC	NC		
	(vii) Processed in any other manner including shrink proofed and/or organdie processed but not printed	-	-do-	NC	21.00 3.6	31.00 3.6	NC	NC	NC	25.00 4.8	NC	NC		
	(viii) -do- and printed	-	-do-	NC	21.00 3.6	31.00 3.6	NC	NC	NC	27.5 3.6	NC	NC		

Contd...

1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12	13.	14.	15.
6.	OTHERS													
	(i) Grey (unprocessed)	-	3 Pie per Yd.	NC										
	(ii) Grey - Printed	-	-do-	NC										
	(iii) Bleached or/and dyed but not printed	-	-do-	NC					As at S. No. 1	As at S. No. 1		As at S. No. 1		
	(iv) -do- and printed	-	-do-	NC										
	(v) Mercerised or/and water proofed (including rubberised) but not printed	-	-do-	NC										
	(vi) -do- and printed	-	-do-	NC										
	(vii) Processed in any other manner including shrink proofed and/or organdie processed but not printed	-	-do-	NC									12.5% / 2.5%	*
	(viii) -do- and printed	-	-do-	NC										

* For the rates of duty introduced w.e.f. 18.6.67 and as modified subsequently, see note 16 below.

NOTES

1. During the period 1.2.1950 and 25.6.1965, rates of duty on cotton fabrics were changed several times, but with a view not to unduly burden the statement these have not been included.

2. With effect from 15.2.1953, handloom cess @ 3 pies per yd was levied. The present rate is 1.9 paise per sq. m. This is in addition to basic and additional excise duties.

3. Duty of additional excise (in lieu of sales tax) has been levied from 14.12.1957. The changes made therein from time to time have been shown in cols. (6) to col. (14). Figures shown as denominator indicates additional excise duty (numerator shows the basic duty).

Contd..

4. From 1.3.1956, a lower duty was payable on coarse Dhoties and sarees. From 19.3.1958, lower rate was also prescribed for Medium Dhoties and sarees. These concessions were withdrawn from 4.7.1958.

5. From 17.10.1958, first 50,000 sq.yds (41,800 sq. metres) of cotton fabrics processed in a month by an independent power processor was exempt. This was restricted to those factories which had not produced on or after 1.10.1957 shrink proofed or organdie processed fabrics. From 24.4.1962, the concession was reduced to the first 20,000 sq.m. and was applicable only to bleaching, dyeing and printing processes. This was finally withdrawn from 1.3.1968.

6. From 28.2.1965, duty on certain specified controlled cloth was payable @ 50% of the normal duty leviable on both grey and processed sorts. From 1.3.1968, controlled grey fabrics were completely exempted; on processed fabrics duty was restricted to 50% of the difference of duty on grey and processed fabrics or of the difference between processing and further processing duty. With effect from 2.5.1968, no basic duty was leviable on controlled cloth. Now, from 15.7.1977, duty payable is 50% of the normal duty.

7. With the introduction of processing duty, duty on cotton fabrics manufactured on handloom and powerloom (special procedure) and processed by an independent power processor was reduced to 4/5ths of the appropriate duty w.e.f. 24.4.1962. From 1.3.1968 separate rates were prescribed for such fabrics depending on whether the processing was done by an independent processor or composite mills. Duty on grey superfine and fine handloom fabrics when processed by a composite mill was less by 5 paise vis-a-vis other superfine and fine cloth processed by them. Handloom fabrics processed by an independent processor were to pay duty at about 80% of the duty leviable if such fabrics were processed by a composite mill. Duty on powerloom fabrics processed by independent processor was 90% of the duty payable on such fabrics processed by a composite mill. From 2.5.1968 duty on grey Medium B and coarse processed by independent processors was further reduced. This position continued till 28.2.1969 when the difference between the duty payable by the independent processor on the one hand and composite mills on the other was reduced

8. From 26.3.1949, fabrics produced by powerloom units were completely exempted. This exemption was withdrawn w.e.f. 1.3.1955. However, from 18.5.1955, an alternate compounded levy procedure - duty liability determined on the basis of the number of looms per shift per month - was introduced. This procedure was subsequently restricted to units having not more than 100 powerlooms (w.e.f. 1.3.1958). Again from 1.4.1958 this special procedure was extended to cover units having not more than 300 powerlooms - only to be restricted to units having not more than 49 powerlooms units (from 24.4.1962). In respect of units which did not opt for the special procedure or were not eligible for it, the rates prescribed for similar kinds of fabrics produced by composite mill were applicable during the period 1.5.1955, to 23.4.1962. From 24.4.1962, lower rates were prescribed. From 15.7.1977, unprocessed cotton fabrics (a few varieities excepted) manufactured by powerlooms are completely free from basic and additional excise duty. Consequently special procedure in relation to authorised powerlooms stands withdrawn.

9. From 1 3.1969, certain costlier varieties of cotton fabrics such as coating,suiting, gaberdine, furnishing cloth and towels etc. which were earlier classifiable as fine, medium or coarse cloth, hence paying a low duty, were made liable to duty at 15% adv. irrespective of the categories based on the average count of yarn used in their

Contd...

manufacture. This was done by creating a new sub-item 19I(1). Now there is no separate category for these products.

10. From 1.3.1969, two new sub-items 19 II and 19 III were created for (a) embroidery on cotton fabrics and (b) cotton fabrics impregnated or coated with plastic materials. During 1-3-1968 and 28-2-1969, these were liable to duty under separate tariff items.

11. From 29.5.1971, cotton fabrics processed without the aid of power or steam which were wholly exempt, were subject to duty. However, rates of duty were lower than the normal rates Compounded levy procedure for processing duty was also extended. From 18.6.1977, such fabrics have been wholly exempt.

12. From 1.3.1973, cotton fabrics containing 30% or more of non-cellulosic fabric /yarn were subjected to duty at 15% adv. by creating a new sub-item 19 I(1A). Now there is no separate category for such fabrics.

13. From 16.3.1976, specific rates of duty applicable to cotton fabrics were replaced by ad valorem rates as shown in col. 14 of the statement. Duty on processed handloom fabrics and on powerloom fabrics processed by independent power processors was relatively lower.

14. Fents and rags of cotton fabrics are liable to basic and additional excise duties from 1960 and 1973 respectively, but are exempted from handloom cess.

15. From 1.8.1974 auxiliary duty of excise at 33⅓% of the basic duty leviable was imposed on all cotton fabrics then subjected to ad valorem duty under Tariff Item 19 I(1A), 19 II & 19 III.

16. From 18.6.1977 duty rate structure in respect of cotton fabrics has been changed to levy excise duty on them on value slab basis instead of category of fabrics dependent on the average count of yarn used in their manufacture. Subsequently, from 15.7.1977 this rate structure has again been modified. Present rates of duty (as on 31.12.77) are as under:

	Description			Rate of duty (Basic + Additional Excise duty) Ad valorem
I	Cotton fabrics in which the average count of yarn is 41s or more			15%
II	Other cotton fabrics whose value rupees per sq. m.			
		exceeds	does not exceed	
	(1)	-	4	2%

Contd...

	exceeds	does not exceed	
(ii)	4	6	3%
(iii)	6	7	4%
(iv)	7	8	6%
(v)	8	9	8%
(vi)	9	10	10%
(vii)	10	11	12%
(viii)	11	12	14%
(ix)	12	-	15%

(a) In the case of handloom fabrics processed by an independent processor approved in this behalf by the Government, the appropriate rate of duty is reduced by 60% subject to maximum reduction of 6% ad valorem except in the case of fabrics having average count of yarn of 41s or more when cleared after processing but without printing. For such fabrics, the rate of duty leviable is 5% ad valorem. Unprocessed handloom fabrics are wholly exempt. When handloom fabrics are processed by a factory owned by a registered handloom cooperative society or any organisation set up or approved by the Government for the purpose of development of handlooms, duty is nil.

(b) In the case of powerloom fabrics or handloom fabrics not covered by (a) above and processed by an independent processor, the appropriate rate of duty is reduced by 30% subject to maximum reduction of 3% ad valorem except in the case of fabrics having average count of yarn of 41s or more when cleared after processing but without printing. For such fabrics, the rate of duty is 8% ad valorem.

(c) In the case of price controlled cloth, namely, Dhoti, Sarees, long cloth, shirting and drill, the appropriate rate of duty is reduced by 50%.

(d) In the case of drill, other than at (c) above, the appropriate rate of duty is reduced by 50%.

(e) In addition to the rates of duty indicated above, handloom cess @ 1.9 paise per sq. metre is also leviable.

(f) There is a separate set of rates of duty for 'fents' and 'rags' arising out of cotton fabrics.

STATEMENT 11

PRODUCTION OF MAN-MADE FIBRES/FILAMENT YARN

(in tonnes)

Description	1972	1973	1974	1975	1976
I. Staple fibre —					
a) Viscose	70337	62627	77346	66829	83374
b) Acetate	359	540	237	317	365
c) Polyester	6604	10527	7933	14336	21061
Total	77300	73694	85516	81482	104800
II. Filament yarn —					
a) Viscose (ex. rayon tyre yarn)	39633	36661	36624	33065	41432
b) Acetate	1541	1631	2009	1888	1825
c) Polyester	548	1856	1273	2490	2418
d) Nylon (ex. nylon tyre yarn)	11545	10918	9124	13378	15453
Total	53267	51066	49030	50821	61128

Source : Handbook of Statistics on Cotton Textile Industry (10th Edition), ICMF, Bombay.

STATEMENT 12

PRODUCTION OF VARIOUS TYPES OF SPUN YARN (OTHER THAN 100% COTTON) MANUFACTURED BY MILLS WORKING ON COTTON-SPINNING SYSTEM

(In million kgs)

Yarn	100% viscose staple	100% non-viscose staple fibre (mainly polyester)	Polyester/ cotton blends	Polyester/ viscose blends	Cotton/ viscose blends	Blends of cotton and other staple fibres except polyester and viscose	Other blends	Total
1	2	3	4	5	6	7	8	9
1972	58	2	10	4	9	3	2	85
1973	56	6	10	5	10	4	2	93
1974	57	3	8	3	9	4	1	85
1975	53	1	11	7	19	2	1	94
1976	63	2	12	15	43	2	4	141

Source: Handbook of Statistics on Cotton Textile Industry (10th Edition), ICMF, Bombay.

STATEMENT 13

IMPORTS OF SYNTHETIC & CELLULOSIC FIBRES & YARNS (APRIL-MARCH)

Synthetic Fibres	1970-71		1971-72		1972-73		1973-74		1974-75		1975-76		1976 (Apr.-Oct.)	
	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs)	Qty. (Kgs.)	Value (Rs)	Qty. (Kgs.)	Value (Rs)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	15)
Polyamide Fibre	117189	1081514	112700	803023	531008	3654536	324781	2422590	151417	2116836	355760	6089479	86790	1254198
Polyester Fibre	3097752	22749502	3026328	18845290	2566219	16513702	636921	4924804	327500	4863681	540657	6688848	272751	3242057
Acrylic Fibre	195272	1618413	107525	745939	260266	1689661	762455	6234174	751832	11587804	3163264	36024701	1771142	22962290
Polypropylene Fibre	-	-	1016	15894	-	-	3000	30476	15220	158163	6630	71204	1278	9819
PVA Fibre	48822	344515	-	-	15000	77986	-	-	-	-	-	-	-	-
Other Fibres	1503212	8848242	1343282	8647964	3228254	17696266	880055	6630540	373069	4339646	575627	6933167	48663	612236
Polyamide Tow	6912	63312	6648	56964	38804	354916	69549	683314	34610	466458	5750	83958	10897	165723
Acrylic Tow	122110	96452	28760	243583	34615	249501	26880	286610	69782	923416	9976	124873	-	-
Polyester Tow	-	-	15345	94387	20935	132351	990	10792	-	-	-	-	-	-
Other Two for Fibre Manufacture	38968	376340	56213	508869	64500	435537	22207	235296	6990	96250	36408	542558	9766	150239
Polypropylene Tops	-	-	-	-	-	-	-	-	2092	15319	-	-	-	-
Total for Synthetic Fibre (I)	5020337	35180590	5199817	29961913	6759601	40804456	2726838	21458596	1732512	24567573	4694074	58558788	2203287	28396562
Cellulosic Fibres														
Viscose Rayon Fibre	-	-	3161471	12601570	926318	4529131	326809	2177389	51938	630987	21590	225110	479200	5147512
Acetate Rayon Fibre	-	-	6162	50361	-	-	-	-	-	-	-	-	-	-
Other Fibres not carded or combed.	1019638	3785271	636779	3305787	532828	2783185	17106	88937	36772	381902	80400	816924	15000	190909
Other Two	8733	31219	8820	36501	144930	786456	192123	1046703	10000	131460	8289	110864	8533	127231
Total for Cellulosic Fibre (II)	1028371	3816490	4035232	15994219	1604076	8098772	536038	3315029	98710	1144349	110279	1152898	502733	5465652
Grand Total for Synthetic & Cellulosic Fibres	6046708	38997080	9235049	45956132	8363677	48903228	3262876	24773625	1831222	25711922	4804353	59711686	2706020	33862214
Polyamide Filament Yarn	1339309	18794969	1938577	27527154	1040023	10912212	689780	11572805	1402300	33565912	1539575	31660419	279749	5396000
Nylon Tyre Yarn (840 deniers)	2095837	22643117	2704879	28893065	2278012	20902159	795716	8751379	1781908	38215497	1313140	27015003	599855	8686016
Nylon Tyre Cord	113322	1323824	33111	382354	31599	475334	495	34565	22735	563045	559	19094	890	29332
Polyester Filament Yarn	158434	1655625	207478	2478088	726765	8400926	954397	9766460	935329	19424218	2159273	27357474	486825	9179701

IMPORTS OF SYNTHETIC & CELLULOSIC FIBRES AND YARNS (APRIL-MARCH)

	1970-71		1971-72		1972-73		1973-74		1974-75		1975-76		1976(April-Oct.)	
	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)	Qty. (Kgs.)	Value (Rs.)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)
Acrylic Filament Yarn	-	-	-	-	-	-	9192	245144	39068	1220643	26985	857084	15041	444458
PVA Filament Yarn	-	-	-	-	-	-	-	-	1586	37353	-	-	-	-
PVC Filament Yarn	-	-	-	-	-	-	-	-	-	-	2987	80404	-	-
Polypropylene Filament Yarn	-	-	-	-	-	-	-	-	-	-	96	3562	-	-
Other synthetic Yarn	64410	632037	4351	48937	92485	1009604	98476	2093075	108262	2366261	185977	4037549	61029	1046509
Total of Synthetic Filament Yarns	3771312	45049572	4889396	57329598	3232864	31879835	238058	32464429	4351190	95393129	5228592	91030589	1443349	24782824
Polyester Spun Yarn	-	-	4980	67943	6904	43477	-	-	137	7862	6420	145637	3328	69832
Acrylic Spun Yarn	-		-	-	15	200	18958	392604	20299	660191	79385	1933946	23810	502853
Polypropyline Spun Yarn	-	-	450	450	-	-	-	-	-	-	-	-	-	-
Other Spun Yarn	8699	163338	9814	89535	2629	47077	48507	1446222	123696	3272672	56136	2011396	13245	376567
Total Spun Yarn	8699	163338	16244	157928	9528	90754	67505	1838826	144132	3940925	141941	4090881	40383	949252
Grand Total of Synthetic Filament & Yarn	3780011	45212910	4904640	57487526	3242412	31969989	2415563	34303254	4495322	99334054	5373533	95121470	1483732	25732076
Viscose Rayon Filament Yarn (Upto 60 deniers)	-	-	-	-	28000	293662	-	-	-	-	3028	126681	-	-
Upto 75 deniers)	-	-	-	-	-	-	-	-	2000	35656	-	-	-	-
Other deniers	-	-	-	-	-	-	-	-	2005	50933	228547	3769930	400000	676676
Acetate Rayon Filament Yarn														
120 deniers	-	-	-	-	-	-	-	-	16266	272511	8690	58409	-	-
150 deniers	-	-	-	-	-	-	12415	109652	-	-	-	-	484	7981
Other Cellulosic Filament Yarns	2246	60746	11834	116028	18105	276970	2531	41200	-	-	1999	53951	218	17069
Total	2246	60746	11834	116028	48105	370632	14946	150852	20271	359100	237264	4009011	400702	701728

Source: Monthly Statistics of Foreign Trade of India Volume II - Imports.
Published by Department of Commercial Intelligence Statistics Calcutta.

STATEMENT 14

CHANGES IN THE RATES OF DUTY ON

RAYON AND SYNTHETIC FIBRES AND YARN (OTHER THAN CONTINUOUS FILAMENT YARN)

Effective ratos of duty Rs. per kg.

Year of levy: 1956

S. No.	Description	CHANGES WITH EFFECT FROM																
		1-12-56	1-3-59	1-10-60	1-3-61	24-4-62	1-3-63	1-3-64	16-10-64	28-2-65	26-5-67	1-3-69	17-3-72	1-3-73	1-3-74	1-8-74	1-3-75	16-3-76	1-1-77
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
1.	Staple fibre and tow																		
(i)	of cellulosic origin	0.27	0.45	NC	0.75	1.00	1.33	1.15	1.15 (0.75) for 1.5d and above	0.60	0.80	1.00	NC	NC	NC	1.50	NC	NC	NC
(ii)	of non-cellulosic origin																		
	(a) acrylic	0.27	0.45	NC	0.75	1.00	1.33	2.67	NC	NC	16.00	6.00	NC	NC	NC	NC	NC	20.00	30.00 (9-5-77)
	(b) polyester upto 2 deniers	0.27	0.45	NC	0.75	1.00	1.33	2.67	NC	NC	16.00	28.00	35.00	36.90	40.00	NC	NC	NC	36.00 (13-4-77)
	above 2 deniers	0.27	0.45	NC	0.75	1.00	1.33	2.67	NC	NC	16.00	28.00	30.00	31.90	40.00	NC	NC	NC	-do-
	(c) Nylon staplefibre	0.27	0.45	NC	0.75	1.00	1.33	2.67	NC	NC	16.00	28.00	30.00	NC	NC	NC	6.00	40.00	NC
	(d) Others	0.27	0.45	NC	0.75	1.00	1.33	2.67	NC	NC	16.00	28.00	30.00	NC	NC	NC	40.00	NC	NC
2.	Yarn spun either wholly out of cellulosic staple fibre or not more then 10% cotton (prior to 17-3-72 - 40%)																		
	of & above NF counts	Below NF counts																	
(1)	84	-	0.27 nil w.e.f. 16-9-57	NC	NC	NC	NC	NC	NC	0.90	0.90	1.00	NC	1.50	NC	2.50	NC	4.00	3.25)
(2)	69	84								0.90	0.90	1.00	NC	1.50	NC	2.00	NC	3.20	2.60) *
(3)	51	69								0.90	0.90	1.00	NC	1.25	NC	1.75	NC	2.80	2.30)
(4)	40	51								0.60	0.60	0.90	NC	1.10	NC	1.50	NC	2.40	1.95)
(5)	34	40								0.45	0.45	0.80	NC	0.80	NC	1.00	NC	1.60	1.30)
(6)	29	34								0.40	0.40	0.60	NC	0.70	NC	0.90	NC	1.45	1.20)
(7)	22	29								0.25	0.25	0.45	NC	0.32	NC	0.40	NC	0.65	0.55)
(8)	14	22								0.15	0.15	0.30	NC	0.20	NC	NC	NC	0.30	0.25)
(9)	-	14								Nil	Nil	NC	NC	0.10	NC	NC	NC	0.15	NC)

Contd...2/-

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
3.	Yarn spun either wholly or partly out of non-cellulosic fibre (other than acrylic)	0.27																	
	If non-cellulosic fibre content is:	nil w.e.f. 16-9-57																	
(i)	50% or more		NC	NC	NC	NC	NC	NC	4.0	NC	14.00	NC	15.00	NC	NC	NC	24.00	NC	
(ii)	less than 50% but not less than 25%		NC	NC	NC	NC	NC	NC	3.0	NC	8.00	NC	12.00	NC	NC	NC	19.20	NC	**
(iii)	less than 25% but not less than 10%								3.0	NC	8.00	NC	10.00	NC	NC	NC	16.00	NC	
(iv)	10% or less								2.0	NC	6.00	NC	7.50	NC	NC	NC	12.00	NC	
4.	yarn spun either wholly out of acrylic fibre or containing not more than 10% of natural fibre																		
I	Manufactured on worsted system	nil w.e.f. 16-9-57	NC	NC	NC	NC	NC	NC											
(a)	Hand knitting											6.00	7.00	NC	NC	NC	11.20		
(b)	Others																		
(i)	of 40 counts and above											12.89	14.00	NC	NC	NC	22.40		
(ii)	of above 20 counts but below 40 "											7.00	8.00	NC	NC	NC	12.80		
(iii)	of 20 counts and below											3.60	4.00	NC	NC	NC	6.40		
II	Manufactured on other system	-do-	NC	NC	NC	NC	NC	NC											
(i)	60 counts & above											@0.80	1.00	8.00	NC	NC	12.60		
(ii)	of above 20 counts but below 60 "											0.80	1.00	5.00	NC	NC	8.00		
(iii)	of 20 counts & below											0.80	1.00	3.00	NC	NC	4.80		

As against serial number 3 above | As against serial number 3 above | As against serial number 3 above | As at serial No.3 except that w.e.f. 9.5.77 duty on yarn containing more than 50% acrylic fibre will be Rs. 10.0 per kg. | Duty rates as applicable to woollen yarn.

@ Effective from 2-9-1968

* Changed rates of duty for spun yarn in which man-made fibre of cellulosic origin predominates, effective from 18.6.77

** From 18-6-77 duty on spun yarn in which non cellulosic fibre (other than acrylic fibre) predominates is Rs. 24 per kg. irrespective of percentage of non-cellulosic fibre content in it or the system on which such yarn has been manufactured.

DESCRIPTION	RATE OF DUTY PER KG.
(i) of counts not exceeding 25s	1.5 paise per count
(ii) of counts exceeding 25 s but not exceeding 35s	40 paise, plus 4 paise per count exceeding 25s.
(iii) of counts exceeding 35s but not exceeding 45s	80 paise plus 8 paise per count exceeding 35s.
(iv) of counts exceeding 45s but not exceeding 55s	Rs.1.60, plus 1½ paise per count exceeding 45s.
(v) of counts exceeding 55s	5.5 paise per count.

(1) Single yarn & multifold yarn in plain (straight) red hanks are wholly exempt.

(2) Duty is reduced by 30 paise per kg. on yarn, single or multiple fold in cross red hanks purchased for handlooms.

STATEMENT 15

CHANGES IN RATES OF DUTY ON

RAYON AND SYNTHETIC - CONTINUOUS FILAMENT YARN

Year of levy - 1956

Effective rate of duty Rs. per kg.

Description	CHANGES WITH EFFECT FROM																	
	1-12-56	1-3-59	1-10-60	1-3-61	2-4-62	1-3-63	1-3-64	28-2-65	1-3-66	26-5-67	24-7-67	1-3-69	17-3-72	1-3-73	1-3-74	1-8-74	1-3-75	16-3-76
	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
Rayon yarn, consisting entirely of cellulosic or re-generated cellulosic or both -																		
Acetate																		
(i) Below 75d	1.10	1.80	1.80	3.00	4.00	5.33	8.00	NC	7.50	10.35 (8.20)	10.35 (8.20)	11.40 (9.80)	NC	10.35	NC	NC	14.50	12.45
(ii) 75d and above but below 100d	0.82	1.35	NC	2.25	3.00	4.00	6.00	NC	6.00	6.70 (6.50)	6.70 (6.50)	7.40 (7.25)	NC	7.80	NC	NC	10.90	9.35
(iii) of 100d	0.82	1.35	NC	2.25	3.00	4.00	6.00	NC	5.00	4.75	NC	5.25	NC	5.80	NC	NC	8.10	6.95
(iv) 101 d and above but below 120d	0.55	0.90	NC	1.50	2.00	2.67	4.00	NC	3.00	4.75	NC	5.25	NC	5.80	NC	NC	8.10	6.95
(v) 120d & above but below 150d	0.55	0.90	NC	1.50	2.00	2.67	4.00	NC	2.50	3.95 (2.75)	3.95 (2.75)	4.35 (3.45)	NC	4.00	NC	NC	5.60	4.80
(vi) 150d & above but below 350d	0.55	0.90	NC	1.50	2.00	2.67	4.00	3.00 (8.12.65)	2.50	3.40 (2.60)	3.40 (2.60)	3.75 (3.15)	NC	3.70	NC	NC	5.20	4.45
(vii) 350d & above but below 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	-do-	2.50	NC	NC	NC	NC	3.05	NC	NC	4.25	3.65
(viii) of 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	-do-	2.50	NC	NC	NC	NC	3.05	NC	NC	4.25	3.65
(ix) above 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	NC	2.00	NC	NC	NC	NC	2.55	NC	NC	NC	NC
b) Others																		
(i) below 75d	1.10	1.80	NC	3.00	4.00	5.33	8.00	NC	8.00	10.35 (8.20)	10.35 (8.20)	11.40 (9.80)	NC	11.40	NC	14.25	19.95	17.10
(ii) 75d & above but below 100d	0.82	1.35	NC	2.25	3.00	4.00	6.00	NC	5.30	6.70 (6.50)	6.70 (6.50)	7.40 (7.25)	NC	7.40	NC	9.25	12.95	11.10
(iii) of 100d	0.82	1.35	NC	2.25	3.00	4.00	6.00	NC	4.75	NC	NC	5.25	NC	NC	NC	6.60	9.25	7.95
(iv) 101d & above but below 120d	0.55	0.90	NC	1.50	2.00	2.67	4.00	NC	4.75	NC	4.75	5.25	NC	NC	NC	6.60	9.25	7.95
(v) 120d & above but below 150d	0.55	0.90	NC	1.50	2.00	2.67	4.00	2.50	2.65	3.95 (2.75)	3.95 (2.75)	4.35 (3.45)	NC	4.35	NC	5.50	7.70	6.60
(vi) 150d & above but below 350d	0.55	0.90	NC	1.50	2.00	2.67	4.00	2.50	NC	3.40 (2.60)	3.40 (2.60)	3.75 (3.15)	NC	3.75	NC	4.70	6.60	5.65
(vii) 350d and above but below 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	2.50	NC	NC	NC	NC	NC	NC	NC	3.15	4.40	3.80
(viii) of 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	2.50	NC	NC	NC	NC	NC	NC	NC	3.15	4.40	3.80
(ix) above 1100d	0.55	0.90	NC	1.50	2.00	2.67	4.00	2.00	NC	NC	NC	NC	NC	NC	NC	2.50	2.50	NC

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
3.	Synthetic Yarn (Fil Yarn)																		
	(a) Viscose Yarn																		
	(i) below 30d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	56.00	38.00	NC	40.00	NC	NC	NC	56.00	NC
	(ii) 30d & above but below 75d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	36.00	33.00	NC	35.00	NC	NC	NC	49.00	NC
	(iii) 75d & above but below 100d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	NC	25.00	NC	NC	NC	35.00	NC
	(iv) 100d & above but below 150d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	NC	NC	NC	28.00	NC
	(v) 150d & above but below 750d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	NC	NC	NC	28.00	NC
	(vi) of 750d	3.31	NC	3.35	NC	4.50	6.00	4.00	NC	NC	16.00	NC	NC	20.00	NC	NC	NC	28.00	NC
	(vii) above 750d	3.31	NC	3.35	NC	4.00 3.00 (3.11.62)	4.00	4.00	NC	NC	NC	NC	NC	5.00	NC	NC	NC	NC	NC
	(b) Polymide (Nylon) Yarn																		
	(i) below 30d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	56.00	38.00	30.00	35.00	33.50	NC	42.00	58.80	NC
	(ii) 30d & above but below 35d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	36.00	33.00	28.00	30.00	38.50	NC	52.00	58.80	NC
	(iii) 35d & above but below 75d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	36.00	30.00	28.00	30.00	33.50	NC	37.00	51.80	NC
	(iv) 75d & above but below 80d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	24.00	25.00	33.50	nC	32.00	44.80	NC
	(v) 80d & above but below 90d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	24.00	25.00	28.50	NC	32.00	44.80	NC
	(vi) 90d & above but below 100d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	NC	20.00	28.50	NC	32.00	44.80	NC
	(vii) of 100d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	16.00	NC	20.00	NC	28.50	NC	32.00	44.80	NC
	(viii) 101d & above but below 110d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	20.00	NC	28.50	NC	32.00	44.80	NC
	(ix) 110d & above but below 150d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	20.00	NC	23.50	NC	27.00	37.80	NC
	(x) 150d & above but below 750d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	8.00	NC	11.50	NC	14.00	19.60	NC
	(xi) of 750d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	8.00	NC	11.50	NC	14.00	19.60	NC
	(xii) above 750 d	3.31	NC	3.35	NC	3.00 (3.11.62)	4.00	4.00	NC	NC	NC	NC	NC	NC	5.85	NC	6.50	NC	NC

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
(c)	Polyester Yarn																		
(i)	below 30d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	56.00	38.00	NC	40.00	41.90	56.00	NC	77.00	NC
(ii)	30d & above but below 75d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	36.00	33.00	NC	35.00	36.96	50.00	NC	70.00	NC
(iii)	75d & above but below 100d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	NC	25.00	26.80	45.00	NC	63.00	NC
(iv)	100d & above but below 150d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	21.90	35.00	NC	49.00	NC
(v)	150d & above but below 750d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	21.90	35.00	NC	49.00	NC
(vi)	of 750d	3.31	NC	3.35	NC	4.50	6.00	4.00	NC	NC	4.00	NC	NC	20.00	21.90	35.00	NC	49.00	NC
(vii)	above 750d	3.31	NC	3.35	NC	4.50 3.00 (3.11.62)	4.00	4.00	NC	NC	NC	NC	NC	5.00	6.90	15.00	NC	NC	NC
(d)	Others																		
(i)	below 30d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	56.00	38.00	NC	40.00	NC	NC	NC	56.00	
(ii)	30d & above but below 75d	3.31	NC	3.35	NC	4.50	6.00	12.00	NC	13.00	36.00	33.00	NC	35.00	NC	NC	NC	49.00	
(iii)	75d & above but below 100d	3.31	NC	3.35	NC	4.50	6.00	10.00	NC	10.67	20.00	NC	NC	25.00	NC	NC	NC	35.00	NC
(iv)	100d & above but below 150d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	NC	NC	NC	28.00 28.00	NC
(v)	150d & above but below 750d	3.31	NC	3.35	NC	4.50	6.00	8.00	NC	8.40	16.00	NC	NC	20.00	NC	NC	NC	28.00	NC
(vi)	of 750d	3.31	NC	3.35	NC	4.50	6.00	4.00	NC	NC	4.00	NC	NC	20.00	NC	NC	NC	28.00	NC
(vii)	above 750d	3.31	NC	3.35	NC	4.50 3.00 (3.11.62)	4.00	4.00	NC	NC	NC	NC	NC	5.00	NC	NC	NC	NC	NC
3.	Polymide yarn for use in the manufacture of fishing nets & parachute cards.	3.31 24 annas per lb.	NC	3.35	NC	4.50 2.25 (3.11.62)	3.00	0.00	NC	NC	NC	NC	NC	4.00	NC	NC	NC	NC	NC
	Textured yarn																		
(a)	made out of duty paid base yarn	Non Excisable																20.00 @ 10.00 (12.5.77)	
(b)	Others																	105.00 @@ 95.00 (12.5.77)	

N C stands for no change

@ 5.00 (18.6.77)

@@ 90.00 (18.6.77)

STATEMENT 16

MAN-MADE FIBRES AND YARN - PRESENT RATES OF EXCISE AND CUSTOMS DUTIES

S.No.	Description	Rate of Excise duty Rs. per Kg.	Customs duties (Basic & Auxiliary)
(1)	(2)	(3)	(4)
1.	Staple fibre and tow —		
	(i) of cellulosic origin	1.50	Nil
	(ii) of non-cellulosic origin —		
	(a) acrylic fibre	30.00	120%
	(b) polyester fibre	36.00	160%
	(c) others	30.00	120%
2.	Rayon and synthetic yarn consisting entirely of cellulosic or regenerated cellulose or both —		
	(a) Acetate		
	(i) below 75 d.	12.45)	
	(ii) 75 d. and above but below 100 d.	9.35)	
	(iii) 100d. " " 120 d.	6.95)	
	(iv) 120d. " " 150 d.	4.80)	
	(v) 150d. " " 350 d.	4.45)	
	(vi) 350d. " but not above 1100 d.	3.65)	
	(vii) above 1100 d.	2.55)	
	(b) Others (such as viscose)	)	Nil
	(i) below 75 d	17.10)	
	(ii) 75 d.and above but below 100 d.	11.10)	
	(iii) 100 d. " " 120 d.	7.95)	
	(iv) 120 d. " " 150 d.	6.60)	
	(v) 150 d. " " 350 d.	5.65)	
	(vi) 350 d. " but not above 1100 d.	3.80)	
	(vii) above 1100 d.	2.50)	

(1)	(2)	(3)	(4)
3.	**Other synthetic yarn**		
	(a) Man-made metallic yarn		
	(i) below 30 d.	56.00	120% **
	(ii) 30 d. and above but below 75 d.	49.00	
	(iii) 75 d. " " 100 d.	35.00	
	(iv) 100 d. " but not above 750 d.	28.00	
	(v) above 750 d.	5.00	
	(b) Polyamide (nylon) yarn		
	(i) below 35 d.	58.80	120%
	(ii) 35 d. and above but below 80 d.	51.80	
	(iii) 80 d. " " 110 d.	44.80	
	(iv) 110 d. " " 150 d.	37.80	
	(v) 150 d. " but not above 750 d.	19.60	
	(vi) above 750 d.	6.50	
	(vii) for use in the manufacture of fishing nets and parachute cords	4.00	
	(c) Polyester yarn		
	(i) below 30 d.	77.00	
	(ii) 30 d. and above but below 75 d.	70.00	
	(iii) 75 d. " " 100 d.	63.00	
	(vi) 100 d. " but not above 750 d.	49.00	
	(v) above 750 d.	15.00	
	(d) High density polyethelene tapes for the manufacture of HDPE fabrics	Nil	
	(e) High density polythelene monofilament yarn of 60 d.	Nil	
	(f) Others		
	(i) below 30 d.	56.00	
	(ii) 30 d. and above but below 75 d.	49.00	
	(iii) 75 d. " " 100 d.	35.00	
	(iv) 100 d. " but not above 750 d.	28.00	
	(v) above 70 d.	5.00	

(1)	(2)		(3)	(4)
4.	Textured yarn			
	(a) Produced out of base yarn		Base yarn duty, if not already yarn + Rs. 5.00 per kg.	
	(b) other textured yarn		90.00	120%
5.	Yarn spun wholly out of staple fibre of cellulosic origin or in which such fibre is predominent —			
	Counts —			
	of and above	less than		
	-	25	1.5 P. per count	
	25	35	40 P. plus 4 paise per count exceeding 25s.	
	35	45	80 P. plus 8 paise per count exceeding 35s	
	45	55	160 P. plus 14 paise per count exceeding 45s.	120% **
	55		5.5 paise per count	
	(Yarn in straight reel hanks is exempt. Duty on cross reel hanks for handlooms is reduced by 30 Paise per kg.)			
6.	Yarn in which acrylic fibre is predominent		Nil	
7.	Yarn in which non-cellulosic fibre (other than acrylic fibre) is predominent		24.0	
8.	Polypropylene spun yarn		Nil	

* Countervailing duty leviable is equal to excise duty on similar indigenous product. This is in

Contd.....

addition to duty shown in col.(4) above. Acrylic continuous filament is however wholly exempt from countervailing duty.

Import duty (excluding countervailing duty) on Nylon tyre yarn is Rs. 120% plus Rs. 11 per kg. and that on acrylic continuous filament at 105% plus Rs. 30 per kg when nylon filament and polyester filament yarn are imported under import replenishment licence scheme, import duty (excluding countervailing duty) is nil.

STATEMENT 17

MAN-MADE FABRICS (RAYON OR ARTIFICIAL SILK FABRICS) CHANGES IN THE STANDARD EFFECTIVE RATES OF DUTY

TARIFF ITEM NO.22
YEAR OF LEVY 1954

S.No.	Period w.e.f.	Category of Fabrics	Rate of duty		
			Basic duty	Additional Excise duty	H.L. Cess
(1)	(2)	(3)	(4)	(5)	(6)
1.	1.8.54	All dutiable rayon or art- silk Fabrics.	One Anna & 6 Pies per yard	-	3 Pies per yard.
2.	27.4.54	"	6 Pies per sq. yard	-	-do-
3.	1.8.55	"	"	-	3 Pies per sq. yard.
4.	14.12.57	"	"	3 Paise per sq. yard.	-do-
5.	1.3.59	"	6 n. Paise per sq. yard	"	-do-
6.	1.10.60	"	7 n. Paise per sq. Metre	3.6 n. Paise per sq. metre	1.9 n. Paise per sq. Metre
7.	24.4.62	1. Unprocessed fabrics.	Nil	Nil	Nil
		2. Processed fabrics.	3.5 P. per sq. m.	3.6 P. per sq. m.	1.9 P. per sq. m.

(1)	(2)	(3)	(4)	(5)	(6)
8.	1.3.70	Processed rayon & artificial silk fabrics falling under sub-item (1) of Tariff item No. 22 —			
		Value per sq. mt.			
		(i) Not exceeding Rs. 2.50	2% adv.	0.6% adv.	1.9 P. per sq. m.
		(ii) Exceeding 2.50 but not exceeding Rs. 3.50	3.5% adv.	1.5% adv.	"
		(iii) Exceeding Rs. 3.50 but not exceeding Rs. 5.00	5% adv.	2% adv.	"
		(iv) Exceeding Rs. 5.00	6.5% adv.	2.2% adv	"
9.	17.3.72	(i) As at (i) above	2.4% adv.	0.6% adv.	"
		(ii) As at (ii) above	3.5% adv.	1.5% adv.	"
		(iii) As at (iii) above	6.0% adv.	2.0% adv.	"
		(iv) As at (iv) above	9.5% adv.	5.5% adv.	"
10.	24.7.72	Value Rs. per sq. mt.			
		Exceeding / Not exceeding			
		(i) - / 3.00	2% adv.	1% adv.	"
		(ii) 3.00 / 4.00	6 P. per sq. m. plus 8% of the I.V.	3. P. per sq.m. plus 7% of the I.V.	"

(1)	(2)	(3)		(4)	(5)	(6)
		Exceeding	Not exceeding			
		(iii) 4.00	5.00	14 P. per sq.m. plus 9% of the I.V.	10 P. per sq.m. plus 7% of the I.V.	1.9 P. per sq.m.
		(iv) 5.00	6.00	23 P. per sq.m. plus 17% of the I.V.	17 P. per sq.m. plus 7% of the I.V.	"
		(v) 6.00	7.00	40 P. per sq.m. plus 18% of the I.V.	24 P. per sq.m. plus 7% of the I.V.	"
		(vi) 7.00	8.00	58 P. per sq.m. plus 18% of the I.V.	31 P. per sq. m. plus 7% of the I.V.	"
		(vii) 8.00	9.00	76 P. per sq.m. plus 13% of the I.V.	38 P. per sq.m. plus 7% of the I.V.	"
		(viii) 9.00	10.00	89 P. per sq.m. plus 11% of the I.V.	45 P. per sq.m. plus 5% of the I.V.	"
		(ix) 10.00		9.5% adv.	5.5% adv.	"

I.V. represents incremental value

11. 1.3.75 Basic duty on fabrics whose value did not exceed Rs. 15/- per sq.m. was withdrawn but on fabrics whose value exceeded Rs. 15/- per sq.m., basic duty continued to be leviable at 9.5% adv. There was no change in the additional duty rates, which remained the same as prescribed with effect from 24.7.72 stated at Sl. No. 10 above.

(1)	(2)	(3)	(4)	(5)	(6)
12.	30.4.75	Basic duty was abolished on processed rayon or artificial silk fabrics irrespective of the value of the fabric. Additional excise duty as at Sl. No. 10 above continues.			

NOTES

1. In addition to the rates of duty shown above, special excise duty at 20% of the effective basic duty was chargeable on processed rayon or art silk fabrics during the period 1.3.63 to 16.3.72. This was merged with basic duty w.e.f. 17.3.72.

2. W.e.f. 1.3.73 duty on rayon and artificial silk fabrics processed with the aid of machines operated without the aid of power or steam, other than the process of calendering with plain rollers, whether done with or without the aid of power or steam has been imposed but the rates are 40% less than those for power processed fabrics.

3. Rates of duty mentioned at Sl. No. 8, 9, 10, 11 and 12 get reduced by 5% if fabrics are cleared from the processing factory without cutting any fents, rags, chindies or any portion of these fabrics, whether damaged or not.

4. During the period 27.4.54 to 23.4.62 duty on rayon or artsilk fabrics could be paid under compounded levy procedure. Rate and amount duly were related to the number of shifts factory run, number of powerlooms/warp-knitting machinery installed/employed and variety of fabrics produced.

STATEMENT 18

MAN-MADE FABRICS (RAYON OR ARTSILK FABRICS) - PRESENT RATES OF DUTY

Description			Rate of Additional excise duty*
I	SOUND FABRICS —		
	Fabrics value per sq, metre Rupees —		
	Exceeding	Not exceeding	
	(i) -	3.00	1% adv.
	(ii) 3.00	4.00	3 P. per sq. m. plus 7% of the I.V.
	(iii) 4.00	5.00	10 P. per sq. m. plus 7% of the I.V.
	(iv) 5.00	6.00	17 P. per sq. m. plus 7% of the I.V.
	(v) 6.00	7.00	24 P. per sq. m. plus 7% of the I.V.
	(vi) 7.00	8.00	31 P. per sq. m. plus 7% of the I.V.
	(vii) 8.00	9.00	38 P. per sq. m. plus 7% of the I.V.
	(viii) 9.00	10.00	45 P. per sq. m. plus 5% of the I.V.
	(ix) 10.00	-	5.5% adv.
	I.V. represents incremental value		
II	Felts & rags		

Description	Rate of Additional excise duty*
1. Processed man-made fabrics —	
(a) containing 50 per cent or more by weight of (i) polyester fibre or yarn or both (ii) acrylic fibre or yarn or both, or (iii) a combination of (i) and (ii).	2.5% adv. (1.00 adv.)
(b) containing 30 per cent or more but less than 50 per cent by weight of (i) polyester fibre or yarn or both; (ii) acrylic fibre or yarn or both; or (iii) a combination of (i) & (ii) "but excluding fents, or as the case may be, rags of fabrics containing more than 50 per cent by weight of polyamide fibre or yarn or both."	2.5% adv. (1.00% adv.)
(c) containing more than 50 per cent by weight of polyamide fibre or yarn or both.	1.0 % adv. (0.5% adv.)
(d) containing 30 per cent or more but not more than 50 per cent by weight or polyamide fibre or yarn or both, but excluding fents, or as the case may be, rags, of fabrics containing 30 per cent, or more but less than 50 per cent by weight of — (i) polyester fibre or yarn or both;	1.0 % adv. (0.5% adv.)

Description	Rate of Additional excise duty*
(ii) acrylic fibre or yarn or both; or	
(iii) a combination of (i) and (ii) .	
2. Other processed rayon or artificial silk fabrics.	0.5% adv. (Nil)

Rayon or artsilk fabrics are exempt from Basic excise duty.

NOTES

1. Figures in brackets against II above indicate the rate of duty for rags.

2. Rates of duty on sound fabrics (listed at I above) processed with the aid of machine operated without the aid of power or steam get reduced by 40%.

3. Rates of duty on sound fabrics (listed at I above) get reduced by 5 per cent if fabrics are cleared from the processing without cutting any fents, rags, chindies or any portion of these fabrics, whether damaged or not.

STATEMENT 19

I. Number of functioning units in the organised sector

(i)	Composite	-	48
(ii)	Spinning	-	101
(iii)	Combing	-	15
(iv)	Tufted yarn/carpet	-	2

II. Installed capacity in the different sectors of the woolen industry

Spinning Capacity		Installed	
Worsted	...	2,13,700	
Woolen	...	1,14,500	
Shoddy	...	29,600	
Union	...	4,672	
Weaving Capacity	...	43,590	(powerlooms)
Combing			
Wool combing	...	47.02	million lbs.
Synthetic combing	...	5.0	million lbs.
Tufted carpets/Yarn	...	2.48	million lbs.

III. Production of woolens during 1974-75, 1975-76 and 1976-77

Description	Unity of measure-ment	1974-75	1975-76	1976-77 (Estimated)
(1)	(2)	(3)	(4)	(5)
Wool Tops	Million kgs.	13.1	13.80	12.28
Worsted yarn				
for weaving	"	11.5	10.00	8.92

Description	Unity of measure-ment	1974-75	1975-76	1976-77 (Estimated)
(1)	(2)	(3)	(4)	(5)
for hosiery	Million kgs.		2.95	2.63
for hand-knitting	"		2.51	2.24
Shoddy yarn	"	5.5	7.44	7.08
Woolen Carpet Yarn	"	14.2	23.74	23.61
Hosiery Items	"	3.0	2.21	1.97
Non-wearable fabrics	"	NA	6.70	6.38
Wearable fabrics	Million metres	NA	26.41	23.56

Source: Report (1976-77) of Ministry of Commerce, Government of India, except for information in col. (3) of item III.

STATEMENT 20

WOOLLEN YARN — TARIFF ITEM 18B

CHANGES IN THE RATES OF CENTRAL EXCISE DUTY — Year of levy - 1961

S. No.	Description	1-3-61	24-4-62	1-3-64	1-12-66 (Rs./kg)	29-5-71	17-3-72	1-9-73	10-7-74	30-8-76	77-78
(1)	(2)	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.
I.	Worsted Yarn -										
1.	Hand knitting yarn										
	(i) grey	10%	15%	15%/20%	2.70	3.5%	5%	5%	7%	20%	"
	(ii) Processed and/or dyed.	10%	15%	15%/20%	4.50	9.5%	13%	12.5%	13%	20%	"
2.	Yarn made from other than wool top.	-	-	-	-	-	-	20%/30%	20%/30%	20%/30%	"*
3.	Hair belting yarn	10%	15%	15%	0.60	2%	3%	Nil	Nil	Nil	"
4.	Others -										
	(a) of 48s counts & above.										
	(i) grey.	"	"	20%	9.60	14.5%	20%	21%	21.5%	21.5%	"
	(ii) processed and/or dyed or spun from dyed wool.	"	"	20%	9.60	14.5%	20%	21%	21.5%	22%	"
	(b) of 32s counts & above but below 48s counts -										
	(i) grey.	"	"	15%	5.25	8.5%	12%	9%	10%	10%	

1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.
	(ii) processed/or dyed or spun fromdyed wool.	10%	15%	15%	5.25	8.5%	12%	9%	10%	11%	
	(c) of 24s counts & above but below 32s counts -										
	(i) grey	"	"	"	5.26	8.5%	12%	9%	10%	6%	
	(ii) processed and/or spun from dyed wool.	"	"	"	5.25%	8.5%	12%	9%	10%	7.5%	
	(d) of 24 counts and below —										
	(i) grey	"	"	"	2.70	3.5%	5%	5%	7%	3.5%	
	(ii) processed and/or dyed or spun from dyed wool.	"	"	"	2.70	3.5%	5%	5%	7%	4.5%	
II.	Woollen yarn containing not more than 5% or virgin wool commonly known as shoddy.	Nil	25 np per kg.	NC	0.40	5.5%	7.5%	7.5%	7.5%	7.5%	
III.	Woollen yarn made from or stripped wool.	5%	Nil	Nil	0.40	5.5%	7.5%	7.5%	7.5%	7.5%	
IV.	All other N.O.S.										
	(i) grey	5%	7.5%	7.5%	0.60	7.5%	10%	10%	10%	10%	
	(ii) processed and/or dyed or spun from dyed wool.	"	7.5%	7.5%	0.60	7.5%	10%	10%	10%	10%	

1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.
V.	Waste woollen yarn commonly known *Nil as hard waste or sweeping waste. (w.e.f. 30.12.61)	Nil	NC	NC	NC	NC	NC	NC	NC	NC	

*See note 4 below

Notes: 1. 'NC' stands for no change.

2. The above rates of duty do not include special duty of excise payable on woollen yarn at the rate of 33-1/3% of the basic duty during 1.3.63 to 16.3.72. From 17.3.72 this duty was merged with the basic excise duty and the rates rounded off.

3. Of the two rates of duty shown in col. (4) against S.No.I(1) and cols. (9), (10) and (11) against S.No. 3, rate of duty applicable depends on the count of yarn.

4. W.e.f. 18.6.77, tariff description of woollen yarn has been amended to include all yarn in which wool and/or acrylic fibre predominates. Present affective rates of duty are as under.-

(a) woollen and acrylic spun yarn containing nil or not more than 1/6th non-cellulosic fibre (other than acrylic fibre) and shoddy yarn. Nil

(b) yarn containing more than 1/6th of non-cellulosic fibre (other than acrylic fibre) —

(i) Other than worsted, containing non-cellulosic fibre in the form of wastes or in the form of fibre produced out of such waste. Nil

(ii) Others Rs. 18 per Kg.

5. During the period 20-4-61 and 24-4-62 manufacturers could avail the compounded levy and pay duty accordingly instead at standard effective rates of duty shown in cols. (3) and (4) above. These rates of duty were as under.-

Description	Period from -			
	24.4.61	24.4.62		1.3.64
		(Rs. per Kg.)		
1. Worsted yarn -				
(a) of 60 counts and above.	2.10	3.25	)(	No compounded
(b) of less than 60 counts.	1.60	2.50	)(	levy rates.
(c) Others	0.40	0.60	)(	

STATEMENT 21

WOOLLEN FABRICS TARIFF ITEM NO. 21
YEAR OF IMPOSITION 1955
CHANGES IN THE RATES OF EXCISE DUTY
PART I (FROM 1.3.1955 TO 23.4.1962)

Description	CHANGES WITH EFFECT FROM						
	1-3-1955	27-4-1956	1-6-1956	14-12-1957	2-8-1958	1-10-1960	1-3-1961
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1. Woollen fabrics manufactured by or on behalf of the same person in one or more factories where less than 5 looms in all were installed.	Non-Excisable	NC	NC	NC	NC	Excisable but exempted	Nil, if only one loom. In excess of one loom but not more than 4 looms - 5.25% ad valorem
2. Woollen fabrics manufactured by or on behalf of the same person in one or more factories in which more than 4 looms in all were installed.	10% ad valorem	6.25% ad valorem	D = 4D/L Where D = duty at 6.25% D = No. of looms installed	NC (5% ad valorem)	NC (D = 4D/L Where D = duty at 5% L = No. of looms installed)	NC	6.25% ad valorem (5%)

Note:- Figures in brackets under columns (5), (6) and (8) show additional excise duty in lieu of sales tax.

contd.....

PART II

(for the period commencing with 24-4-62)

S.No.	Description	CHANGES WITH EFFECT FROM									
		24-4-1962	11-6-1962	1-3-1963	1-3-1968	1-8-1969	29-6-1971	17-8-1972	21-7-1973	30-8-1976	13-11-76
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
1(1)	Unprocessed fabrics	NIL	NIL	NIL	NIL	NIL	NIL	NIL	NIL	NIL	NIL
(2)	Processed fabrics (other than embroidery)										
(A)	If woven by a factory (other than a composite mill) and processed by an independent processor										
	(a) fabrics containing not less than 60% worsted woolen yarn -	5% (5%)	3 1/3% (3 1/3%)	4% (3 1/3%)	NC	NC	NC	4% (4%)	2.5% (2.5%)	4.25%(3.25%) 4.5%(3.5%) 4.75%(3.75%)	2.5% (2.5%)
	(b) fabrics containing not less than 60% woollen yarn (other than worsted or shoddy										
/commonly	(i) interior blankets made from indigenous wool or blankets/known as barrack or hospital blankets	"	"	"	"	"	"	"	2% (1%)	4%(3%) 3%(2.5%)	2% (2%)
	(ii) other blankets	"	"	"	"	"	"	"	2.5% (2.5%)	4% (3%)	2.5% (2.5%)
	(iii) fabrics other than blankets	"	"	"	"	"	"	"	2% (2%)	4.5% (3.5)	2.5% (2.5%)
	(c) fabrics containing not less than 90% of shoddy yarn										
	(i) blankets	"	"	"	"	"	"	"	2% (2%)	4% (3%)	2% (2%)
	(ii) melton cloth	"	"	"	"	"	"	"	1.5% (1.5%)	"	"
	(iii) other fabrics	"	"	"	"	"	"	"	1.5% (1.5%)	"	2.5% (2.5%)
	(d) other fabrics not covered by A(a), (b) and (c) above	"	"	"	"	"	"	"	NC	4%(3%) 3.75%(3.75%) 4.25%(3.25%) 4.5%(3.5%) 5%(4%)	"
(B)	If woven by a factory (other than a composite mill) and processed by a composite mill	"	5% (5%)	6% (5%)	"	"	"	NC	NC	6% 5%	4% (4%)
(C)	Other fabrics i.e., fabrics woven and/or processed by composite mills	"	"	"	"	"	"	"	"	NC	NC

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
2.	Embroidered fabrics (duty imposed on 1.3.68)										
	(i) Manufactured on vertical type automatic shuttle embroidery machine -										
	(i) under normal procedure				Basic fabric duty, if not already paid plus 20% ad valorem	Basic fabric duty, if not paid plus 10% ad valorem	Basic fabric duty, if not already paid plus 5% ad valorem	NC	NC	NC	NC
	(ii) under special procedure (with effect from 1-3-68)					Rs.19 per metre of machine per shift.	Rs.12.70 per metre of machine per shift.	NC	NC	NC	NC
(B)	Other embroidered fabrics					Base fabric duty if not already paid.	NC	NC	NC	NC	NC

NOTES

1. NC stands for no change from the previous period.

2. Prior to 1-10-1960 woollen fabric manufactured by or on behalf of the same person in one or more factories in which less than 8 looms in all were installed was non-excisable. From 1-10-60 it became excisable but was exempted till 28-2-61.

3. During the period 1-7-61 to 23-4-62 (both days inclusive) manufacturer could avail of special procedure and pay duty at the rates given below instead of at the standard rates of duty shown in part I of the above statement:-

Shift	Rate of duty per loom per shift per month	
	Basic duty	Additional duty
	Rs.	Rs.
First	100	60
Second	100	60
Third	75	60

(Duty was nil if not more than 2 powerlooms working in not more than one shift were employed).

4. From 24-4-62, woollen fabrics manufactured on handlooms were brought under excise net (earlier these were non-excisable).

5. Col. (11) contains alternative rates of duty against the same entry. The rate applicable depended on composition and percentage content of fibres in the yarn and count of yarn used.

6. Figures in brackets under columns (3), (4), (5), (9), (10), (11) and (12) show the additional excise duty in lieu of sales tax.

7. In addition to basic and additional excise duties, there is handloom cess at 1.9 paise per sq. m. on processed woollen fabrics.

8. Apart from unprocessed woollen fabrics, following fabrics are exempt from basic duty, additional excise duty and handloom cess:—
   (1) Processed khadi.
   (2) Woollen fabrics of 15 cms. or less in width.
   (3) Hairbeltings.
   (4) Cutpieces (not exceeding 23 cms. in length) if used within the factory for retrieving shoddy wool.
   (5) Woollen knitted fabrics used within the factory for manufacture of hosiery articles.
   (6) Defective portions of the woollen fabrics, given free of cost as "flag allowance" to the purchasers.

STATEMENT 22

EXCISE REVENUE FROM WOOL TOPS, WOOLLEN YARN AND WOOLLEN FABRICS DURING 1972-73 TO 1976-77

(Rs. in lakhs)

Year	Wool tops	Woollen yarn	Woollen fabrics
1972-73	390	420	559
1973-74	269	332	631
1974-75	378	350	695
1975-76	485	500	849
1976-77	794	722	1066

Source: Directorate of Statistics and Intelligence, Central Excise and Customs, New Delhi.

APPENDIX - 12

DUTY STRUCTURE - PAPER AND PAPER BOARDS

EXCISE:

Excise duty, at varying specific rates, was levied for the first time on different varieties of paper and paper boards in the year 1955. The duties were thereafter changed on a number of occasions - the last major change being in the 1976-77 Budget when the hitherto applicable specific duties were converted to ad valorem basis and the system of Tariff classification was also considerably rationalised. In the 1977-78 Budget, certain modifications were made in regard to concessions to smaller paper mills and the incentives for use of unconventional raw materials.

2. For the purpose of levy of Central Excise duty, different types of paper and paper boards are at present classified under Item No. 17 of the Central Excise Tariff and sub-divided into two broad categories. The first category /sub-item 17(1)/covers all varieties of printing and writing papers for which the prescribed tariff rate of duty is 25 per cent ad valorem. All other varieties of paper (which cover packaging papers like kraft, tissue, cigarette tissue, filter paper, match paper, toilet paper, etc.) as also all paper boards (like duplex and triplex boards, art board, ticket board, mill boards and straw boards) are classified under the second category (residuary in nature) for paper and paper boards /sub-item 17 (2)/ which are liable to a duty of 30 per cent ad valorem. This duty of 30 per cent ad valorem extends even to paper or paper boards which are manufactured from other varieties of paper/boards (usually called converted paper/paper boards) - like waxed paper, polythene coated papers, bituminised papers, corrugated boards, etc. There are, however, provisions to give relief of the duty paid on the base paper/board /by 56(A) or set off procedure/, so effectively, the converted papers also are liable to the 30 per cent duty.

3. The above duty structure has been changed by a number of exemptions which fix lower rates for certain categories of paper and paper boards or give relief to smaller paper mills and even mill board and straw board units. There is another concession which reduces the normal duty liability on any variety of paper by 33-1/3 per cent if unconventional raw materials like bagasse, cereal straws and jute stalks are used upto prescribed limits.

4. In the case of printing and writing varieties of paper, white printing paper of prescribed substance, which is required to be produced by the paper mills under paper Production (Control) Order, 1974, is charged to duty at the rate of 5.5% ad valorem. For this paper, there is an informal price and distribution control. The industry is allowed to charge ex-factory price not exceeding Rs. 2,750 per metric tonne. Certain commoner varieties of printing and writing paper (viz., unbleached, badami, creamlaid and cream wove) of substance not exceeding 65 gsm. are chargeable to a duty of 15% ad valorem while all the other categories of printing and writing varieties are liable to 25% ad valorem. Blotting paper is also chargeable to 25% though the tariff rate leviable is higher. Poster paper is chargeable to 30% as it is classified as a packaging variety. As for paper boards and other varieties of paper (excluding printing and writing) the effective duty charged at present is 30%

5. The rates mentioned above are those applicable for organised paper mills. The duty liability is considerably reduced in the case of smaller paper mills. At present, a concession is

given to smaller paper mills depending upon their annual installed capacity. The concession varies for paper mills with different installed capacity as indicated in the following Table:

TABLE

EXEMPTION TO SMALLER PAPER MILLS

S. No.	Description of Paper Mill	Extent of exemption
1.	Paper mill whose annual installed capacity in respect of all varieties of paper and paper boards does not exceed 2000 tonnes.	Seventy-five per cent of the duty leviable.
2.	Paper mill whose annual installed capacity in respect of all varieties of paper and paper boards exceeds 2000 tonnes but does not exceed 5000 tonnes.	Sixty per cent of the duty leviable.
3.	Paper mill whose annual installed capacity in respect of all varieties of paper and paper boards exceeds 5000 tonnes but does not exceed 10000 tonnes.	Fifty per cent of the duty leviable.

The above concession is not available for clearances of paper boards and certain speciality papers (cigarette tissue, glassine paper etc.) which, when produced in the smaller paper mills, have to pay the rate as for integrated paper mills.

MILL BOARDS AND STRAW BOARDS

6. In the case of the mill boards and the straw boards, (of prescribed thickness, colour etc.), to provide relief to smaller units a lower rate of duty for clearance not exceeding 1,000 tonnes has been prescribed. The first 500 tonnes of mill board or straw boards (or both) produced by any unit are allowed to be cleared at the concessional rate of 15 per cent ad valorem while the next 500 tonnes are assessed at 25 per cent ad valorem. The clearances in excess of 1,000 tonnes, are charged to a duty of 30% ad valorem.

IMPORT DUTY:

7. There are no imports of common grades of paper or paper boards. The present imports (valued around Rs. 15 crores/annum) are restricted to certain speciality papers such as currency paper, electrical insulation paper, high strength kraft paper and paper boards, filter paper etc. The imported varieties of paper or paper boards, are assessed to a duty of 120% ad valorem (basic duty 100% and auxiliary duty 20%) apart from the countervailing duty on account of the excise leviable on indigenous production. Thus, on imported papers like insulation paper for wires and cables, or filter paper, the total impact of customs and countervailing duties is 186 per cent ad valorem. These papers are presumed to be classified under the residuary tariff item No. 17(2) of the Excise Tariff, even though they are not said to be indigenously produced.

APPENDIX 13

EXCERPTS FROM THE REPORT TITLED "ROAD TRANSPORT: TAXATION AND RELATED PROBLEMS" BY SHRI ASIT CHANDMAL, Honorary Consultant to the Committee.

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(1) OBJECTIVE:

The road transport industry is a major contributor to the revenues of the Centre, the States, and municipal bodies through a wide variety of indirect taxes.

This report highlights the actual impact of the present system of taxation, and attempts the formulation of proposals for rationalisation of the tax structure as it exists to-day.

The related problem of the allocation of resources raised through road transport, especially on the construction and maintenance of roads, is also examined.

(2) INTRODUCTION:

No one component of the development process is sufficient in itself to bring about the transformation in living conditions that India is trying to achieve, and it would hence be naive and erroneous to single out any one element as the key to progress. Transport, however, has special significance because of its pervasive and ubiquitous role in facilitating the achievement of socio-economic objectives.

It is axiomatic therefore that the development of an integrated transportation system should receive top priority in the country's development strategy. The total system should be a synergistic integration of both road and rail transport. Since road and rail transport are by far the most important of the available forms of transport, we will not discuss water and air transport.

A process of total system optimization would necessarily have to consider the linkages between these two modes of transport and view them as being complementary and not competitive.

The Indian Constitution treats road and water transport differently from rail and air transport. Whereas all matters pertaining to the latter are in the Union list (seventh schedule), only national highways and waterways are Union subjects. Individual states have legislative jurisdiction over state roads and inland waterways, taxes on goods and passengers carried thereon, tolls, and taxes on vehicles (the latter being subject to the provisions of an entry on the concurrent list). The states also decide on the sales tax to be charged on vehicles, diesel, lubricants, and spares, as well as various specific fees necessary for the operation of vehicles. Given India's federal structure, and the present system of taxation,

this has inevitably resulted in the following:

(a) All states (and Union territories) have different rates of taxes on the manufacture, sale, and operations of vehicles. The rules for regulating road transport are also different. There is a plethora of rates, rules, and regulations which has resulted in highly inflated vehicle prices and operating costs.

(b) A restrictive system of licensing, permits, checkposts and other controls obtains in all states, resulting in considerable (and often unnecessary) social or economic costs.

(c) Different states give differing priorities to resource allocation and implementation of road transport projects. Intra and inter-regional imbalances in development are inevitable.

(3) INDIRECT TAXES ON THE MANUFACTURE & SALE OF VEHICLES:

3.1 Introduction

3.1.1 The incidence of indirect taxes on the manufacture and sale of vehicles can be divided into two categories:

(a) "Invisible" tax in manufacture, i.e. taxes which are levied on inputs at the different production stages, from raw materials through intermediate products to the assembled vehicle. This represents the tax on the ex-works cost of the vehicle, and are not "visible" to the consumer.

(b) "Visible" taxes on sale, i.e. post-manufacture taxes like excise and sales tax and octroi on the finished vehicle. This is an easily ascertainable component of the tax included in the final price to the customer.

3.2 "Invisible" Tax in Manufacture

3.2.1 The production of vehicles involves multi-stage highly specialised operations, starting from basic industries such as steel, aluminium, glass, rubber, through intermediate products such as tyres, batteries, starter motors, forgings, castings going into the assembly of aggregates such as gear boxes and engines, to finally the fully assembled vehicle.

3.2.2 The incidence of indirect taxes is at all these various stages of production. To illustrate the magnitude of the numbers involved, TELCO alone purchases 5000 items essential for the manufacture of its vehicles. These items, which are purchased from 600 suppliers, range from raw materials like steel and sand; hardware items like nuts and bolts; highly sophisticated products like fuel injection pumps, starter motor, generators, bearings, and indirect materials like cutting tools and lubricants. Each one of the suppliers of these items has his own multiplicity of suppliers. Thus the computation of the total indirect tax content in the final price of a vehicle to the consumer is extremely

complex and time consuming. This has now been done by the Association of Indian Automobile Manufacturers (AIAM) for 8 different vehicles types.

3.2.3 We have used the data from the AIAM study for the following representative vehicle models.

(a) Truck: TELCO 1210 chassis (excluding body), payload 7.1/2 tonnes, 4788 cc., DI Diesel Engine, semi forward control, produced by Tata Engineering & Locomotive Company Limited, Jamshedpur.

(b) Mini-Bus: (Matador) Light commercial vehicle (including body), 4-wheeler, with 1797 cc. diesel engine, produced by Bajaj Tempo Limited, Poona.

(c) Car: (Padmini) Passenger Car, 4-door sedan, with 1089 cc. petrol engine, produced by Premier Automobiles Limited, Bombay.

(d) Scooter: Bajaj 150 cc., Petrol Engine, produced by Bajaj Auto Limited, Poona.

3.2.4 In short, the association collected and collated data on indirect tax incidence for the following categories:

(a) "Direct payments", i.e. taxes directly paid by a vehicle manufacturer on all his purchases.

(b) "Built-in Tax", i.e. the tax element already existing (prior to purchase) in the semi-finished and finished goods purchased from vendor firms.

(c) "Base Tax", i.e. estimated built-in tax in certain base materials supplied by indigenous outside parties to both the vehicle manufacturers and the vendor firms.

(d) Central Excise: This is chargeable on the ex-works price (i.e. cost of manufactured vehicle plus tax in manufacture), though at some centres the excise authorities include items like dealer's commission in the excisable value.

(e) Central sales-tax: 4% on ex-works price plus central excise.

(f) Local (State) Sales-tax: This varies from state to State and vehicle-type to vehicle-type. The rate is applied on a base of all costs, charges and taxes (including central sales tax) upto the stage of levy.

(g) Octroi Duty: This rate varies from vehicle-type to vehicle-type and from one local area to another. The levy is collected on a base of all costs and taxes borne till then (including local sales-tax).

3.2.5 The summarised findings of this study (after taking into account the main changes in excise duty made by the Finance Bill, 1977) are given in Exhibits 3.1 and 3.2 and Exhibits 3.3 and 3.4.

3.3 An Appraisal of the present system

3.3.1 Effect on prices

Exhibit 3.1, clearly shows effect of taxes on road transport vehicle prices. The actual tax incidence, as a percentage of the cost of the vehicle excluding taxes, ranges from between 51% to 52% for scooters and cars to between 59% to 65% for commercial vehicles. This tax incidence is naturally fully reflected in the price to the consumer, thus resulting in the present high prices.

The inflationary effect of the present system of taxes is not so readily discerned because of the cascading effect and to some extent due to the tax component of working capital locked up in inventories and work-in-progress at the various production stages.

3.3.2 Cascading effect

The present system of multiple taxation gives rise to cascading which has a hidden but substantial effect on the prices of the end product. This is highlighted in Exhibit 3.2. For example, although the nominal tax on a TATA truck in Bombay is 32%, the total tax content amounts to as much as 59% (which includes tax on material inputs in the manufacturing process). The difference is mainly on account of "invisible" taxes whose effect is compounded by the impact of the end "visible" tax. Hence, multiple taxation leads to cascading and substantially inflated prices of the end product.

Exhibit 3.3 gives examples of the cascading effect on 5 major components used in the manufacture of commercial vehicles.

Exhibit 3.1

TAX INCIDENCE ON VEHICLES: EFFECT ON PRICES

VEHICLE TYPE (1)	PRICE TO CUSTOMER (1) (2)	TOTAL TAX CONTENT (3)	TAX AS % OF PRICE (EXCLUDING TAX) (4)
	(Rupees)		
1. Truck	1,11,478	41,319	58.9%
2. Mini-Bus	54,060	21,442	65.7%

VEHICLE TYPE (1)	PRICE TO CUSTOMER (1) (2)	TOTAL TAX CONTENT (3)	TAX AS % OF PRICE (EXCLUDING TAX) (4)
	(Rupees)		
3. Car (2)	30,395	10,158	50.2%
4. Scooter	4,064	1,370	50.9%

Notes: (1) This is a derived figure, based on the AIAM data and incorporating the changes made in the Finance Act, 1977. Similarly, the prices shown exhibit 3.4 are also derived. These are not materially different from prevalent actual prices.

(2) The AIAM data does not seem to have considered 6% additional sales tax for Premier Padmini Car. Considering this, the figures under columns (3) and (4) would be Rs. 10,348 and 51.6% respectively.

(3) The consumer price indicated is the price for sale in Bombay.

Exhibit 3.2

TAX INCIDENCE ON VEHICLES: CASCADING EFFECT

	VEHICLE TYPE			
	TRUCK	MINI-BUS	CAR	SCOOTER
1. NOMINAL RATE				
(a) Central Excise (%)	12.5%	15.0%	17.5%	12.5%
(b) State Sales-tax (including surcharge (%)	12.0% + 6.0% SC	12.0% + 6.0% SC	12.0% + 6.0% SC	12.0% + 6.0% SC
(c) Octroi	4.0%	4.0%	-	3.0%
SUM-TOTAL OF NOMINAL RATES (%)	31.9%	34.8%	32.4%	30.6%
2. CUMULATIVE LEVY (%)	58.9%	65.7%	51.6%	50.9%

The above rates are calculated for vehicles sold in Bombay.

Exhibit 3.3

CASCADING EFFECT ON MAJOR COMPONENTS

	NOMINAL RATE TO MANUFACTURER OF COMMERCIAL VEHICLES			CUMULATIVE LEVY
	EXCISE DUTY	SALES TAX	TOTAL NOMINAL RATE	
	%	%	%	%
Tyres & Tubes	55	4	61.2	87.9
Starter Motor	20	4	24.8	41.9
Fasteners	10	4	14.4	31.1
Radiator	-	4	4.0	33.3
Bearings	15	4	19.6	53.5

Exhibit 3.4

VARIATIONS IN PRICES & CUMULATIVE LEVY

	BOMBAY	CALCUTTA	MADRAS	DELHI
PADMINI CAR				
Price to customer (in Rs.)	30,395	33,180	31,392	32,449
Total Tax Rate	51.6%	50.0%	48.2%	52.2%
TELCO TRUCK CHASSIS				
Price to customer (in Rs.)	1,11,478	1,07,710	1,10,098	1,05,263
Total Tax Rate	58.9%	55.7%	56.7%	50.2%

3.3.3 There was a sharp fall in the demand for cars (and, consequently in their production and sale) starting in 1974 (please see Exhibit 3.5 below), due to prices highly inflated by the tax structure and the final total tax incidence. Of course sharp increases in operating costs, mainly the tax on petrol, was also a major contributory factor to the slump in demand.

The demand for cars was much higher than the sales shown in the years prior to 1974-75. There were 5-year waiting lists. However, starting from 1974, and especially in 1975, demand slumped and cars were being stock piled. Only when relief in taxation was given that demand started picking up again.

A reduction in excise duty from 20% to 15% was effected from 16.3.1976. Further, with effect from the same date, tyres and tubes which carried an excise duty of 55% were exempted from duty if fitted as original equipment on cars. Local sales tax was also cut by as much as 50% in nine major states. The increase in demand during 1976 was apparent immediately. (However demand has still not picked up to pre 1974-75 levels). The excise duty has since been increased from 15% to 17.5% in June 1977.

Exhibit 3.5

PRODUCTION AND SALE OF MOTOR CARS

YEAR	PRODUCTION	SALES
	Nos.	Nos.
1972	38828	38901
1973	39937	39712
1974	36009	36252
1975	23070	22939
1976	31556	30602

3.3.4 The present tax structure also results in unintended effects. While the cumulative levy as a percentage, significantly lower for cars as compared to commercial vehicles (in Bombay, they are 52% and 59% to 65% respectively), this disparity remains even if notional adjustments on account of central sales tax and octroi are made to ensure strict comparability of figures. (Please refer to Annexure 1 for details of these calculations). Since in a developing country where, more encouragement need be given to mass transport (as against personal transport), this disparity calls for correction.

The only explanation seems to be that under the present system it is virtually impossible for the tax levying authorities to calculate the impact on the cost of the final product of a change in tax rate on the multiplicity of raw materials and intermediate products which go into the manufacture of vehicles.

Since we have shown that diminishing returns are operating in the case of cars (and hence the tax rates on cars should not be increased but reduced) clearly there is a case for reviewing the taxes borne by commercial vehicles.

The arguments for such a reconsideration are obvious: commercial vehicles encourage investment, thus providing employment, and by taxing the annual output, a stream of revenues is generated for long periods of time, which would more than make up for the one time loss of revenue entailed in lowering taxes.

3.3.5 The other undesirable effect of the present system of taxes is that it increases working capital needs. On the basis of a sample study of actual inventory holdings, it is found that for TELCO vehicles alone, the tax element in working capital locked up, at both TELCO and its vendor firms, is over 28 crores. At present interest rates, the interest charges on the tax component in working capital is over Rs.4 crores. Surely, this is a totally non-productive cost, which inevitably is reflected in the price to the consumer. Further, capital, which is a scarce resource, is unnecessarily frozen under the present tax system.

3.3.6 The cascading effect increases the cost to the vehicle manufacturer of vendor item inputs. In general, the longer the chain, and greater the number of product transfer linkages that are taxed, the greater will be the impact of the cascading effect, and hence greater the cost. Also, the greater the value added in the earlier stages, the greater will be the impact of the tax on taxes. It may happen that in a cost reduction drive the industry would tend to reduce the number of such transfers, i.e. manufacture of process in-house rather than encourage ancillary production. This is contrary to the Government's and the industry's objective to encourage ancillary manufacturers and small-scale vendor firms.

3.3.7 In addition to the above, there is also an inflationary effect because of the so-called "mark-up on tax". This occurs because, at present, taxes on manufacturing inputs are an integral part of input costs and hence at each stage of production when the product changes hands, the mark-ups (and, consequently prices) are inflated to the extent that it is calculated on the tax-inclusive cost upto that stage.

3.4 Value Added Tax - A Viable Alternative

3.4.1 Many countries have adopted the Value Added Tax (VAT) system in place of the conventional multi-stage turnover tax. We are of the opinion that an optimal VAT system can be designed in the Indian context so as to eliminate the basic disadvantages of the present system of indirect taxes. Such a system would achieve the following:

(a) Cascading and unintended effects: Under the VAT system, the effective tax rate depends solely on the tax rate applicable at the final stage. The incidence of taxation can hence be precisely calculated, and the Government can be certain of the tax burden imposed on a product. This is in sharp contrast to the present system where, as 58.9% and 50.2%, effective tax rates on TELCO trucks and Padmini cars are much higher than the nominal rates of 31.9% and 31.6% respectively. The consequent unintended effect of existing cascading is apparent.

(b) Adverse effect on prices: As already seen, the present system raises prices without adding to Government revenues, viz. the "mark-up on tax" effect and the interest cost of working capital unnecessarily locked up as tax component in inventories. We estimate that for a TELCO vehicle,

the inflated mark-up effect comes to about Rs. 1, 500 per vehicle and the extra interest cost is about Rs. 1, 600 per vehicle. Under the VAT system, the availability of tax credits on inputs would simultaneously release scarce working capital for (other) productive purposes and also eliminate the mark-up on tax.

(c) Vertical integration: Under the present system the cumulative tax incidence is higher if the value added is more in earlier stages and it also increases with the number of taxable stages. This tax incidence can be minimized by maximizing vertical integration. The VAT system would remove this disincentive against the development of the ancillary sector.

(d) Duty drawback on exports: At best, the duty drawback facilities are presently available for excise, customs, and countervailing duties paid on direct material inputs. This normally is much less than the total tax component. A VAT scheme would allow for a total refund of all indirect taxes (i.e. VAT exempts exports), thereby making them more competitive in international markets.

(e) Tax evasion: Under the tax credit method of VAT (the "invoice" method), evasion is difficult because it provides a ready method for cross-checking records. Also it is in the interest of a taxable person to insist on paying tax and obtaining an invoice as otherwise he would not be able to claim tax credit.

3.4.2 VAT administration:

Under the "invoice" method, a manufacturer's net VAT liability is the difference between the VAT collected on sales and VAT paid on purchases, the VAT liability being discharged on a monthly or quarterly basis. Administrative costs are not expected to rise because the sales tax and excise duty administration already in vogue is both elaborate and comprehensive. As for the assessees, it is the organized sector of the industry which generates a large chunk of indirect taxes. This sector already has accounting practices amenable to changes necessitated by VAT. However, for successful implementation of VAT, the system users would have to be properly educated.

3.4.3 Multi-stage turnover taxation, single-stage manufacturers' sales taxation, tandem systems, excise exemptions under Rules 56-A and 56-B of the Central Excise Rules could also be possible alternatives to the present system. However, except for Rules 56-A and 56-B, none of the other systems would be acceptable. Even excise exemptions under these rules are limited and restrictive in scope, and cumbersome in administration. Admittedly, the rules can be extensively amended and administrative simplification introduced. Logically extended, such improvisations would inevitably lead to a system of VAT, which is thus the best possible alternative to the present system of taxation.

(4) INDIRECT TAXES AND ROAD TRANSPORT OPERATIONS

4.1 Introduction

The various types of taxes borne by the owner in order to operate his vehicle are as follows:

(a) Fees and taxes such as passenger tax, motor vehicle tax, permit fees, etc., can be called "Specific" taxes and are usually a fixed cost per annum.

(b) "Non-Specific" or variable taxes which vary with the operations of vehicles on the road, such as excise duty, sales tax, customs duty and octroi, if any, on diesel, lubricants and spare parts.

Incidentally, apart from the above, on certain routes, the vehicle operator has to pay octroi transit fees or miscellaneous tollfees like bridge tax, etc.

4.2 (A) SPECIFIC TAXES AND FEES:

4.2.1 Items of taxes that come under this category arise out of specific enactments made on the road transport industry. The rationale behind the imposition of these taxes is to cater to certain public costs of the industry. It should be noted that under entries 56 and 57 of the List II of the Seventh Schedule of the Constitution of India, the "taxes on goods and passengers carried by road or on inland waterways and the taxes on vehicles, whether mechanically propelled or not, suitable for use on roads, including tramcars, subject to the provisions of Entry 35 of List III" come under the State List. The states were thus empowered to enact laws for the collection of taxes from the industry according to their requirements. This has resulted in a plethora of fees and taxes and also wide disparities between the states in the burden of taxes borne by the vehicle owners.

4.2.2 The following is indicative of the innumerable fees borne by an operator. (The fees and taxes given in brackets are approximate figures applicable in Maharashtra.)

(a) SMALL FEES

(1) Fee for learner's driving licence (Rs.3)

(2) Fee for driving test (Rs.5 for each test in each part of the third schedule)

(3) Fee for driving licence (Rs.11)

(4) Fee for issue of conductor's licence (Rs.5.50) (applicable for passenger transport)

(5) Fee for issue of public service vehicle badge (Rs.3.50)

(6) Fee for issue of conductor's badge (Rs.3.50)

(7) Fee for registration - varies for motor cycle, light motor vehicle, and other vehicles (Rs.5, Rs.15, and Rs.30 respectively) OR

(8) Fee for temporary registration of a motor vehicle (Rs. 2)

(9) Fee for inspection of Motor Vehicles for issue or renewal of fitness certificate (Rs. 5)

(10) Fee for issue of fitness certificate (Rs. 10) OR

(11) Fee for renewal of certificate of fitness

(a) if applied 30 days before expiry (Rs. 5)

(b) other-wise (Rs. 10)

(12) Fee for making note in certificate of registration hire purchase agreement/hypothecation (where applicable) (Rs. 10)

(13) Fee for transfer of ownership (when vehicle is sold/transferred) (Rs. 2 plus Rs. 5 when ownership is subject to hire purchase)

(14) Fee for issue of trade certificate (annual) (Rs. 10)

(15) Fee for grant of permit/counter signature (Rs. 10) OR

(16) Fee for renewal of permit/counter signature (Rs. 5)

(17) Fee for grant or renewal of temporary permit (where applicable) (Rs. 5 per month)

(18) Fee for replacement of motor vehicles covered by stage carriage permit/public carrier permit/contract carriage permit when replacer vehicle is of larger capacity (where applicable) (Rs. 18)

(19) Fee for transfer of permit (when permit is transferred) (Rs. 10)

Note: In respect of all the above separate fees are prescribed for issue of duplicates, for renewals, for preferring appeals against refusals, and for obtaining copies of documents for the purpose of appeals.

(b) LARGE TAXES

(20) Motor vehicle tax - also known as road tax, token tax, etc. (Rs. 4, 130)

(21) Goods tax in respect of public goods carriers (Rs. 1, 170)

(22) Passenger tax in respect of passenger buses (Rs. 26, 000)

(23) Wheel tax (Rs. 300)

(24) Permit fees like that for national, zonal, temporary permits payable to States other than the State of Origin. (Fees depend on the nature of permit. For example, it is Rs. 700 per annum for each state for national permits; Rs. 650 per month for temporary permits in Uttar Pradesh, etc.)

The fees listed above are indicative and not exhaustive.

4.2.3 Small Fees

There does not seem to be any rationale behind the multiplicity of rates ranging from Re. 1 to Rs. 11 for various fees (there are about 70 such items in the Bombay Motor Vehicle Rules). The prevalance of innumerable low rates of fees for various purposes should be eliminated or rationalized. For example in Maharashtra a fee of Rs. 5.50 is charged for issue of conductor's licence and Rs. 3.50 for issue of conductor's badge. There could as well be a single collection of say Rs. 9 instead of two separate fees. Another instance is the prescription of Rs. 5 for issue of a duplicate driving licence, whereas it is only Rs. 2.50 for issue of duplicate conductor's licence.

It is difficult to imagine the harassment, nuisance value, and social and administrative costs of such fees. The revenue from these fees is insignificant and utterly incommensurate with the costs of collection. For Maharashtra during 1975-76, this represented 2% of the other Motor Vehicle specific taxes and only 0.2% of the state's total revenues (excluding tax allocations from the centre).

4.2.4 Large Taxes

Road tax is a tax under the State Motor Vehicle Taxation Acts levied on all motor vehicles used or kept for use in such states. The proceeds of the tax collected under this Act are normally utilised for compensating the local authorities towards maintenance of roads falling in their jurisdiction. Evidence of payment of motor vehicle tax or road tax also operates as a licence to ply on the roads of the state, subject only to the restrictions imposed by the permit issued by the Transport Authority concerned. There is also a provision for the issue of a temporary licence on the payment of the prescribed tax.

Some of the states have a separate tax on goods and passengers, levied on public carriers (goods transport) and stage carriages (passenger transport). Some of these states accept a composite fee in lieu of goods tax and/or passenger tax.

4.2.5 Different rates have been prescribed by various states for commercial vehicles and non-commercial vehicles, and the rates vary according to weight specifications in the case of goods vehicles and permitted passenger capacity in respect of passenger vehicles. A comparison of rates between the different states is given in Exhibit 4.1, in respect of vehicles having a specified laden weight (15,500 kgs) and passenger capacity (50 seats plus 17 standees).

4.2.6 While many of the states have not supplied the information, a comparison of the available data presented in Exhibit 4.1 reveals the wide disparity between state to state. It would be seen that the motor vehicle tax for goods carriers is 5 times higher in Kerala and Tamil Nadu (at Rs. 5,000 per annum) than in Chandigarh. Although Chandigarh has a goods tax of Rs. 300 per annum in addition, this does not narrow down the difference to any great extent. Goods tax is prevalent in Maharashtra (Rs. 1,350) and Bihar (Rs. 3,000) but not in Bengal or Tamil Nadu. Further, the road tax on passenger buses in Kerala and Tamil Nadu /both of which do not have a separate passenger tax/ vary considerably at Rs. 15,360 per annum and Rs. 32,160 per annum respectively.

4.2.7 The levy of passenger tax, is high percentage of fares collected. It ranges from 10% to 35% in the states which have supplied the information. Since the rates in some states like Madhya Pradesh seem to be on fares inclusive of tax, the effective rate of tax would work out to much more than what it appears, i.e. 25% on fare inclusive of tax would actually be 33.1/3% on fare. This difinitely acts as a deterrent to the growth of road transport.

In the light of what is stated above, there does exist a case for review of the levy of passenger tax. The transport undertakings should be saved the time and efforts that they now expend to satisfy the authorities on the fares collected by them. The states which have not yet merged the goods and passenger tax with the motor vehicles tax would do well to follow the example set by other states like Kerala and Karnataka. This will convert variable taxes into specific (fixed) taxes. This step alone would help in moving towards uniformity between states and make tax collections administratively simpler. Exhibit 4.1 shows the collections from the above forms of taxation for three financial years. It is our considered opinion that the same revenue could be obtained by the levying of a consolidated motor vehicles tax, viz., consolidating motor vehicles and goods tax for trucks, and motor vehicles tax and passenger tax for buses. This simplification is desirable as much from the point of view of Government's administrative convenience as it is for the expediency of the transporters.

4.2.8 Even though the Indian Motor Vehicles Act is a Central Act, each State Government has framed separate rules for its territory resulting in unnecessary variations between states. In this context, a certain degree of uniformity all over the country is desirable. Also, and equally important, is the need to simplify the various levies and procedures, both for small and large fees, to the extent possible, without vitiating the control or revenue aspects. Finally, there should be some check to see that these levies do not become unduly high.

4.2.9 The levy of various small fees mainly serves the Control function rather than the revenue function. As such, any rationalisation would have to be comprehensive in coverage without having too many rules and fees. We have recommended a rationalised structure (appended to the report as Annexure 2 consisting of 16 items of levy (as against the present 75) and 6 different rates (as against the 16 rates now in vogue for comparable items). This scheme can serve as a model for the different states.

4.3 (B) NON-SPECIFIC OR VARIABLE TAXES

In the previous section, we identified the different specific taxes met by the road transport industry. These are paid as a basic pre-requisite for operations on the road. In addition, in the process of road transport operations, the operator has also to pay "non-specific" or variable taxes. These are in the form of excise duty, sales tax, customs duty and octroi, if any, levied on fuel, lubricants and spares, all of which are essential to operate a vehicle. The total impact of these taxes is proportional to the extent of vehicle operations.

4.3.2 In this section, we discuss these non-specific (variable) taxes and highlight their impact in terms of costs to the individual operators.

(a) Excise duty

4.3.3 Central excise duty (at varying rates) is levied on the following basic inputs to road transport operations:

	Item	Excise Duty Rate adv.
1.	Fuel:	
	(i) Petrol	290%
	(ii) Diesel	67%
2.	Lubricants	20%
3.	Spare Parts:	
	(i) Tyres & Tubes	55%
	(ii) Batteries	17.1/2%
	(iii) Other spare parts (i.e. brake linings, clutch facings, engine valves, gaskets, nozzles and nozzle holders, pistons, piston rings, gudgeon, circlips, shock absorbers, spark plugs, thin-walled bearings, tierod ends, electric horns, filter elements, inserts and cartridges).	11% or 20% (as applicable)

(b) Sales Tax

4.3.4 Sales tax is paid on fuel, lubricants, and spares at different rates. These rates are not the same in every state since each state has its own sales tax structure. In Exhibit 4.2 we have listed the various sales tax rates as applicable on these inputs in different states. The corresponding revenues accruing to the states have also been tabulated.

4.3.5 We note that significant variation in sales tax rates does not exist for the different states. Given this low degree of divergence, it would not be very difficult to arrive at a uniform sales tax structure for the country.

(c) Customs Duty

4.3.6 In addition to excise duty and sales tax, customs duty is also paid in respect of imported spares. The rate applicable is 100 per cent ad valorem on c.i.f. value.

(d) "Invisible" Taxes

4.3.7 In addition to the above items of "visible" taxes (except for imported spares), the cost of fuel, lubricants and spares would include items of "invisible" taxes which go into the production of these basic inputs.

4.3.8 These are the non-specific tax payments made by the operators in the course of their operations. We have also covered specific payments in an earlier section. Having discussed both these components of total indirect taxes in operations, we proceed to illustrate their impact on the cost of operations.

4.4 (c) IMPACT OF TAXES ON OPERATING COSTS

4.4.1 Introduction

A detailed analysis of the operating costs of the two sections of the road transport industry viz., goods transport, and passenger transport in mofussil areas, has been made for fully effective vehicles operating in Maharashtra. The results of this analysis (alongwith the assumptions) have been given in Exhibit 4.3 of the report. The findings of this analysis have been summarized as under.

4.4.2 The percentage of indirect tax element on the total cost of operation, excluding such taxes, works out to about 49% in the case of small operators, 45% in the case of fleet operators (both referring to goods transport) and 55% in the case of road transport undertakings.

The major components of the 'non-specific' or variable, tax element on the cost of goods transport are the prevalent taxes on diesel and tyres. These account for 82% of the total indirect taxes on variable cost, and 40% of the total variable cost excluding taxes.

For passenger transport, the major component is passenger tax, accounting for 65% of the total indirect taxes on variable cost, and 61% of the total variable cost excluding taxes.

4.4.3 If the goods transport operations are really confined to the maximum legally permitted load of 9 tonnes, the small operator would at best break even and the fleet operator would lose over Rs. 5,000 per annum, since the total contribution would fail even to cover his fixed expenses.

4.4.4 Consequently, in order to earn reasonable profits, the number of kilometres run and/or the average tonnage carried has to be substantially increased by the truck operators. Because of the limitations on the distance covered per day, due to delays at checkposts and other impen-iments, the hard-pressed operator is compelled to resort to overloading - even beyond the legally permitted overloading limit of 25%. This over-loading can be as high as double the recommended payload of the vehicle. For example, a TATA Semi-forward control truck having a payload of 7.1/2 tonnes is often loaded with 15 tonnes or more. Such overloading leads to vehicle wear and tear, road damage, great risks in passing through bridges and culverts designed to stand a much lesser load and the incentive to commute to rural areas where roads are not developed is reduced. Overloading is also a great safety hazard, resulting in many accidents.

4.5 Conclusion

4.5.1 Our analysis shows that substantial revenues are generated in the form of indirect taxes on road transport operations. We have estimated that for a fully effective vehicle in Maharashtra, these taxes amount to Rs. 54, 000 per truck and Rs. 54, 000 per bus on an annual basis (Exhibit 4. 3). However, taking into account the impacts of reduced operations (and operational efficiencies) over a vehicle's life (1), and allowing for variations in specific and non-specific fees and taxes in different states (Exhibit 4. 1: Table 1 and Exhibit 4. 2: Table 1), the average annual taxes from vehicle operations are estimated to be around Rs. 36, 000 per truck and Rs. 41, 000 per bus (2). Considering the active commercial vehicle population to be around 3, 00, 000 trucks and 1, 00, 000 buses, the indirect tax revenues generated by their operations would be of the order of Rs. 1, 500 crores, i. e. more than 12% of the total tax revenues generated in the country.

5.2.6 The Socio-economic Cost of Octroi

The social costs because of octroi and other check-posts are of two different types, viz. delays at check-posts and their consequences, and the fact that check-posts become the foci for the growth of corrupt practices. A survey to quantify delays was carried out on some of the major routes in India. The findings of this study are given in Exhibit 5. 3.

5.2.7 Delays at check-posts range from 30% to 45% of the effective travelling time (the total time for which a vehicle is actually moving). The impact of delays of such magnitude in terms of socio-economic costs is:

(1) Delays reduce the overall speed of road transport. It is only during the actual movement that fixed costs (in terms of investments in vehicles and establishment) and variable costs (on fuel, salaries and wages, and maintenance costs) are recovered. The non-recovery of these costs during delays implies a 'shadow cost of delay' to the operator, and therefore increase in transportation costs which are ultimately borne by the customer.

(2) Delays imply locking up of goods carrying capacity. Considering that commercial vehicles cost as much as Rs. 1. 25 lakhs, the cost of making unproductive capital assets of the order of Rs. 350 crores is staggering.

(3) From the view point of investment, it may be noted that the total capital cost of installing capacity for producing 35, 000 vehicles per annum would now be at least Rs. 800 crores. Moreover, such a capacity can only be realised after a gestation period of a decade.

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(1) Detailed calculations for tyres and diesel consumption are appended in Annexure 3.

(2) Analysis of the average annual taxes is presented in Annexure 3.

(4) Removal of octroi check-posts would release this capacity for productive use. Besides the increase in capacity is immediate.

(5) Frequent stoppages imply substantial deviations from optimal cruising speed. Specifically, the vehicle has to keep on breaking and accelerating at very frequent intervals, and, at times, the engine is kept idling while waiting at check-posts. In addition, the operator drives faster to make up for the time lost at check-posts. All these deviations from the optimal recommended cruising speed result in insufficient attention to road safety, avoidable fuel consumption, and greater wear and tear of tyres, brake linings and gear-box. Out of these factors, the non-productive consumption of fuel literally burns up a valuable nonrenewable resource. In immediate terms it implies greater operating costs (and the resulting inflationery impact on freight rates) and drainage of valuable foreign exchange resources. The cost of accidents, including the loss of human lives, is not quantifiable.

5.2.8 We have also seen that, besides delay, check-posts are nucleii around which corruption crystallizes. No further comment on this very real impendiment to the flow of traffic is made in this report.

5.2.9 We have seen in this section that the socio-economic costs of check-posts (especially octroi) are staggering. It is apparent from the discussion that some alternative has to be found to the present octroi scheme. This should be such that the check-posts can be abolished without affecting the revenues of local bodies.

Exhibit 5.3

DELAYS DUE TO CHECK-POSTS

SR. NO.	ROUTE	NUMBER OF CHECK-POSTS*	TIME SPENT AT CHECK-POSTS (HRS) (1)	EFFECTIVE TRAVELLING TIME** (HRS) (2)	(1) AS% OF (2)
1.	Delhi/Bombay	41	15.48	33.18	46.65%
2.	Madras/Calcutta	46	15.67	48.00	32.65%
3.	Delhi/Calcutta	55	10.68	35.22	30.32%

* Comprises mainly octroi check-posts.

** This is the time for which the vehicle is actually moving.

(6) ROAD DEVELOPMENT

6.1 Importance of Roads in National Development

Having described the enormous revenues generated by the road transport industry, we now argue the case for a much higher proportion of these revenues to be allocated to road development. Roads are an essential part of the infrastructure necessary for development. The effect on creation of employment and increasing agricultural production through road construction and maintenance is considerable. We describe these benefits in the following pages.

6.2 Road Development and Employment

6.2.1 The National Council of Applied Economic Research (NCAER), in a study carried out in 1960 on 'Employment Potential of Road Transport' estimated that the total employment opportunity generated is 17.02 per bus and 11.12 for goods vehicles in terms of number of workers. These figures represent the total of direct and indirect employment opportunities and also take into account the multiplier effect which operates because of the employment in the various service sectors which are attached to the road transport industry.

6.2.2 In another study, in 1974, on 'Employment in Road Transport and Road Construction', NCAER arrived at the following figures for man-years of employment opportunities created in the construction of 1 km. of different kinds of roads:

Exhibit 6.1

Type of Road	Employment Opportunity (Man-Years Per KM)
National Highway	141 - 153
State Highway	85 - 96
District Road	78 - 85
Village Road	25 - 32

6.2.3 It was estimated in the study that a Rs. 1 crore outlay for road construction would generate employment opportunities equivalent to 5,000 - 5,200 man-years (or 7,200 man-years for village roads). Taking Central and State sectors together, the total outlay on road construction in the Draft 5th Five Year Plan was Rs. 1,400 crores. As for village roads, an additional outlay of Rs. 500 crores was suggested. With these outlays, NCAER estimated that the total employment opportunity would be 10.8 million man-years. Most of these employment opportunities would be for the class of unskilled workers, that is, the poorest sections of society.

6.3 Road Development and Agriculture

6.3 1 In a study on 42 randomly selected road-side(RS) villages and another 42 isolated (IS) villages in the Tungabhadra Project area (1), comparisions were made for the following:

(a) Popularity of farm equipment.

(b) Adoption of improved farm practices (e.g. use of high-yielding variety of seeds, fertilizers, plant protection, etc.)

(c) Transport costs for different commodities.

(d) Village and market prices of various agricultural commodities.

The findings of this study showed that:

(a) Improved farm techniques were much less popular in the isolated villages as compared to road-side villages. For example, tractors were used in 95% of the road-side villages, while the corresponding percentage for isolated villages was 24%. Some of the farmers in the isolated villages indicated that although they could afford to buy tractors, they were unwilling to do so because of bad-roads and difficulty in operation and servicing them.

(b) The adoption, and level of adoption, of improved farm practices, namely, the use of high yielding seeds, fertilizer application and plant protection for various crops like jowar, cotton, groundnuts, bajra, and paddy were relatively more popular in road-side villages as compared to isolated villages.

It was found that the percentage of farmers adopting high yielding variety of jowar, cotton, and groundnuts was around eight times higher for road-side villages. Similarly, for jowar and cotton, the percentage of farmers applying fertilizers was six times higher in road-side villages as compared to isolated villages.

(c) Although the distance from the market centres to both isolated and road-side villages was approximately the same, the cost of transportation per tonne-mile of both inputs as well as various agricultural commodities was nearly double for isolated villages as compared to road-side villages.

(d) In the case of isolated villages farmers had to invariably use bullock-carts to transport their produce to the nearest roads and then use trucks. This resulted in more time and cost for transporting their commodities to the market towns. The cost of transportation per tonne-mile was found to be more for carts than for trucks by at least 50%.

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1. 'Transport and Green Revolution' by R. Ramanna and A.N. Krishnamurthy published in 'Transport Planning and Finance', ed. D.N. Najundappa, Karnataka University: Dharwar 1973.

(e) The farmers in isolated villages are denied uptodate price information because of lack of adequate transport and communication facilities, and have to depend on either the itinerant merchant or neighbours who have recently visited the market town for price information. Consequently, they are obliged to sell their produce at unremunerative prices.

6.3.2 From the above discussion it can be concluded that farmers in the isolated villages are in a disadvantageous position, both in respect of procuring their input materials and disposing of their produce. Hence, to sustain an accelerated rate of agricultural productivity and production the development (and provision) of transport facilities in terms of village to village and rural to urban roads is vital.

6.3.3 Studies have shown that in all developing countries, road development by itself leads to generation of large agricultural surpluses since farmers then produce not merely for subsistence but also for market sales.

6.4 Road and Roads Development: Present Statistics and Resources Allocation

6.4.1 The Brookings Institute has made the following observations on the condition of Indian roads:

> ".....One of these impendiments is the state of highways. Four out of five miles of National Highways are one lane. There is not yet a completely connected National Highway system. 400 kms. of gaps are yet to be closed, and more than 50 major bridges need to be built. Culverts and bridges are often weak, and pavements inadequate. State and district roads, which comprise the rest of the main road system, are even poorer than the National Highways. Narrow, and bumpy, often flooded during the monsoon, they are severly limited in load-carrying capacity and permissible speed. And on the vastly larger network of village access roads, conditions are generally so poor that motorized traffic is impossible."

Even after allowing for subsequent improvement (the above observation was made in the early sixties), the present condition of roads is deplorable.

6.4.2 For example, statistics on roads for the period 1965 to 1972 indicate that even though, in total, lengths of both surfaced and unsurfaced roads have gone up by approximately 47% (1965-66: base), the proportion of surfaced roads in total roads has actually gone down from 44.6% to 41.8%.

In conjunction with statistics on India's area (3.288 million sq. kms.) and population (586 million in 1974), the following indicators emerge (for road lengths as on 31.3.1972):

(a) Per 100 sq.km. of area, India provides 34.33 km. of roads of all kinds, but only 14.36 of surfaced roads. (The corresponding figures for Ceylon, and underdeveloped country are 64.39 and 58.37 respectively; and for Spain, a semi-industrialised country, 27.60, since Spain has no unsurfaced roads).

(b) Per lakh of population, India provides 192.7 km. of roads of all kinds, but only 80.5 km. of surfaced roads. (The corresponding figures for Ceylon are 324.3 and 294 respectively; and for Spain is 404).

6.4 In the course of this chapter we have underlined the importance of roads in the national development effort and emphasised the need to improve road conditions (so that operating costs would be reduced). However, the above statistics do not indicate any such realization on the part of the Government. Even though road transport industry has been contributing over fifteen hundred crores as revenue to the exchequer, the expenses on roads are only around Rs. 350 crores.

An analysis of statistics on revenue from the road transport industry and the expenditure on roads is revealing. We find that the expenditure as a percentage of revenue fell from 67.3% in 1959-60 to 27.1% in 1974-75, a clear indication of resource diversion to other sectors of investment. In absolute terms, the increase in revenues was over eight-folds (from Rs. 135 crores in 1959-60 to Rs. 1,238 crores in 1974-75) while the expenditure on roads increased only five-folds (from Rs. 90 crores in 1959-60 to Rs. 335 crores in 1974-75).

6.5 Road Development and the Railways

6.5.1 As indicated above, the State has to make a conscious choice on the allocation of resources between the different modes of transport. In the past such emphasis has been directed towards the railways, as against roads. (The growth of waterways and the airline sector is subject to many other considerations and a discussion on this is beyond the scope of this study.) As against rail transport, it is significant that roads and road transport ensured decentralized development all along the route and not concentrated development at terminal points.

6.5.2 This is because any linear extension of transport tends to polarise rather than diffuse economic development. "By its linear extension of transport, a rail-road tends to cheapen the long-distance movement of goods, and this permits the development of cities and complex industrial centres at the extremities of any railway exis. The products of such cities or industrial centres will, to a large extent, be sold in country villages, but the village will gain from the process of industrialization only to the extent that the prices of village imports will fall. But owing to the income inelasticity of demand for food and other farm products, and to "administered prices" of most village imports, the normal consequence of the city-village trade is for the terms of trade to move against the village." (4) In view of this it is imperative that development be diffused and not polarised. Road transport is ideal for such a process because development can take place throughout the area covered by roads. In contrast, development along rail-lines takes place only at discontinuous points (i.e. stations where the train stops).

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4. Source: Perspective report on "Market Towns and Spatial Development in India", National Council of Applied Economic Research, New Delhi, 1972, p. 3.

6.5.3 Resource allocation statistics clearly indicate that in comparison to the revenues generated by the two modes of transport, the expenditures on railway and roads are highly disproportionate. This is highlighted in Exhibit 6.2.

6.5.4 While road transport brings in approximately five times as much revenue to the exchequer as the railways, public investment on roads is less than half that on railways. It is vital that this approach to resource allocation be changed and road and rail transport treated as complementary and not competitive.

Exhibit 4.1: Table 1

STATEWISE SPECIFIC TAX RATES ON OPERATIONS

STATE/UNION TERRITORY	MOTOR VEHICLES TAX PER ANNUM		GOODS TAX PER ANNUM	PASSENGER TAX PER ANNUM
	GOODS VEHICLES	PASSENGER VEHICLES		
	(Rs.)	(Rs.)	(Rs.)	(Rs.)
1. Andhra Pradesh				
2. Arunachal Pradesh				
3. Assam				
4. Bengal	3745	2490	NIL	N.A.
5. Bihar	N.A.	N.A.	20% of freight or 3,000/-	25% on fares
6. Goa	2790	1715	5% on freight or 450/-	10% on fares or 8,100/
7. Gujarat				
8. Himachal Pradesh				
9. Haryana				
10. Jammu & Kashmir	N.A.	N.A.	N.A.	N.A.
11. Kerala	5000	15,360	Goods tax and Passenger tax merged with Motor Vehicles Tax with effect from 1.10.1978	
12. Karnataka				
13. Madhya Pradesh	2978	N.A.	10% of minimum freight or*	25% of fare inclusive of tax or a composition fee
14. Maharashtra	4130 (for general limits)	3300 (for general limits)	1350	17.5% of fare for mofussil areas
15. Manipur				
16. Nagaland	2400	2000	N.A.	N.A.
17. Orissa				
18. Punjab	N.A.	N.A.	1050	35% of fare
19. Rajasthan	2670	2750 (55 per seat)	1470 plus Surcharge @ 10% Rs. 147	30% of value of fare (on pucca roads) 5% Surcharge
20. Sikkim	N.A.	N.A.	NIL	NIL
21. Tamil Nadu	5000	32160	NIL	N.A.
22. Tripura				
23. Uttar Pradesh				
(a) Chandigarh	1000	3000	300	35% of fare
(b) Dadra Nagar Haveli	1550	-	NIL	NIL
(c) Delhi	N.A.	N.A.	N.A.	N.A.

NOTE: For goods vehicles RLW of 15500 kgs been assumed

For passenger vehicles a seating capacity of 50 with 17 standees is assumed.

Composition Fee,

* according to the formula $\frac{RLW - ULW}{55}$ per month

Where RLW : Registered Laden Weight

ULW : Unladen in Kgs.

Source: Replies sent by State Governments/Union Territories to questionnaires sent by the Indirect Taxation Enquiry Committee.

Exhibit 4.1 : Table 2

STATEWISE COLLECTIONS OF SPECIFIC TAXES

(Rupees in Lakhs)

STATE / UNION TERRITORY	MOTOR VEHICLE TAXES				GOODS TAXES				PASSENGER TAX				MOTOR VEHICLE FEES			
	'72-73	'73-74	'74-75	'75-76	'72-73	'73-74	'74-75	'75-76	'72-73	'73-74	'74-75	'75-76	'72-73	'73-74	'74-75	'75-76
1. Andhra Pradesh																
2. Arunachal Pradesh																
3. Assam																
4. Bengal	627.85	623.17	765.00	-									243.71	270.62	174.09	
5. Bihar	-	525.00	531.00	875.00	-	344.00	391.00	413.00	Break-up between Goods taxes and Passenger taxes not available.				-	60.00	68.00	97.00
6. Goa	-	41.26	62.82	84.96	-	-	-	37.98	-do-				-	3.02	3.68	3.83
7. Gujarat																
8. Himachal Pradesh																
9. Haryana																
10. Jammu & Kashmir*	-	102.46	103.33	105.22	-	395.98	441.03	634.38		-				-		
11. Kerala	-	574.82	624.14	806.29	- (Discontinued w.e.f. 1.10.1975)	-	60.24	44.66	-	-	208.52	184.63	-	59.54	61.55	45.42
12. Karnataka																
13. Madhya Pradesh	-	484.75	559.09	643.81	-	298.67	314.02	370.76	-	626.95	762.23	978.68	-	59.72	79.41	117.16
14. Maharashtra	-	1877.15	1970.13	2217.69	-	429.77	532.95	580.99	-	1581.63	1956.07	2455.74	-	89.13	78.47	100.90
15. Manipur																
16. Nagaland	-	10.18	9.96	11.23												
17. Orissa																
18. Punjab	-	-	-	-	-	1117.34	1360.48	1580.90	Break-up between Goods tax and Passenger tax not available.				-	-	-	-
19. Rajasthan	-	555.65	610.27	654.38	-	639.00	818.73	990.82	-do-							
20. Sikkim	-	Average collection 8.16														
21. Tamil Nadu																
22. Tripura																
23. Uttar Pradesh																
(a) Chandigarh	-	5.50	6.17	8.71	-	10.76	12.74	14.64	Break-up between Goods tax and Passenger tax not available.							
(b) Dadra Nagar Haveli	-	0.74	0.76	0.86	--	nil	--		--	nil	--		-	-	0.02	0.03
(c) Delhi	-	283.60	309.66	340.97									-	47.97	46.39	46.09

*J & K has got only basic tolls (on vehicles) and additional tolls (on goods) in lieu of Motor Vehicle Tax and Goods tax. The figures give are such toll collections.

Source : Replies sent by State Governments/Union Territories to questionnaires sent by the Indirect Taxation Enquiry Committee.

Exhibit 4.2 : Table 1

SALES TAX RATES IN DIFFERENT STATES

STATE/ UNION TERRITORY	COMMERCIAL VEHICLES	PASSENGER CARS	TYRES & TUBES	HIGH SPEED DIESEL	PETROL	LUBRICANTS	BATTERY	SPARES
1. Andhra Pradesh	12.25 of Turnover							
2. Arunachal Pradesh								
3. Assam	12%							
4. Bengal	12% + SC 2% + Addl. SC 3 or 8%	7%	10% + SC 2% + ASC 3 or 8%	13%	10%	6% + SC 2% + ASC 3 or 8%	15% + SC 2% + ASC 3 or 8%	15% + SC 2% + ASC 3 or 8%
5. Bihar	12% + 1% on Turnover	7%	N.A.	15%	7%	7%	N.A.	N.A.
6. Goa	12%	6%	4% or 12%	12%	12%	6%	12%	12%
7. Gujarat	12% + 6% on ST							
8. Himachal Pradesh	10%							
9. Haryana	10% + 2% on ST							
10. Jammu & Kashmir	10% + 5% on ST							
11. Kerala	15%							
12. Karnataka	15%							
13. Madhya Pradesh	9%	7%	11%	9%	10%	8%	11%	11%
14. Maharashtra	12%	12%	12%	9%	12%	5%	12%	12%
15. Manipur	12%							
16. Nagaland	11%	6%	11%	7 paise/litre	8paise/litre	Grease 10p/litre Others 9p/litre	11%	11%
17. Orissa	12%							
18. Punjab	10% + 2% on ST	10%	10%	6%	6%	6%	10%	10%
19. Rajasthan	10%	10%	10%	12.5%	15%	N.A.	10%	10%
20. Sikkim	5%	5%	5%	10 paise/litre	15 paise/litre	5%	5%	5%
21. Tamil Nadu	15% + 5% on ST							
22. Tripura	7%							
23. Uttar Pradesh	9% + 1% on Turnover							
(a) Chandigarh	10%	10%	10%	6%	6%	6%	10%	10%
(b) Dadra Nagar Haveli	----------	No Sales Tax Levied In This Territory					----------	
(c) Delhi	10%	10%	10%	7%	7%	7%	10%	10%

Source : Replies sent by State Governments/Union Territories to questionnaires sent by the Indirect Taxation Enquiry Committee.

Exhibit 4.2 : Table 2

STATEWISE SALES TAX COLLECTIONS

(Rupees in Lakhs)

STATE/ UNION TERRITORY	ALL MOTOR VEHICLES			MOTOR VEHICLE PARTS						FUEL						LUBRICANTS		
				TYRES & TUBES			OTHERS			PETROL			DIESEL					
	'73-74	'74-75	'75-76	'73-74	'74-75	'75-76	'73-74	'74-75	'75-76	'73-74	'74-75	'75-76	'73-74	'74-75	'75-76	'73-74	'74-75	'75-76
1. Andhra Pradesh																		
2. Arunachal Pradesh																		
3. Assam																		
4. Bengal	207.36	307.12	251.03	Revenue from tyres included in others.			245.95	380.70	509.44	1261.00	1106.00	1277.00*	Only total revenue from fuel available.			92.00	105.46	127.53
5. Bihar	N.A.	N.A.	N.A.	- do -			46.15	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
6. Goa	40.74	73.06	65.86	- do -			30.46	47.61	38.72	N.A.	N.A.	N.A.	47.51	64.82	60.10	3.44	5.61	5.81
7. Gujarat																		
8. Himachal Pradesh																		
9. Haryana																		
10. Jammu & Kashmir																		
11. Kerala																		
12. Karnataka																		
13. Madhya Pradesh	160.31	165.10	263.00	Revenue from tyres not available separately.			233.21	305.73	259.94	362.34	448.48	587.46	Includes revenue from all petroleum products.			N.A.	N.A.	N.A.
14. Maharashtra	745.00	819.00	901.00	- d o -			890.00	979.00	1077.00	738.00	1036.00	1074.00	515.00	741.00	923.00	113.00	124.00	137.00
15. Manipur																		
16. Nagaland	8.49	4.14	6.53	Revenue from tyres not available separately.			5.88	13.27	3.43	5.91	5.71	5.71	Only total revenue from fuel available.			0.45	0.41	0.47
17. Orissa																		
18. Punjab	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
19. Rajasthan	N.A.	N.A.	N.A.	Revenue from tyres not available separately.			73.98*	N.A.	N.A.	79.75*	N.A.	N.A.	113.05*	N.A.	N.A.	N.A.	N.A.	N.A.
20. Sikkim	N.A.	N.A.	N.A.	- d o -			0.31	0.80	0.86	0.64	1.01	1.46	0.14	0.16	0.32	N.A.	N.A.	N.A.
21. Tamil Nadu																		
22. Tripura																		
23. Uttar Pradesh																		
(a) Chandigarh	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	10.00*	Tax collected under Motor Spirit Taxation Act.						N.A.	N.A.	* 0.25
(b) Dadra Nagar Haveli	---------- No Sales Tax Levied In This Territory ----------																	
(c) Delhi Delhi Act	N.A.	N.A.	N.A.	Revenue from tyres not separately available.			330.25	367.10	421.86	413.92	658.58	809.11	Including revenue from all petroleum products.			N.A.	N.A.	N.A.
C S T							141.26	201.02	238.61	79.00	107.27	160.90						

* Estimates

* Includes revenue from aviation fuel.

Source : Replies sent by State Governments/Union Territories to questionnaires sent by the Indirect Taxation Enquiry Committee.

Exhibit 4.3 : Table 1

SUMMARY OF OPERATIONS AND REVENUE

				GOODS TRANSPORT		PASSENGER TRANSPORT UNDER-TAKING (MOFUSSIL OPERATIONS)
				SMALL OPERATOR	FLEET OPERATOR	
		(A) COSTS PER KILOMETRE				
1.	(i)	Variable cost	Paise	98.99	98.76	130.39
	(ii)	Tax Content in varibale cost	"	32.38	33.03	63.29
	(iii)	Percentage of tax content on variable cost excluding such taxes		48.61%	50.25%	94.32%
2.	(i)	Fixed cost	Paise	26.34	41.61	59.01
	(ii)	Tax content in fixed cost	"	8.84	10.60	4.13
	(iii)	Percentage of tax content on fixed cost excluding such taxes		50.51%	34.18%	7.53%
3.	(i)	Total costs	Paise	125.33	140.37	189.40
	(ii)	Tax content	"	41.22	43.63	67.42
	(iii)	Percentage of tax content on costs excluding such taxes		49.01%	45.10%	55.27%

Contd.....

Exhibit 4.3 : Table 1 (contd)

SUMMARY OF OPERATIONS AND REVENUE

				GOODS TRANSPORT		PASSENGER TRANSPORT UNDER-TAKING (MOFUSSIL OPERATIONS)
				SMALL OPERATOR	FLEET OPERATOR	
		(B) COSTS PER TONNE KILOMETRE/PASSENGER KILOMETRE				
4.	(i)	Variable cost	Paise	11.00	10.97	3.72
	(ii)	Fixed cost	"	2.93	4.62	1.69
	(iii)	Total cost	"	13.93	15.69	5.41
	(iv)	Tax content in total cost	"	4.58	4.85	1.93
		(C) REVENUE & BREAK-EVEN POINT				
5.	(i)	Contribution per tonne kilometre/ passenger kilometre	Paise	3.00	4.03	2.28
	(ii)	Break-even point in tonne kilometre/ passenger kilometres		10,53,333	10,32,506	20,70,175
	(iii)	Level of activity as per assumptions (tonne kms/passenger kms)		10,80,000	9,00,000	28,00,000
	(iv)	Profit/Loss per annum on the basis of 5 (iii)	Rupees	(+) 800	(-) 5,340	(+) 16,640
		(D) TAXES PER VEHICLE GENERATED PER ANNUM				
6.	(i)	Variable	Rupees	38,854	33,039	50,634
	(ii)	Fixed	"	10,600	10,600	3,300
	(iii)	Total	"	49,454	43,639	53,934

Exhibit 4.3 : Table 2

VARIABLE EXPENSES : SMALL OPERATOR

DESCRIPTION	ANNUAL CONSUMPTION QUANTITY	ANNUAL CONSUMPTION AMOUNT Rs.	EXCISE DUTY Rs.	CUSTOMS DUTY Rs.	SALES TAX Rs.	BUILT* TAXES Rs.	TOTAL INDIRECT TAXES Rs.	PER KILOMETRE COST Paise	PER KILOMETRE INDIRECT TAXES Paise
Depreciation	-	17,700	Proportionate tax element in vehicle is not considered					14.75	
Diesel @ 1.37/Lit.	30000 Lts	41,100	15,128	-	3,394	-	18,522	34.25	15.44
Lubricants - Oil	430 Lts	4,300	683	-	205	-	888	3.58	0.74
- Grease	50 Kgs	600	95	-	29	-	124	0.50	0.10
Tyres & Tubes @ Rs.2,137	14 Nos	29,918	9,478	-	3,206	600	13,284	24.93	11.07
Batteries @ Rs.1,375	-	916	122	-	98	82	302	0.76	0.25
Other Spares									
- Indigenous	-	9,720	789	-	1,041	846	2,676	8.10	2.23
- Imported	-	1,080	-	482	116	-	598	0.90	0.50
Servicing & Repair Charges	-	5,000	-	-	-	-	-	4.17	-
Driver & Cleaner Bhatta	-	6,000	-	-	-	-	-	5.00	-
Octroi Transit Fees	-	1,560	-	-	-	-	1,560	1.30	1.30

Contd.....

Exhibit 4.3.: Table 2 (Contd.)

VARIABLE EXPENSES : SMALL OPERATOR

DESCRIPTION	ANNUAL CONSUMPTION QUANTITY	ANNUAL CONSUMPTION AMOUNT Rs.	EXCISE DUTY Rs.	CUSTOMS DUTY Rs.	SALES TAX Rs.	BUILT* TAXES Rs.	TOTAL INDIRECT TAXES Rs.	PER KILOMETRE COST Paise	PER KILOMETRE INDIRECT TAXES Paise
Miscellaneous Fees (Estimated @ Rs.25 per month)	-	300	-	-	-	-	300	0.25	0.25
Fine paid for violation of traffic offences	-	600	-	-	-	-	600	0.50	0.50
Total Variable Cost		1,18,794	26,295	482	8,089	1,528	38,854	98.99	32.38

Note: * These are built-in taxes included in the ex-works price of the products.

Exhibit 4.3 : Table 3

VARIABLE EXPENSES : FLEET OPERATORS

DESCRIPTION	ANNUAL CONSUMPTION QUANTITY	ANNUAL CONSUMPTION AMOUNT Rs.	EXCISE DUTY Rs.	CUSTOMS DUTY Rs.	SALES TAX Rs.	BUILT* TAXES Rs.	TOTAL INDIRECT TAXES Rs.	PER KILOMETRE COST Paise	PER KILOMETRE INDIRECT TAXES Paise
Depreciation	-	14,750	Proportionate tax element in vehicle is not considered.					14.75	-
Diesel @ 1.37/Lit.	25000 Lts.	34,250	12,606	-	2,828	-	15,434	34.25	15.43
Lubricants - Oil	375 Lts.	3,750	595	-	179	-	774	3.75	0.77
- Grease	40 Kgs.	480	76	-	23	-	99	0.48	0.10
Tyres & Tubes @ Rs.2,137	12 Nos.	25,644	8,124	-	2,748	516	11,388	25.64	11.39
Batteries @ Rs. 1,375	-	688	91	-	74	68	233	0.69	0.23
Other Spares									
- Indigenous	-	8,640	701	-	926	752	2,379	8.64	2.38
- Imported	-	960	-	429	103	-	532	0.96	0.53
Servicing & Repair Charges	-	5,000	-	-	-	-	-	5.00	-
Driver & Cleaner Bhatta	-	2,400	-	-	-	-	-	2.40	-
Octroi Transit Fees	-	1,300	-	-	-	-	1,300	1.30	1.30
Miscellaneous Fees (Estimated @ Rs.25 per month)	-	300	-	-	-	-	300	0.30	0.30
Fine paid for violation of traffic offences	-	600	-	-	-	-	600	0.60	0.60
Total Variable Cost		98,762	22,193	429	6,881	1,336	33,039	98.76	33.03

Note : *These are built-in taxes included in the ex-works price of the products.

Exhibit 4.3 : Table 4

VARIABLE EXPENSES : STATE TRANSPORT UNDERTAKINGS

DESCRIPTION	ANNUAL CONSUMPTION QUANTITY	ANNUAL CONSUMPTION AMOUNT Rs.	EXCISE DUTY Rs.	CUSTOMS DUTY Rs.	SALES TAX Rs.	BUILT* TAXES Rs.	TOTAL INDIRECT TAXES Rs.	PER KILOMETRE COST Paise	PER KILOMETRE INDIRECT TAXES Paise
Depreciation	-	16,000	-	-	-	-	-	20.00	-
Diesel	16000 Lts	21,920	8,068	-	1,809	-	9,877	27.40	12.35
Lubricants	-	4,000	635	-	190	-	825	5.00	1.03
Tyres	4 Nos.	8,544	2,707	-	915	172	3,794	10.68	4.74
Battery	-	688	91	-	74	62	227	0.86	0.28
Spares - Indigenous	-	8,640	701	-	926	752	2,379	10.80	2.97
- Imported	-	960	-	429	103	-	532	1.20	0.67
Repairs	-	10,560	-	-	-	-	-	13.20	-
Passenger tax	-	33,000	-	-	-	-	33,000	41.25	41.25
Total Variable Cost		1,04,312	12,202	429	4,017	986	50,634	130.39	63.29

Note : *These are built-in taxes included in the ex-works price of the products.

Exhibit 4.3 : Table 5

ASSUMPTIONS IN THE COMPUTATION OF COST OF OPERATIONS

			GOODS TRANSPORT		PASSENGER TRANSPORT UNDER-TAKINGS (MOFUSSIL OPERATIONS)
			SMALL OPERATOR	FLEET OPERATOR	
1.	Number of kilometres run annually		1,20,000	1,00,000	80,000
2.	Number of kilometres per litre of diesel		4	4	5
3.	Consumption per annum				---
	(i) Lubricants - Oil	(Lts.)	430	375	340
	- Grease	(Kgs.)	50	40	60
	(ii) Number of Tyres		14	12	4
	(iii) Equivalent Battery		0.67	0.50	0.50
	(iv) Indigenous Spare Parts	(Rs.)	9,720.00	8,640.00	8,640.00
	(v) Imported Spare Parts	(Rs.)	1,080.00	960.00	960.00
	(vi) Repairs & Servicing	(Rs.)	5,000.00	5,000.00	10,560.00
4.	Costs per kilometre				
	(i) Driver/Cleaner Bhatta	(Paise)	5.00	2.40	-
	(ii) Octroi Transit Fees	(Paise)	1.30	1.30	-
	(iii) Miscellaneous Fees	(Paise)	0.25	0.30	-
	(iv) Fine paid for violation of offences	(Paise)	0.50	0.60	-
	(v) Depreciation	(Paise)	14.75	14.75	20.00
5.	Standing Charges per annum				
	(i) Interest on capital	(Rs.)	15,750.00	15,750.00	16,000.00

Exhibit 4.3 : Table 5 (Contd.)

ASSUMPTIONS IN THE COMPUTATION OF COST OF OPERATIONS

			GOODS TRANSPORT		PASSENGER TRANSPORT UNDER-TAKINGS (MOFUSSIL OPERATIONS)
			SMALL OPERATOR	FLEET OPERATOR	
(ii)	Motor vehicles tax	(Rs.)	4,130.00	4,130.00	3,300.00
(iii)	Goods tax (composition Fee)	(Rs.)	1,170.00	1,170.00	-
(iv)	Municipal wheel tax	(Rs.)	300.00	300.00	-
(v)	Permit fees	(Rs.)	5,000.00	5,000.00	-
(vi)	Passenger tax	(Rs.)	-	-	33,000.00
(vii)	Establishment & Other Charges	(Rs.)	3,750.00	13,760.00	26,000.00
(viii)	Insurance	(Rs.)	1,500.00	1,500.00	1,900.00
6.	Permitted Tonnage	(Tonnes)	9	9	N.A.
7.	Average passenger occupancy	(Nos)	N.A.	N.A.	35
8.	Fare per passenger Km.	(Paise)	N.A.	N.A.	6.00
9.	Freight earning per tonne kilometre	(Paise)	14.00	15.00	N.A.
10.	Rates of Sales Tax		As applicable for the Maharashtra State		
11.	Excise duty on diesel, lubricants, tyres and tubes, and batteries		Rates of Central Excise Duty applicable as on 31.5.1977		
12.	Excise duty on other spares		At an average rate of 10% on indigenous consumption		
13.	Customs duty on spares	.....	100% ad valorem		.....
14.	Built-in-taxes —				
	(i) Tyres and Tubes	.....	Rs.43 per tyre and tube		.....
	(ii) Batteries	.....	@ 9%		.....
	(iii) Other Spares	.....	@ 8.7%		.....

Annexure 1 : Table 1

TAX INCIDENCE (NOTIONAL) ON VEHICLES: TELCO TRUCK

(Figures in rupees)

	BOMBAY	CALCUTTA	DELHI	MADRAS
1. Ex-works price excldg. taxes	65,209	65,209	65,209	65,209
2. Built-in taxes	14,935	14,935	14,935	14,935
3. Excise Duty	10,220	10,220	10,220	10,220
4. Central Sales Tax	3,615	3,615	3,615	3,615
5. Freight-tax on diesel	205	33	149	182
6. Freight & insurance (excldg. tax element)	3,163	1,538	2,405	2,585
7. Octroi Duty	3,894	955	483	NIL
8. Dealer Margin	2,300	2,300	2,300	2,300
9. State Sales Tax	12,425	13,061	9,932	15,600
10. Additional Sales Tax (not passed on)	745	-	-	-
11. Price to Customer	1,15,966	1,11,866	1,09,248	1,14,646
12. Total Tax Content	46,039	42,819	39,334	44,552
13. Tax Exclusive Customer Price	69,927	69,047	69,914	70,094
14. % of (12) upon (13)	65.8%	62.0%	56.3%	63.6%

Annexure 1 : Table 2

TAX INCIDENCE (NOTIONAL) ON VEHICLES: PREMIER PADMINI

(Figures in rupees)

	BOMBAY	CALCUTTA	DELHI	MADRAS
1. Ex-works price excldg. taxes	18,900	18,900	18,900	18,900
2. Built-in taxes	3,175	3,175	3,175	3,175
3. Excise Duty	3,863	3,863	3,863	3,863
4. Central Sales Tax	1,038	1,038	1,038	1,038
5. Freight-tax on petrol	-	450	350	350
6. Freight & insurance (excldg. tax element)	84	1,522	816	684
7. Octroi Duty	1,082	868	130	NIL
8. Dealer Margin	1,250	1,250	1,250	1,250
9. State Sales Tax	3,527	2,175	2,952	2,151
10. Additional Sales Tax (not passed on)	212	-	-	-
11. Price to Customer	32,919	33,241	32,474	31,411
12. Total Tax Content	12,897	11,569	11,508	10,577
13. Tax Exclusive Customer Price	20,022	21,672	20,966	20,834
14. % of (12) upon (13)	64.4%	53.4%	54.9%	50.8%

Annexure 2

RECOMMENDED MODEL OF MOTOR VEHICLE FEES

S.No.	DESCRIPTION	FEE (Rupees)
1.	Learner's Driving Licence	5
2.	Driving Teste i.e., tests for competence: /For all or any test(s) in III Schedule/	10
3.	Driver's Licence :	
	(i) For Transport Vehicles (with badge)	15
	(ii) For others	10
4.	Conductor's Licence (with badge)	10
5.	Vehicle Registration :	
	(A) Permanent	
	(i) Motor Cycle or Invalid Carriage	10
	(ii) Light Motor Vehicle	15
	(iii) Others	30
	(B) Temporary	5
6.	Certificate of Fitness (and for renewals thereof) including Inspection Fee	15
7.	Application for Permits, Countersignatures etc., (and for renewals thereof) - temporary or otherwise	10
8.	Public Service Vehicle Badge	10
9.	Trade Certificate	10 (per annum)

contd.

Annexure 2 - (contd.)

RECOMMENDED MODEL OF MOTOR VEHICLE FEES

S.NO.	DESCRIPTION	FEE (Rupees)
10.	Tourist Vehicle Permit	30
11.	Transfer of Ownership (Vehicle or Permit)	5
12.	Endorsement of Hire Purchase (for entry, cancellation or upon transfer)	5
13.	Agents and Canvassers' Licence :	
	(i) Under Section 66A(1)(i)	10
	(ii) Under Section 66A (1)(ii) (for each establishment)	75
14.	Appeals under the 'Act'	5
15.	Issue of duplicates (certificates, licences, badges etc.)	5 (for each)
16.	Copies of documents etc.	2 (per copy)

NOTE: The rationalised structure given above excludes the testing charges payable for technical evaluation of fare meters, trailer design, producer gas plant etc., which require the incurrence of technical costs apart from administrative costs.

Annexure 3 : Table 1

COMMERCIAL VEHICLES : VEHICLE AGE DISTRIBUTION

	PRODUCTION YEAR	BUSES	TRUCKS
A.	IN PEAK OPERATIONS		
	1976	14,721	23,835
	1975	12,251	24,467
	1974	10,836	24,998
	1973	9,185	24,315
	1972	9,225	21,020
	1971	11,478	22,819
		67,696	1,41,454
B.	MODERATE OPERATIONS		
	1970	10,162	23,786
	1969	8,992	20,361
	1968	9,185	20,670
	1967	7,296	19,561
		35,635	84,378
C.	MARGINAL OPERATIONS*		
	1966	3,000	26,365
	1965	2,500	27,916
	1964	2,000	23,966
		7,500	78,247
	TOTAL VEHICLES PRODUCED (A) + (B) + (C)	1,10,831	3,04,079
	Less: Cannibalised Vehicles (estimated for rounding off)	10,831	4,079
	VEHICLES ON ROAD	1,00,000	3,00,000

NOTE : (*) These are estimates.

Annexure 3 : Table 2

COMMERCIAL VEHICLES : CONSUMPTION OF TYRES

PRODUCTION YEARS	BUSES			TRUCKS		
	TYRE USAGE	NO. OF VEHICLES	NO. OF TYRES	TYRE USAGE	NO. OF VEHICLES	NO. OF TYRES
1973-76	4	47,000	1,48,000	12	97,500	11,80,000
1971-72	3	20,500	61,500	10	43,750	4,37,500
1970	2	10,000	20,000	8	23,750	1,90,000
1967-69	1	22,000	22,000	5	60,500	3,02,500
1964-66	1	500	500	2	74,500	1,49,000
TOTAL	-	1,00,000	2,52,000 OR 2,50,000	-	3,00,000	22,59,000 OR 22,50,000

Average Annual Tyre Consumption :

(1) Buses : 2.5 tyres

(2) Trucks : 7.5 tyres

Annexure 3 : Table 3

COMMERCIAL VEHICLES : CONSUMPTION OF DIESEL

PRODUCTION YEARS	BUSES			TRUCKS		
	ANNUAL RUN (KMS.)	NO. OF VEHICLES	DIESEL* CONSUMPTION	ANNUAL RUN (KMS)	NO. OF VEHICLES	DIESEL* CONSUMPTION
1973-76	1,00,000	47,000	9.40	1,20,000	97,500	29,25
1971-72	80,000	20,500	3.28	1,00,000	43,750	10.94
1970	70,000	10,000	1.40	80,000	23,750	4.75
1967-69	60,000	22,000	2.64	60,000	60,500	9.07
1964-66	40,000	500	0.04	50,000	74,500	9.31
TOTAL	-	1,00,000	16.76	-	3,00,000	63.32

Average Annual Diesel Consumption :

(1) Buses : 16,750 litres

(2) Trucks : 21,100 litres.

* Diesel consumption in lakh kilo litres.

Annexure 3 : Table 4

COMMERCIAL VEHICLES : AVERAGE ANNUAL TAXES GENERATED

(Figures in Rupees)

DESCRIPTION	PER BUS	PER TRUCK
Diesel	11,000	13,850
Lubricants	1,000	1,000
Tyres & Tubes	1,500	6,200
Batteries & Other Spare Parts :	4,100	4,200
Motor Vehicle Tax, Passenger or Goods Tax, Permit Fees, Wheel Tax, etc.	23,300	10,550
	40,900	35,800

Exhibit 6.2

(i) Public Investments on Roads and Railways

Type of Transport Expenditure	First Plan (1951-56)	Second Plan (1956-61)	Third Plan (1961-66)	3 Annual Plans (1966-69)	Fourth Plan (1969-74)	Fifth Plan (1974-79)	Total
			(Rupees In Crores)				
Railways	260	814	1326	526	1050	2202	6178
Roads	131	234	440	308	871	902	2886
Expenditure on Roads as % of expenditure on railways	50,38%	28.75%	33.18%	58.56%	82.95%	40.96%	46.71%

Source : Government of India: Five Year Plan and Annual Plan Reports.

(ii) Contribution to Exchequer by Road and Rail Transport Industry.

Year	Rail Transport	Road Transport	Railway's Contribution as a Percentage of Road Transport's Contribution
1970-71	133.64	683.00	19.57%
1971-72	157.25	813.00	19.34%
1972-73	184.23	947.00	19.45%
1973-74	196.63	1113.00	17.67%
1974-75	230.89	1238.00	18.65%

Source : 1. Indian Railways; ANNUAL REPORT AND ACCOUNTS.

2. Demand for Grants for Expenditure of the Central Government on Railways.

3. Indian Roads and Transport Development Association. (Data obtained from State/Central Revenue Budgets.)

APPENDIX - 14

INDIRECT TAXATION OF IRON AND STEEL AND ITS IMPACT

1. Excise taxation of iron and steel had its beginning in 1934, when a duty of Rs. 4 per tonne was levied on steel ingots as a revenue measure. This rate was revised to Rs. 40 per tonne in the year 1957 following TEC's observations about the low incidence of duty on them. Subsequently, in 1960, excise duty on pig iron was introduced with a view to imposing effectively a duty on uses of pig iron in processes other than making steel ingots. In the same year tin plates and tinned sheets were brought under excise levy purely as a revenue measure. Finally, in 1962 semi-finished as well as other iron and steel products were brought under excise. During this period as well as subsequently, increases were made in effective rates. In December, 1971, a regulatory duty was imposed on all the iron and steel items, except pig iron, with a view to bridging the gap between the higher priced imported steel and cheaper indigenous supplies. This duty was later replaced in March, 1973 by an auxiliary duty, the quantum of which was also increased in the year 1974 on revenue considerations as the gap between international and indigenous prices had widened. Details of the evolution of the tariff on steel ingots, pig iron (iron in crude form), tin plate and tinned sheets and iron or steel products are brought out briefly in Statements 1 to 4 attached to this appendix.

EVOLUTION OF TAX STRUCTURE

2. A notable feature of the evolution of the tariff relating to the iron and steel group of items is that rates of duty have mostly been specific (still they are). Further, even though excise levies on the iron and steel group is a three-point levy-pig iron, ingot and rolled products - duties paid at earlier stages are usually given credit for or set off, against duty payable on the products arising at the second and third stages. Moreover, through exemptions, preferential treatment has been extended to mini-steel plants and rerollers and lower or 'nil' duties have been prescribed for products made out of old scrap etc.

3. Import duties relating to iron and steel products, which were largely specific in nature and widely varying in incidence, attained uniformity and stability with the all-round rationalisation of customs tariff brought about in the year 1965. The general effective rate of duty on prime steel was then fixed at 40% ad valorem. Differential rates were, however, applied in respect of specified products, e.g. the duty on stainless steel sheets and plates was fixed at 100% ad valorem. Since then, the rates of duty on stainless steel products have been varied from time to time. Prior to the Budget for 1977-78, the rates on stainless steel varied from 120% to 320% ad valorem . Similarly, alloy and special steels were subject to a duty of 75% ad valorem until the 1977-78 Budget. At present, the rates of import duty including auxiliary duty on the iron and steel group are:—

(a)	general rate	-35% ad valorem
(b)	alloy steel and high carbon steel	-40% ad valorem

(c)	stainless steel		
	(i) sheets	]	Varying from 40% to 220% ad valorem depending upon the thickness of the materials.
	(ii) plates & strips	]	

In addition these products attract countervailing duty at the rates prescribed under excise tariff.

4. For the purpose of sales tax, iron and steel products, being among the essential raw materials entering into the very wide wariety of products, have been regarded as goods of special importance. With the enactment of the CST Act, in 1956, iron and steel came to be placed in the list of "declared goods" on which sales tax is chargeable at a ceiling rate and at only one stage when the sales are made within a State. The present ceiling rate applicable on iron and steel is 4% ad valorem which is also the rate of CST on inter-State sales.

IMPORTS AND INDIGENOUS PRODUCTION OF IRON AND STEEL

5. The requirements of iron and steel in the country are now mostly met by indigenous production. Imports have been gradually on the decline as indigenous production has increased and in net terms, the country has emerged as an exporter of iron and steel. The products which are imported are by and large special categories of steel whose production is insufficient or has not yet been developed within the country. The principal items of import are alloy steel and stainless steel, electrical steel sheets, cold rolled coils, and sheets as well as plates. The imports of steel items for the last three years by broad categories are indicated in Statement 5 attached to this appendix.

6. The growth in the indigenous production of mild steel has indeed been substantial since 1971-72. From about 4.9 million tonnes the production of saleable steel has risen to 7.6 million tonnes during 1971-72 to 1976-77, the capacity utilisation of main plants having increased from 65% to 84% and 66% to 92% for ingots and saleable steel, respectively. During the same period, the production of mini-steel plants also registered an increase but in terms of utilisation of capacity (about 30% presently) the performance of this sector is far from satisfactory. Details of production of mild steel materials during this period are given in Statement 6 attached to this appendix. The performance of the alloy and special steel sector, which came into being in a real sense only during the sixties when plants with specialised facilities to manufacture alloy and special steels were set up, has also been good over the last 5/6 years, though the country is still dependent on imports for special categories of tool and high carbon steel as well as stainless steel. At present, the total licensed capacity for finished alloy and special steel including electrical steel sheets is 3.68 million tonnes. The capacity utilisation in this sector for the year 1976-77 was of the order of 70%.

TRENDS IN CONSUMPTION OF MILD STEEL

7. Though the production of mild steel has been buoyant, the demand for it has not been growing proportionately, with the result, it is reported that stocks of some categories of mild steel piling up. The slackening of the growth in consumption of steel is mainly attributable to a slowing down of the pace of investment in the economy and lower outlays in the railways and the construction sector.

8. Turning to the consumption pattern of mild steel, a broad idea can be obtained from Statements 7 and 8 attached to this appendix from two different perspectives and for two different periods, 1971-72 and 1975-76. The 1971-72 study reveals that the major users of mild steel materials in that year were :—

(a) basic industries such as manufacture of metal products, heavy engineering goods and mining

(b) rail road industry

(c) building industry

(d) fastener industry

(e) transport industry

(f) miscellaneous engineering goods

Substantial quantities (about 28% of the total) were also sold to trade whose exact breakdown is not available though it is believed that the major portion of it would have gone to private construction and small scale manufacturers. The 1975-76 study which is restricted to the domestic sales of main producers by major customer groups (whose categorisation is somewhat different from the study for 1971-72) reveals that the major consumers of mild steel during 1975-76 were:—

(a) steel and coal industry
(b) defence
(c) electricity boards/power stations
(d) railway wagon building industry
(e) government departments (including public works department)
(f) rerollers
(g) tubes manufacturers
(h) wire drawing industry
(i) foundry industry
(j) miscellaneous engineering goods

Here again, about 27% of the offtake has gone through trade channels the classification of which into different end uses is not available. Both the studies, however, reveal that a substantial quantity of mild steel is consumed by sectors which are not taxed further under excise. From the latter study, it can also be estimated that consumption of steel in the public sector would be about 27% to 30% of the total off-take from the main steel plants.

PRICES AND EXCISE DUTY INCIDENCE

9. Since 1964, the prices of mild steel products emanating from main steel plants are fixed by the Joint Plant Committee (JPC) with the Iron & Steel Controller as its Chairman. These include apart from net realisation to the plants (i.e. ex-factory price)- the elements of excise duty equalised freight, contribution to JPC, JPC Engineering Goods Export Assistance Fund and Rerollers Freight Differential Fund etc. While the prices of various categories have been changed several times since 1964, a major change in the pricing policy came into force with effect from 15th October, 1973, when, to ensure

supply of steel to meet bulk of the priority needs of Government departments, and units in the public sector at fairly low prices, the prices of plates, structurals and railway materials were kept at the level prevailing before 15.10.1973 while the prices of other categories were revised upwards with a view to mopping up the surplus profits at various points. Changes made thereafter in JPC prices, have been mainly on account of factors like increase in excise duties, railway freight and increase in the price of coal. A point worth taking note of is that revisions made since 1971 in excise tax rates have not been in accord with changes in the pricing policy. Thus, we find that the increase in excise duty, in the case of joists, and bars/rods was of the order of Rs. 142.50, Rs. 101.25 per tonne while the price increase in their case has been Rs. 812 and Rs. 408 per tonne. More such examples may be had from Statement 9 attached to this appendix.

10. As at present, the prices for various products vary from about Rs. 1000 to Rs. 3500 per tonne as may be seen from Table 1 below:—

TABLE 1

JPC PRICES OF SELECTED MILD STEEL PRODUCTS

S. No.	Category	JPC (Base Price) (in Rs. per tonne)
1.	2	3
1.	Bars and rods 6 mm	2002
2.	Bars and Rods 10 mm	1752
3.	Joists 125 x 70 mm	1448
4.	Channels 125 x 65 mm	1377
5.	Angles 100 x 6 mm	1377
6.	Mild Steel Plates 6 mm	1523
7.	Hot rolled sheets 24 G	2497
8.	Cold Rolled Sheets	2772
9.	Galvanised plain sheets - 24 G	3332
10.	Light rails - 30 lbs	1126
11.	Heavy rails - 90 lbs	1006
12.	Sleepers (pressed)	1136
13.	Wheels - Diesel/electric loco	3473
14.	Skelp	2056

11. If we convert the specific duties into ad valorem incidence based on current JPC prices, the following position as in Table 2 emerges :

TABLE- 2

AD VALOREM INCIDENCE OF SOME MILD STEEL PRODUCTS

S. No.	Description of Iron and Steel products	Total duty incidence as percentage of price
1	2	3
1.	Plates	29.8
2.	Joists	30.6
3.	Billets	26.4
4.	Blooms	29.3
5.	Bars & rods in straight lengths	
	(i) upto 25 mm	23.2
	(ii) upto 60 mm	24.1
	(iii) above 60 mm	30.0
6.	Flats	
	(i) upto 5 mm thickness	32.0
	(ii) upto 10 mm thickness	23.3
	(iii) above 10 mm thickness	21.6
7.	Skelp	36.7
8.	Galvanised sheets/coils	
	(i) 16/22 G	40.1
	(ii) 24 G and thinner	33.4
9.	Hot rolled sheets	24.4 (average)
10.	Cold rolled sheets	31.9 (average)
11.	Railway materials	
	(i) crossing sleeper bars	14.6
	(ii) light rails (15 kg.)	15.5
	(iii) Heavy rails (52 kg.)	16.7

significantly enough, it is found that there is appreciable variation in ad valorem incidence as between different products due mainly to the specific rate structure.

12. The prices of alloy and special steels on the other hand are not governed by any control and are in general much higher than mild steel prices. The average per tonne price inclusive of excise duty ranges from Rs.4000/- to as high as Rs.60,000/- as may be seen from Table 3 below:-

TABLE 3

APPROXIMATE AVERAGE PRICES OF SOME ALLOY/ SPECIAL STEELS

S. No.	Category	Approximate average price (including excise duty) (Rs. per tonne)
1	2	3
1.	Carbon constructional steels	4000
2.	Alloy constructional steels	5000 to 12000
3.	Rolled alloy steel rounds	15000
4.	Rolled high speed steel bars	60000
5.	Forged constructional steels	5000 to 8000
6.	Forged die steels and tool steels	15000
7.	Carbon tool steels	8000
8.	Stainless steel sheets/plates	50000 to 60000

13. In the case of alloy and special steels also the variation in the incidence of duty from product to product is quite significant, though, in general, incidence in ad valorem terms is low compared to that of mild steel materials since the prices of these items are far higher and the same specific rates apply. Thus, the ad valorem incidence on stainless steel plates is as low as 0.6% while that on carbon constructional steel is as high as 10%.

14. As regards imported steel items the approximate total incidence of import and countervailing duties works out as shown in Table 4 below:—

TABLE 4

INCIDENCE OF IMPORT AND COUNTERVAILING DUTIES ON SELECTED IMPORTED ITEMS

S. No.	Description of item	As % of CIF Price		
		Import duty (Basic + aux.)	Countervailing duty (Avg.) in ad valorem terms	Incidence
1	2	3	4	5
1.	Mild steel			
	(a) Plates	35	25	60
	(b) Cold rolled sheets	35	27	62
2.	Alloy and special steel sections	40	15	55
3.	Stainless steel sheets			
	(a) Utensil grade	220	5	225
	(b) Industrial uses	45	5	50
4.	Stainless steel strips			
	(a) Utensil grade	220	4	224
	(b) Industrial uses	45	6	51

15. Three major points need to be taken note of arising out of the foregoing discussion on incidence. Firstly, there is considerable divergence in the ad valorem incidence on different product groups and on different categories within the same group (e.g., finished steel items). Secondly, when seen in conjunction with the consumption pattern it appears that some categories used predominantly in further industrial production (e.g., skelp) bear higher duty incidence than products used in non-taxed or less taxed sectors (e.g., structurals). Thirdly, even in the case of essential imports of steel items, particularly those used for machine building, the cumulative duty incidence on imports is as high as 50% to 60% of the imported price.

16. In terms of import on end user industries the studies conducted on the basis of data on consumption of mild steel by major customer groups as related to home sales of main producers (who account for a total revenue of about Rs. 167 crores) show that the total excise tax burden is shared by the different sectors/groups in the manner indicated below:—

IMPACT OF EXCISE AND CUSTOMS DUTIES ON MILD STEEL ON END-USER INDUSTRIES

S. No.	Sector/Group	Tax borne appros. Rs. lakhs	% of total
1.	Public sector	4010	27.6
2.	Industry (direct consumption)	6240	43.3
3.	Trade/house building etc.	4202	29.1
	Total :	14452	100.0

It is further seen that within the public sector, the major burden is borne by organisations engaged in the building up of infrastructure. Thus, along with the tax burden borne by the residuary category, whose break up could not be obtained, it transpires that on an overall basis, 30 - 35% excise duty on mild steel is borne by sectors not taxed further under excise. Our studies, details of which appear in Statement 10 attached to this appendix are confined to mild steel products primarily because they account for the greater part of revenue and because pig iron and ingots do not have significant direct application in other activities.

17. To assess the impact of excise and customs duties on steel on different end-products, we conducted a selective study, the results of which are tabulated in Statement 11 attached to this appendix. It shows that the impact of customs and excise duties on steel items is particularly significant in the case of passenger cars, trucks, air conditioning machinery, electric motors and steel furniture each of which are subject to excise levies at rates which are moderate to high.

18. Excise duties on tin plates and tinned sheets have a significant effect on prices of containers used for packing essential commodities and processed foods. Thus the customs duty on tin plate and excise on containers constitutes about 44% of the basic price of a tin container used for packing 1 kg. of Baby Food. In the case of vanaspati (4 kg.) the cumulative levy on containers amounts to nearly 3% of the price of vanaspati while in the case of canned pineapple slices - (450 gms) the cumulative levy on containers is about 8% of the price of the canned product.

19. From the point of view of revenue, the iron and steel group has emerged as one of the major contributors to total excise collections. The yield of excise revenues from the iron and steel group as a whole, since the year 1972-73 is given in the Table 5 below:—

REVENUE TRENDS

TABLE 5

EXCISE REVENUES OF IRON AND STEEL ITEMS

Year	Iron in crude form	Steel ingots	Iron or steel products	Tin plate & tinned sheets (Rs. crores)
	(Rs.)	(Rs.)	(Rs.)	(Rs.)
1972-73	5.62	5.53	148.16	4.04
1973-74	6.02	11.40	155.84	3.15
1974-75	10.07	12.41	205.85	2.98
1975-76	9.20	12.94	228.27	3.64
1976-77	9.00	9.00	254.00	3.50

Source : Explanatory memoranda to the Budget

20. The yearwise customs revenues from imports of iron and steel since 1972-73 are as in Table 6 below:

TABLE 6

CUSTOMS REVENUES FROM IRON & STEEL ITEMS

Year	Customs Revenues (Rs. crores)
1972-73	122.94
1973-74	138.60
1974-75	211.18
1975-76	154.25
1976-77 (RBE)	162.00
1977-78 (SBE)	142.77

(Source : Explanatory memoranda to the Budgets)

STATEMENT - 1

EVOLUTION OF EXCISE RATE STRUCTURE IN RESPECT OF STEEL INGOTS

(T.I. 26)

S. No.	Effective from	Steel ingots	Steel ingots in the manufacture of which duty-paid iron in any crude form is used.	Steel ingots manufactured with the aid of electric furnace.
			(Rate : Rs. per ton)	
1.	1934	4	4	4
2.	16-5-1957	40	40	40
			(Rate : Rs. per metric tonne)	
3.	1-3-1960	40	30	40
4.	1-10-1960	39.35	29.35	39.35 (Nil w.e.f. 24/4/62)
5.	1-3-1964	50	20	Duty on steel ingots less duty paid on fresh unused steel scrap.
6.	28-2-1965	60	30	-do-
7.	20-8-1965	75	35	-do-
8.	30-3-1968	75	Duty on steel ingots less duty paid on iron in any crude form	-do- (Nil w.e.f. 1-3-1969)
9.	13-12-1971	75+37.5 (regulatory duty) = 112.5	-do-	Nil
10.	17-3-1972	100+50 (regulatory duty) = 150	-do-	Nil
11.	1-3-1973	100+75 (auxiliary duty) = 175	-do-	50 + 37.5 (auxiliary) = 87.5 duty) 100 + 75 (auxiliary = 175 duty) w.e.f. 1-3-1974

S. No.	Effective from	Steel ingots	Steel ingots in the manufacture of which duty-paid iron in any crude form is used.	Steel ingots manufactured with the aid of electric furnace.
			(Rate : Rs. per ton)	
12.	1-8-1974	100+100 (auxiliary duty) = 200	Duty on steel ingots less duty paid on iron in any crude form	100+100 (auxiliary duty) = 200
13.	9-12-1975	No change	-do-	25+25 = 50 (auxiliary duty) = 50
14.	18-6-1977	330	-do-	180

Note:- 1. The tariff description of the item was enlarged w.e.f. 1-3-1964 to include steel melting scrap also.

2. In respect of ordnance factories producing steel ingots for supply to Central Government, there has been full exemption from excise duty since 1956.

STATEMENT - 2

EVOLUTION OF EXCISE TARIFF IN RESPECT OF IRON IN ANY CRUDE FORM
(including pig iron, molten iron)

(T.I. 25)

S. No.	Effective from	Effective rate (Rs. per tonne)	Rationale for levy/change in rates etc.
1.	1.3.1960	10	The intention behind the levy was to effectively impose a duty on pig iron going into uses other than making steel ingots.
2.	1.3.1964	30	The tariff description of the item was revised and the rate raised as a sequel to abolition of surcharge on iron and steel.
3.	20.8.1965	40	Duty rate raised as a revenue measure.
4.	1.3.1974	50	Duty rate raised as a rationalisation measure which incidentally was to yield additional revenue.
5.	1.8.74	70	Duty rate increased as a revenue raising measure.

Note:- 1. From 1.3.60 to 28.2.64, the levy was restricted to pig iron. Thereafter the tariff description was revised thus:—

Iron in any crude form including pig iron, scrap iron, molten iron or iron cast in any other shape or size.

STATEMENT - 3

EVOLUTION OF EXCISE TARIFF ON TIN PLATE AND TINNED SHEETS (T.I. 28)

S. No.	Effective from	Effective rate of duty (Rs. per M.T.)	Rationale for levy/change
1.	1.3.1960	200	Duty levied as a revenue measure.
2.	1.3.1963	200 (inclusive of Special Excise @ 10% of basic)	Special excise @ 10% of basic levied as a revenue measure intended mainly to meet defence expenditure.
3.	28.2.1965	Plates: 255 (basic) + 25.50 (Special); Sheets: 255 (basic) + 22.50 (Special). (Rate conditional upon use of excise/c.v. duty paid plate/sheet under T.I. 26AA).	Duty increased to correspond with the increase in the rates of duty on other flat products of general consumption.
4.	1.3.1970	400	Duty rationalised in order to remove the anomaly of the indigenous tin plate paying a higher cumulative duty than the additional duty borne by imported tin plates.
5.	13.12.1971	400 (Basic) + 200 (Regulatory)	Regulatory duty imposed to bridge the gap between the prices of imported and indigenous products.
6.	17.3.1972	520 (Basic) + 208 (Regulatory)	Duty raised to further bridge the gap between the prices of imported and indigenous products.
7.	1.3.1973	520 (Basic) + 260 (Auxiliary)	Auxiliary duty imposed in lieu of regulatory duty and at a higher rate to bring about a further reduction between imported and indigenous prices.
8.	1.8.1974	520 (Basic) + 364 (Auxiliary)	Auxiliary duty raised to 70% of basic duty as a revenue measure.

Statement 4

EFFECTIVE RATES OF EXCISE DUTY ON CERTAIN IRON AND STEEL PRODUCTS SINCE 28-2-1965

(Duty shewn as .Rs. per tonne and includes basic + regulatory duty)

S.No.	Description	24-4-62	10-5-62	1-3-64	28.2.65	20-8-65	13-12-71	17-3-72	1-3-73	Current from 1-8-74
1.	Semi finished steel including blooms, billets, slabs, sheets, bars, tin bars and hoc bars.	5% ad. val.	69.35	90.00	105.00	125.00	187.50	243.75	288.75	330.00
	Bars, rods, coils, wires, joists, girders, angles, channels, tees, beams, zeds, through piling and all other rolled, forged or extruded shapes and sections except rails and sleepherbars.	5% ad. val.	69.35 (bars & roads, zeds etc.) 79.35	90.00	105.00	125.00	187.50	243.75	288.75	330.00
3.	Uncoated plates.	7½ adv.	91.85	110.00	120.00	135.00	202.50	263.25	306.25	350.00
4.	Plates and Sheets, Hoops and Strips excepted uncoated plates and galvanised plates and sheets									
	(i) Cold rolled	7½ adv.	91.85	110.00	120.00	250.00	375.00	287.50	568.75	650.00
	(ii) Others.	7½ adv.	91.85	110.00	120.00	275.00	262.50	341.25	393.75	450.00
5.	Galvanised plates/ sheets.	7½ adv.	99.85	200.00	300.00	325.50	487.50	633.75	743.75	850.00
6.	Skelp.	7½ adv.	91.85	150.00	200.00	250.00	375.00	487.50	487.50	562.50
7.	Cold Rolled strips.	7½ adv.	99.35	110.00	200.00	250.00	375.00	487.50	568.75	650.00
8.	Hot rolled strips.	7½ adv.	99.35	110.00	200.00	175.00	262.50	341.25	393.75	450.00
9.	Seamlessspipes and tubes	5% adv.	110.00	110.00	120.00	135.00	202.50	263.25	306.25	350.00
10.	Steel Castings	5% adv.	50.00	50.00	60.00	75.00	112.50	146.25	175.00	200.00
11.	Rails & Sleepers bars	5% adv.	50.00	50.00	60.00	75.00	97.50	146.25	175.00	175.00

NOTE:-

(1) The above duties include ingot stage duty except in the case of the rate as on 24-4-1962. Where ingot stage duty is already paid, set off in respect of the same is given against product duty.

(2) Increase in duties w.e.f. 13-12-71 were on account of imposition of regulatory duty at 50% of basic duty as a measure of bridge the gap between international and indigenous prices.

(3) Increase in duties w.e.f. 17-3-72 were on account of increase in basic duties effected as a revenue measure.

(4) With effect from 1-3-73 regulatory duty was replaced by an auxiliary duty and an increase was effected in the rate simultaneously.

(5) With effect from 1-8-74, the rates of auxiliary duty were further increased.

STATEMENT 5

CATEGORY-WISE IMPORTS OF IRON AND STEEL

(QUANTITY - IN 000 TONNES AND VALUE Rs. Crores)

S. No.	Category	1974-75		1975-76		1976-77	
		Qty.	Value	Qty.	Value	Qty.	Value
1.	Sponge Iron etc.	0.7	0.19	0.5	0.25	0.5	0.26
2.	Mild Steel	876.6	251.48	355.3	125.35	246.0	80.96
3.	High Carban Steel	159.5	49.06	66.2	28.52	30.2	13.77
4.	Alloy Steel	80.1	61.83	51.8	43.81	39.0	34.65
5.	Railway materials	16.7	5.92	6.6	4.85	5.5	3.06
6.	Iron & Steel Scrap	10.5	2.13	17.6	3.29	35.1	6.37
7.	Total iron & Steel	1144.1	370.61	498.0	206.07	356.3	139.07

(Source:- Monthly Bulletin of Statistics - Deptt. of Steel & Mines)

STATEMENT 6

Production : Steel materials

PRODUCTS	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77
A MAIN PRODUCERS SALEABLE SEMIS:						
Billets/Squares	745	793	706	904	1271	1407
Blooms	138	106.3	88.5	83	139	434
Slabs	23	24.3	19.5	35	213	
Others	125	135	148.5	128.3	140	132
Total	1031	1058.6	962.5	1150.3	1763	1973
B. FINISHED STEEL (SALEABLE):						
(a) Rounds/Flats	751	714	870	776	692	750
Wire Rods	298	406	380	372	392	473
Structurals	678	811	540	715	819	838
Plates	287	320	303	344	447	706
HR Coils	120	198	171	198	322	659
Skelp	233	244	194	246	264	282
B P Sheets	220	194	170	204	242	248
Cold Rolled Sheets	103	104	95	92	98	91
Cold Rolled Coils	50	56	87	98	104	186
G. P. Sheets	58	70	71	75	62	114
G C Sheets	108	93	88	81	111	74

PRODUCTS		1971-72	1972-73	1973-74	1974-75	1975-76	1976-77
	Electrical Sheets	44	48	39	51	50	44
	Tin Plates	40	45	35	30	48	54
	Others	11	7	10	45	55	43
	Total (a)	3001	3310	3053	3327	3706	4562
	RAILWAY MATERIALS :						
(b)	Hy. Rails	370	322	252	243	201	306
	Light Rails	6	4	10	12	14	15
	Sleepers	56	45	37	50	61	41
	Wheel & Axles	32	30	22	33	37	37
	Fish Plates	4	5	4	4	2	1
	Others	17	12	15	12	3	-
	Total (b):	485	418	340	354	318	400
	TOTAL FINISHED STEEL : (a) + (b)	3486	3728	3393	3681	4024	4884
	TOTAL SALEABLE STEEL (A + B) Main producers	4517	4787	4356	4831	5787	6857
C.	Production of Mini Steel Plants	370	450	600	700	400	750
	GRAND TOTAL SALEABLE STEEL (A+B+C)	4887	5237	4956	5531	6187	7607

(Source : Hindustan Steel Ltd.)

SECTIONWISE AND CATEGORYWISE SUPPLY STRUCTURE OF IRON AND STEEL INDUSTRY OF INDIA
(BASED ON JPC DATA : 1971-72)

Statement 7

(Despatches in tonnes)

SECTORS	Pig Iron	Semi	Plates	Sheets	Strips	Skelp	Angles	Channels	Joist	Rounds	Flats	Squares	Tor steel	Rails	Others	Total
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1. Basic Ind.	203,697	642,098	3,727	3,876	53,324	194,254	4,860	2,059	1,708	19,813	6,600	18,452	473	12,125	2,989	1,170,055
2. Container Ind.	-	-	3,63[illegible]	20,818	12,065	46	1,249	191	206	69	158	23	68	-	-	38,533
3. Fitting Ind.	362	10,095	506	2,291	938	2,537	124	-	306	132,196	1,189	2,445	-	-	-	152,989
4. Handtools Ind.	2,557	56	1,022	2,203	742	159	-	-		156	22	-	-	-	-	6,917
5. Agri. Machinery	66,859	805	2,461	13,184	99	1,140	1,849	226	633	6,641	1,315	794	-	339	110	96,455
6. Mining Machinery	612	299	2,745	1,365	-	-	1,092	935	337	484	178	29	1,185	1,465	-	10,726
7. Industrial Machinery	25,931	2,590	5,606	4,147	-	-	974	895	679	3,443	68	-	1,093	40	15	45,481
8. Commercial Machinery	5,092	-	148	2,054	85	-	22	-	-	375	21	-	-	-	-	7,797
9. Elec. Machinery	9,017	110	1,545	3,971	559	-	987	504	1,595	7,761	94	-	134	450	-	26,727
10. Comm. Equp.	2,175	-	1,107	1,245	5,305	-	21,987	4,068	1,292	3,885	153	-	1,579	7,195	20	50,001
11. Machinery Comp	23,801	250	5,070	5,451	1,312	-	1,227	1,150	557	8,195	150	66	-	48	318	47,595
12. Boilers	276	-	3,269	1,603	672	-	840	2,434	1,454	1,352	257	-	247	-	44	12,448
13. Rail Road	75,134	49,584	31,728	40,421	19,204	-	12,517	15,291	2,897	18,367	10,130	1,322	1,834	83,011	60,401	422,341
14. Ship Bldg.	631	74	10,308	814	-	-	1,271	1,475	451	2,208	215	-	2,352	-	24	19,823
15. Motor Vehl.	2,746	21	3,925	15,096	3,257	811	1,122	746	203	5,597	393	262	-	50	-	34,229
16. Air Crafts	-	-	163	44	-	-	24	-	-	182	-	-	339	-	-	752
17. Misc Manuf.	16,469	15,452	11,808	32,621	11,335	8,086	13,447	4,431	3,525	59,373	2,622	2,114	1,408	1,754	106,451	290,896
18. Transport Constn.&Main)	23	-	7,926	1,127	174		7,376	3,969	3,378	32,124	217	77	6,121	74,736	2,292	139,540
19. Building	8,070	660	0,144	20,106	1,547	237	37,618	21,463	18,456	90,194	4,277	290	22,053	5,248	8,446	298,791
20. Irrigation	2,943	23	5,399	2,618	273	-	2,826	2,433	1,468	39,108	656	2,223	8,487	2,154	4,451	75,062
21. T.P. Plants	-	-	4,596	1,767	328	53	3,527	1,683	3,206	9,405	602	-	4,951	285	53	30,456
22. H.E. Projects	-	-	845	1,349	-	-	2,350	3,324	4,112	11,019	391	-	4,995	460	758	29,603
23. Def. Prod.	1,463	5,124	3,508	13,511	-	-	4,995	1,887	596	16,643	491	262	5,933	-	-	54,413
24. Export (HSL)	218,100	-	-	800	-	-	16,000	46,300	26,400	500	-	-	-	65,800	-	373,900
25. Resale	131,992	28,760	50,645	136,305	5,291	12,214	36,973	15,771	18,077	168,485	17,143	12,867	17,227	6,619	1,798	660,167
26. Not Specf.	2,101	2,952	14,414	23,625	1,257	-	52,753	29,951	69,906	11,723	4,763	437	31,437	14,005	2,753	382,077
Unclassified	53,995	85,592	12,607	26,744	5,356	6,911	11,108	8,700	11,186	30,937	2,497	2,934	2,852	3,891	24,483	294,792
TOTAL ::	854,046	844,545	248,860	379,156	123,123	226,448	239,118	169,889	172,602	750,235	54,602	45,097	114,767	334,675	215,406	4,772,566

Note: (i) The above data is in respect of mild steel items only.
(ii) Basic industries include metal products, heavy engineering and mining industry.

(Source : Hindustan Steel Ltd.)

STATEMENT 8

MAIN PRODUCERS: CONSUMPTION OF IRON & STEEL - 1975-76 (In '000 M/T)

(By Major Customer-Groups)

Sl. No.	G R O U P	Pig Iron	Semis	Railway Materials	Structurals	Bars & Rods	Plates	Sheets	Skelp/ HR Strips	Total
1.	Steel & Coal	69.1	109.1	14.2	49.3	42.7	48.2	15.4	2.9	350.9
2.	Defence	2.6	1.1	1.2	23.8	42.3	20.0	23.3	0.5	114.8
3.	SEB/Power	0.3	0.3	8.3	110.4	63.7	27.8	3.6	0.5	214.9
4.	Other Govt.Deptt.	1.0	-	2.2	14.7	60.4	7.3	6.8	0.2	92.6
5.	Rly. wagon Bldrs.	18.9	7.7	117.3	36.5	26.8	24.6	33.8	14.3	279.9
6.	Ports/Shipyard	0.2	-	1.0	2.6	4.6	8.3	4.8	0.3	21.8
7.	P & T	1.7	-	0.3	1.5	3.3	0.2	-	5.0	12.0
8.	P W. D.	0.5	-	0.6	14.0	95.5	6.7	6.8	0.7	124.8
9.	Major Public	22.2	0.3	1.5	17.6	3.9	20.0	7.3	0.6	73.4
10.	Bright Bar	1.2	4.9	0.1	0.4	16.2	0.6	1.2	-	24.6
11.	Elect. Mfrs.	5.0	-	-	0.8	0.6	1.1	14.9	-	22.4
12.	Re-rollers	14.7	346.4	19.3	2.4	70.8	2.3	8.3	1.9	466.1
13.	Tubes Mfrs	5.3	2.1	-	0.5	48.2	2.3	6.4	291.8	356.6
14.	Wire Drawing	6.0	21.5	0.4	1.1	86.7	1.4	9.9	0.5	126.5
15.	Cement/Oil/Textile	5.1	-	2.6	18.8	16.0	15.9	5.4	1.2	65.2
16.	Basic Metal	0.2	7.8	0.5	5.4	0.9	4.1	3.2	-	22.1
17.	Main Fabricators	8.1	1.4	1.4	22.4	6.9	10.7	6.5	4.0	61.4
18.	Auto Mfrs.	1.8	-	0.2	2.2	3.0	5.8	8.1	1.9	23.0
19.	Furniture Makers	0.2	-	-	0.4	0.3	2.2	12.0	0.6	15.7
20.	Drum & Barrel	0.5	-	-	1.0	1.0	2.2	22.2	0.0	27.5
21.	Fastner Industries	0.6	5.9	0.1	0.2	5.9	0.1	0.8	1.1	14.7
22.	Multipurpose	71.2	68.8	9.5	24.4	21.3	22.7	28.7	14.8	261.4
23.	Foundry	271.5	7.5	1.8	3.1	2.0	1.8	3.3	0.4	291.4
24.	House Builders	0.6	-	0.1	1.8	10.0	0.3	2.2	-	15.0
25.	Corporate Bodies	0.5	2.7	1.1	9.9	24.8	8.0	3.9	0.4	51.3
26.	SSIC/Agro Indus.	161.2	-	0.6	54.3	14.0	6.0	31.9	2.0	270.0
27.	Miscellaneous	-	-	-	0.2	2.9	0.1	0.7	-	3.9
28.	Trade	97.2	115.9	17.7	133.7	145.6	47.8	156.0	25.2	739.3
29.	Unclassified	91.0	99.0	27.2	71.0	103.9	28.9	61.4	18.0	500.4
	T O T A L :	857.4	802.4	229.4	624.4	923.4	327.4	488.8	389.4	4643.6

NOTE : (i) The above categorisation does not include items like Tin Plates, Pipes, Defectives and Scrap.

Source: SAIL International Ltd.

Statement : 9

EXCISE DUTY CHANGES VIS-A-VIS PRICE CHANGES

S.No.	Description	Price as on 15.12.71	Excise duty as on 15.12.71	Price as on 14.10.73	Excise duty as on 14.10.73	Current prices	Current Excise duty	Increase in prices		Increase in duty	
		A	B	C	D	E	F	E-A	E-C	F-B	(F-D)
1.	Bars and rods	940	187.50	1201	288.75	1752	330.00	812	551	101.25	41.25
2.	Plates*	1160	202.50	1338	341.25	1523	450.00	363	183	247.50	108.75
3.	Billets	878	187.50	1134	288.75	1582	330.00	704	448	142.50	41.25
4.	Skelp	1237	375.00	1425	487.50	2056	552.50	819	631	177.50	65.00
5.	Cold rolled sheets	1552	375.00	1821	568.75	2572	650.00	1020	751	275.00	81.25
6.	Joists*	1040	187.50	1266	288.75	1448	330.00	408	182	142.50	41.25
7.	Galvanised sheets	2029	487.50	2360	743.75	2972	850.00	943	612	362.50	106.25

Note : *The prices of these items were pegged at pre 15.10.73 levels when change in ITC Policy was announced on 15.10.1973.

Statement 10

DISTRIBUTION OF EXCISE TAX BURDEN AS OF 1975-76
(Based on Data on Consumption of iron and mild steel by major consumer groups with reference to domestic sales of the main producers)

S.No.	Consumer groups	Total quantity of iron and steel consumed (000 tonnes)	Approx. excise tax borne (Rs. lakhs)	Excise borne as % of total (%)
(1)	(2)	(3)	(4)	(5)
1.	Steel and coal industry	350.9	1016	7.0
2.	Defence	114.8	424	2.9
3.	Electricity boards/power stations	214.9	717	5.0
4.	Rly, wegon builders	279.9	784	5.4
5.	Ports and shipyard	21.8	66	0.4
6.	Public works deptt.	124.8	426	2.9
7.	Major public undertakings	73.4	214	1.5
8.	Other Govt. deptts.	104.6	359	2.5
9.	Bright bar mfrs.	24.6	81	0.6
10.	Electrical mfrs.	22.4	94	0.7
11.	Rerollers	466.1	1520	10.5
12.	Tubes manufacturers	356.6	1527	10.6
13.	Wire drawing	126.5	427	3.0
14.	Cement/Oil/Textile industries	65.2	215	1.5

Contd..../-

(1)	(2)	(3)	(4)	(5)
15.	Basic metal industries	22.1	79	0.5
16.	Steel fabricators (Main)	61.4	201	1.4
17.	Auto manufacturers	23.0	91	0.7
18.	Furniture manufacturers	15.7	78	0.5
19.	Drum and barrel mfrs.	27.5	139	1.0
20.	Fastener industries	14.7	50	0.3
21.	Foundry	291.4	263	1.8
22.	Miscellaneous engg. industries	261.4	758	0.4
23.	House builders	15.0	56	5.2
24.	Corporate bodies	51.3	177	1.2
25.	Small scale/Agro industries Corp.	270.0	544	3.8
26.	Trade/un-classified	1243.6	4146	28.7
		4643.6	14452	100.0

Note: i) The above study is based on the data for main producers' domestic sales of mild steel materials by major consumer group for the year 1975-76 (of. Table 4 Statement 8).

ii) The items included above account for about 90% of the production of the main producers who together paid about Rs. 166 crs. as excise taxes in 1976-77.

Statement : 11

IMPACT OF CUSTOMS AND EXCISE DUTIES PAID ON STEEL ON SOME SELECTED PRODUCTS

S. No.	Product description	Ex-factory price (unit-number)	Final product excise duty (Adv.)	Input duties paid on steel			Customs and excise duties on steel as % of ex-factory price.
				Customs	Excise	Total	
		Rs.		Rs.	Rs.	Rs.	%
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1.	Textile machinery/Automatic 100 m - 150cm	40,700	2%	-	250.00*	250.00	0.6
2.	Passenger car	21,075	17.5%	917.00	221.00	1138.00	5.4
3.	Truck	80,137	12.5%	3424.00	708.00	4132.00	5.2
4.	Tractor	37,501	10%	372.00	212.00	584.00	1.6
5.	Air conditioning machinery	1,870	100%	68.67	17.58	86.25	4.0
6.	Vertical Pump MF	6,500	26%	-	131.29	131.29	2.0
7.	Elec. Motors SPM-1	400	20%	-	4.76	4.76	1.1
8.	Elec. Motor (QU 100 L4)	779	15%	-	23.59	23.59	3.0
9.	(3 Phase 50 Cycle 10 H.P. 132 M 4 Motor)	1,840	15%	2.93	58.40	61.33	3.3
10.	Steel Furniture (Cabinet)	620	10%	-	62.75	62.75	10.1
11.	Strong Boxes	250	10%	-	12.00	12.00	4.8

* Includes duty on first stage inputs only.

APPENDIX - 15

TAXATION OF NON-FERROUS METALS

EXCISE DUTY STRUCTURE - ALUMINIUM

The excise duty on aluminium was levied, at the rate of Rs. 300/- per tonne, for the first time in the year 1960. Apart from revenue considerations, the high profits being made by the industry and trade due to domestic shortage (which could not be met by substantial imports) influenced the imposition. The duty was later enhanced on a number of occasions, the details of which are given in Statement - I. The important features of these changes are set out below.

2. During the period 1-3-1963 to 16-3-1972, the metal was subject to a special excise at the rate of 20% of the basic excise duty (mainly for raising additional revenue); the specific duties were converted to an ad valorem basis in the 1970-71 Budget. A regulatory duty was imposed during the period 13. 12. 1971 to 28. 2. 1973 to regulate the consumption of aluminium due to the limited domestic production and foreign exchange constraints on imports. This was later converted to an auxiliary duty in the 1973-74 Budget. The duty was not withdrawn when the indigenous production showed substantial improvement later. Because it would have meant loss of revenue. Aluminium ingots and certain specified manufactures (bars, rods, sheets, circles, foils, etc.) were subject to a uniform duty of 40 per cent ad valorem, irrespective of its form or any particular specifications , at the time of presentation of 1975-76 Budget.

3. In the 1975-76 Budget, an additional excise duty at the rate of Rs. 2000/- per tonne was imposed on certain grades of aluminium other than what is usually known as 'Electrical conductor grade' (or EC grade). The heavy additional duty on commercial grade was intended to discourage its production and to stimulate greater production of EC grade aluminium whose indigenous availability had suffered considerably. Later, in the same year, as a part of an integrated policy for the development of aluminium industry, the duty structure was revised with effect from 15th July, 1975. The concept of "levy" and other than "levy" aluminium was introduced. The primary producers were statutorily required to deliver to the processing units, manufacturing conductors and cables at a controlled price under "levy", a fixed proportion of their total production in the form of EC grade aluminium. Retention prices were fixed in respect of the levy metal delivered by the primary producers and this covered the actual costs only. The manufacturers were, however, simultaneously allowed to sell at prices of their own the production which was not required to be delivered under the levy. In other words, the control on prices exercised till then was withdrawn in respect of other than "levy" aluminium. To ensure that the "levy" metal which was much cheaper and intended for priority uses did not get diverted to other uses, simultaneously the excise duty structure was radically changed. The excise duty on "levy" aluminium was increased from 40 per cent to 50 per cent ad valorem plus Rs. 2, 000 per tonne, while the duty on commercial grade aluminium (of 40 per cent ad valorem + Rs. 2, 000 per tonne) which was inclusive of duty at Rs. 2, 000 per tonne imposed for encouraging greater production of EC grade aluminium, was kept unchanged. In order to counteract the impact of the deliberate increase in excise duty on "levy" metal the State Electricity Boards were made eligible for a subsidy at a prescribed rate of Rs, 3, 130 per tonne of "levy" aluminium used for conductors bought by them from conductor manufacturers in which the "levy" aluminium was used. This subsidy, however, was not available to other consumers of the levy aluminium e.g. other cables and wires manufacturers, transformer producers, etc.

4. In the 1976-77 Budget, the duty on non-levy metal was reduced by Rs. 1, 200 per tonne to give relief to the industry as it was facing a demand recession particularly in respect of commercial grade metal. Thus, at present, "levy" ingots are subject to an ad valorem-cum-specific duty of 50 per cent plus Rs. 2, 000 per tonne, whose incidence comes to about 80 per cent ad valorem at the existing controlled prices. Where the subsidy is available, the effective incidence is substantially reduced but is still about 33 per cent ad valorem. The duty imposed on other than "levy" aluminium ingots is 40 per cent plus Rs. 800 per tonne whose incidence comes to about 50 per cent at current ex-factory prices of primary producers.

5. The above duties apply to ingots and manufactures like bars, rods, sheets, plates, circles, pipes and tubes, made out of such ingots - there being a provision to give relief of the duty paid at the ingot stage. In the case of aluminium foils and circles of prescribed thickness used for utensils, however, the rates have been reduced but even then the incidence is higher than 30 per cent.

IMPORTS

6. As for imports, aluminium (in crude form) is chargeable to a 45 per cent customs duty apart from the countervailing duty equivalent to excise duty leviable on indigenous production.

DUTY STRUCTURE - COPPER

7. The excise duty on copper was levied for the first time in the year 1961 when a duty of Rs. 300/- per tonne was imposed on certain manufactures of copper, like plates, and sheets. Copper in crude form was subjected to duty at the rate of Rs. 100/- per tonne in the following year's Budget (1962-63). The duty was revised thereafter on a number of occasions as shown in Statement 2. At present, the excise duty on copper and copper alloys (which contain not less than 50 per cent by weight of copper) is Rs. 5, 600/- per tonne if it is in the form of crude or semis like ingots, blocks, wire rods and wire bars, while in the case of copper manufactures, viz. plates, sheets, circles, strips and foils, it is Rs. 6, 300/- per tonne. Pipes and tubes of copper and copper alloys are assessed to ad valorem duty, the existing rate being 28 per cent. These rates are applicable to products made out of virgin metal. In the case of copper and its manufactures produced from scrap there is no duty on crude or semis, while in the case of plates, sheets , circles, etc. a reduced duty of Rs. 700/- per tonne is applicable.

8. The increases in the excise duties on copper effected from time to time in the sixties were mainly intended to curb the consumption of copper and conserve foreign exchange as the bulk of it was imported. Prior to 1971 the import duty on copper was GATT bound; this fact also influenced Government, while effecting increases in the duties on copper as it was only through higher excise that an additional levy on imports could be made as a countervailing duty. However, no reduction in the excise duty was effected when after release from the GATT binding a basic customs duty of 30 per cent was levied on imported copper in the 1971-72 Budget. Likewise, the regulatory duty of excise levied during the period December, 1971 to February, 1973 to regulate and restrain the consumption of copper, was not withdrawn but converted to an auxiliary duty in the 1973-74 Budget and continued thereafter, even though foreign exchange considerations did not, it would seem, require specific constraints on indigenous consumption. A further substantial

increase in excise duty in the Supplementary Budget of 1974 was made, since at that time, the international prices of copper had gone up steeply and the only indigenous producer of copper, which was also selling its produce at price on par with those of imported copper, was getting a windfall benefit. The additional excise was meant to mop up part of this fortuitous gain. Though international prices later came down substantially the duties were only partly reduced in the 1976-77 Budget. But this relief was more to help the indigenous producer than the consumers.

CUSTOMS DUTY

9. As for customs duty, it was only after GATT release that a basic import duty of 30 per cent was levied on unwrought copper in the 1971-72 Budget, as mentioned above. This duty was stepped up to 40 per cent in the 1973-74 Budget. Though it was raised to the 55 per cent level for sometime as part of the 1976-77 Budget proposals, the duty was brought down to the existing level of 45 per cent (40 per cent basic and 5 per cent auxiliary) plus the countervailing duty as the international prices had shown significant upward movement within a short period after the presentation of the Budget. The total incidence inclusive of the impact of the countervailing duty exceeds 90 per cent of the current c.i.f. prices.

DUTY STRUCTURE
ZINC AND LEAD

10. As in the case of copper, certain manufactures of zinc-plates sheets, circles etc.- were also subjected to excise duty at the rate of Rs. 300/- per tonne in the 1961-62 Budget. The duty on zinc in unwrought form was levied in the Supplementary Budget of 1965. Though there was hardly any indigenous production, the excise was imposed to raise revenue from imported zinc as import duties could not be levied on zinc because it was a GATT bound item assessable at nil rate. The excise duty was in fact continued and even raised further, though zinc was freed from GATT bindings in 1970-71. A regulatory duty was imposed on zinc in December, 1971 as on other non-ferrous metals (aluminium and copper), to curb its indigenous consumption; it was converted to an auxiliary duty and later merged with the basic duty, but was not withdrawn. Again, as in the case of copper, in the case of zinc also, substantial increases in excise duties were effected in August, 1974, to siphon off a part of the fortuitous profits being enjoyed by the indigenous manufacturers due to the high international prices of zinc. The duties have remained at that high level despite the changes in our foreign exchange position and in the international prices thereafter. At present, unwrought zinc attracts a duty of Rs. 2,600/- per tonne, while zinc manufactures like sheets, plates and circles pay a duty of Rs. 3,500/- per tonee.

11. A customs duty of 40 per cent was levied on zinc in the 1971-72 Budget after obtaining its release from GATT binding. The existing customs duties on zinc in unwrought form is the same as for copper, i.e., 45 per cent plus the countervailing duty. The incidence of total import duty inclusive of the countervailing duty effect comes to more than 90 per cent at the current c.i.f. prices.

LEAD AND OTHER
NON FERROUS METALS
DUTY STRUCTURE

12. Lead was subject to an excise duty for the first time in the year 1965 when as a part of the Supplementary Budget proposals a duty of Rs. 500/- per tonne was imposed on unwrought lead. As for unwrought zinc, the imposition of excise on lead was more to raise revenue in the form of countervailing duty on imports than to tax indigenous production. Because of GATT binding no import duties could be levied. However, after the

GATT release in 1970-71, a duty at the rate of 40 per cent was imposed on imported lead in the 1971-72 Budget without changing the excise duty. At present, imported lead attracts a duty of 45 per cent (40 per cent basic plus 5 per cent auxiliary) apart from the countervailing duty of Rs. 500/- per tonne.

13. As for other non-ferrous metals, like tin, nickel and cobalt, there is at present no indigenous production. These metals, when imported, are subject to the customs duty of 45 per cent (40 per cent basic and 5 per cent auxiliary) as other non-ferrous metals are.

14. The Central Government realises more than Rs. 250 crores by way of customs and excise duties from non-ferrous metals as may be seen from the following Table indicating revised estimates for 1976-77:

REVENUE YIELD

TABLE 1 – REVENUE REALISATION FROM NON FERROUS METALS

S. No.	Description	Revenue from indigenous production	Revenue from imports
		1976-77 (RE) Rs. crores	
1.	Aluminium	113.04	3.04
2.	Copper	19.06	43.03
3.	Zinc	7.08	37.08
4.	Lead	0.33	11.03
5.	Other non-ferrous metals		
	(i) Tin	-	11.00
	(ii) Nickel	—	10.02
	Total :	139.51	115.20

Source: Explanatory memorandum on the Budget of the Central Government, for 1977-78.

15. To examine how this substantial tax burden was borne by various sectors of the economy and what impact these duties have on the prices of products of different consuming industries using them as an input, we initiated selective studies. The studies attempted to find out for the important metals, namely, aluminium, copper, zinc, lead, nickel and tin, the broad consumption pattern and then in respect of a selected range of products of the major consuming sectors for each metal, the impact which the existing level of duties had on their prices. We outline in the following paragraphs the results of these studies in respect of each of the non-ferrous metals mentioned above.

16. The total consumption of aluminium in recent years has fluctuated between 1.7 lakh tonnes and 2 lakh tonnes per annum; most of it has been met by indigenous production. The actual production, import and export pattern, in the last five years has been as follows:

ALUMINIUM-
CONSUMPTION PATTERN

TABLE 2 - PRODUCTION , IMPORTS AND EXPORTS PATTERN OF ALUMINIUM SINCE 1971-72.

Year	Production (Tonnes)	Imports (Tonnes)	Exports (Tonnes)
1971-72	1,81,485	21,236	-
1972-73	1,74,777	1,664	-
1973-74	1,40,847	1,605	-
1974-75	1,26,551	2,688	-
1975-76	1,87,276	4,841	11,857
1976-77	2,08,687	Neg.	22,716

Source: Department of Mines, Ministry of Steel and Mines.

17. The Table shows that there was a setback in production during 1972-73 to 1974-75. This was mostly due to power shortage. Considerable improvement in production was achieved in 1975-76 and 1976-77 and in fact certain quantities of aluminium had even to be exported as the pick up in indigenous demand lagged behind the growth in production. The production in 1977-78 is again said to have suffered a setback due to power shortage which may necessitate some imports. However, with the availability of sufficient indigenous capacity, barring unforeseen circumstances, no imports of aluminium should be necessary as a regular feature.

18. To study the detailed consumption pattern and to see if there has been any shift in the actual sales pattern we collected figures of actual sales from primary producers for the years 1971 and 1976. About 75 per cent of production of EC grade aluminium (accounting for about 50 per cent of the total production of the primary producers) is utilised for the manufacture of conductors which are supplied to State Electricity Boards. In respect of these supplies, the subsidy scheme referred to earlier is applicable. The remaining 25 per cent or so of the EC grade metal is used for the manufacture of wires and cables (other than conductors for which State Electricity Boards are subsidized), transformers etc.

CONSUMPTION PATTERN
OF EC GRADE

19. The commercial grade aluminium finds multifarious uses in industries covering household utility articles like utensils, electrical appliances and pressure cookers; transport and automobiles e.g. bus bodies and motor vehicle parts; packaging for various purposes including food and pharmaceuticals; secondary extruders, consumer durables, defence needs, coinage, etc. Statement 3 indicates the consumption pattern according to major consuming sectors, as well as the excise duty burden borne by these sectors on their purchase of aluminium from the primary producers - separately for the years 1971 and 1976. As may be seen from the Statement, utensil manufacturers and bus body builders were the biggest consumers of commercial grade aluminium accounting respectively for 29.3 per cent and 15.8 per cent of total consumption of that commodity in 1976. Canning and packaging, casting alloys as well as secondary extruders also consume a significant part of the total commercial grade aluminium. It is also seen that the share of utensil manufacturers, the packaging industry and the paint industry has declined in 1976 from the level in 1971. The share in total consumption went up for bus body manufacturers, automobiles and motor vehicle parts units, secondary extruders, defence applications and construction.

CONSUMPTION PATTERN OF COMMERCIAL GRADE

20. The above consumption pattern indicates broadly the share of the total duty on aluminium being borne by the major consuming sectors. To have an idea of the actual impact on the prices of the diverse products turned out by the sectors referred to above data were collected from selected representative manufacturers using aluminium as an input. The results obtained are in Statement 4, which also indicates the excise duties at the final product stage, wherever levied. The impact of the existing duties on aluminium varies from industry to industry, being very high in certain sectors, some of which are also the major consumers. For utensils produced from virgin aluminium, the incidence of the input duty itself constitutes on an average 20 per cent of the price of utensils. For an other domestic article like pressure cookers, the input duty effect constitutes on an average 10 per cent of the price. For some domestic electrical appliances the duty on aluminium amounts to a significant addition to costs. In the case of bus-body builders the effect ranges from about 5 per cent (for all steel bodies) to about 18 per cent (for all aluminium bodies) of the value charged for constructing bus-bodies; and it forms about 2 per cent to 6 per cent of the final price of buses (inclusive of chassis and body cost). Its use as a packaging material has substantial impact on the prices of certain drugs; the impact is, however, maximum on the prices of wires and cables - in some cases, the incidence of input duty alone exceeds 50 per cent, the cables paying duty at the product stage separately.

IMPACT ON PRICES

21. Though the indigenous production of copper has gone up in recent years, unlike in respect of aluminium, we still depend on imports to a significant extent to meet our domestic total requirements. At present, the consumption of virgin copper is placed at 55 to 60 thousand tonnes per annum. Out of this, the indigenous production was around 22,400 tonnes in 1976-77, the balance of demand being met by imports. The following Table indicates the consumption pattern of copper since 1971-72 as also the level of indigenous production and imports.

CONSUMPTION PATTERN - COPPER

TABLE 3 - PRODUCTION IMPORTS AND CONSUMPTION PATTERN OF COPPER SINCE 1971-72.

(in tonnes)

Year	Production	Imports	Consumption
1971-72	6500	56200	64400
1972-73	8700	54500	57200
1973-74	8800	52600	59300
1974-75	9900	41800	37800
1975-76	18600	14800	47500
1976-77	22400	40600	54700

Source: Department of Mines, Ministry of Steel and Mines.

Indigenous production has increased in recent years. There was, however, decline in consumption during 1974-75 and 1975-76, which has been attributed to high international prices coupled with high level of import duties and the general recessionary trends in pockets of engineering industry. Consumption of copper has, however, picked up in 1976-77.

22. Copper being a strategic raw material, its use has been regulated under the Copper Control Order which, in fact, prohibits its use for manufacturing conductors. Its use for manufacturing winding wires for armatures, motors, relays, transformers, etc., or for certain other category of cables like telephone cables is permitted. It also finds application in ordnance factories, mints, railways, and general engineering goods and electrical equipment industries, including industrial machinery and machine tools and auto-ancillaries. Copper salts have extensive use in chemical industry, in printing and dyeing of textiles; and alloys of copper, especially brass, are used for manufacturing of utensils and handicrafts. The Table below is indicative of the consumption pattern according to major consuming sectors in the year 1976 as revealed by our study (based upon the sales of the indigenous producer and MMTC):

TABLE 4 - OFFTAKE OF COPPER BY USER INDUSTRIES - 1976

Sl. No.	User Industry	Purchases of virgin copper from HCL & MMTC in 1976	Col. (3) as percentage of total purchases of virgin copper by all user industries
(1)	(2)	(3)	(4)
		(Tonnes)	
1.	Winding wires	20,000	35.6
2.	Cables other than telephone cables	5,125	8.4
3.	Telephone cables	1,500	2.6
4.	Electrical motors, transformers and other electrical equipments	3,621	6.3
5.	Utensils	1,640	2.9
6.	Mint	3,837	6.7
7.	Ordnance Factories	2,749	4.8
8.	Railways	1,367	2.4

(1)	(2)	(3)	(4)
9.	All others	17,248	30.3
	Total	57,087	100.0

Source: Minerals and Metals Trading Corporation and Hindustan Copper Ltd.

The above consumption pattern, however, does not take into account the consumption of scrap-based copper and its manufactures produced by the secondary manufacturers, which is approximately 20,00 tonnes per annum. Most of this copper gets consumed in non-electrical applications - utensils manufacturers claiming the major share.

23. As for the impact on the prices of the products of industries using copper as an input, the Table below gives an indication of the kind of effect on prices, the Central taxes on copper (excise or customs) have on a few selected products of user industries .

TABLE 5 - IMPACT ON PRICES OF PRODUCTS OF USER INDUSTRIES

Sl. No.	Description of the product using copper as an input	Ex-factory price/unit Rs.	Element of duty borne on copper used per unit		Duty borne on copper as % of ex-factory price of the product	Duty borne on the finished product % ad valorem
			Customs Rs.	Excise Rs.		
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1.	4 x 2.5 mm armoured PVC control cable	6700/- per km	1299.00	-	19.4	17.5
2.	Super enamelled winding wires	42/- per kg	12.76	-	30.4	10.0
3.	Welding cable	3600/- per 100 mts	751.96	-	20.9	17.5
4.	7 x 2.5 sq. mm unarmoured cable	8663/- per km	1915.00	-	22.0	17.5
5.	6.3/8 MVA Power distribution transformer	3,73,000.00 per set	-	15120.00	4.1	2.0
6.	Paper covered strips 14 x 2.2 mm	34,300/- per 1000 kg	12062.00	-	35.2	10.0
7.	Electric Motors 40 HP 4 Pole CVTF	18,250/- per set	-	182.70	1.0	10.0
8.	3 Phase Induction Motors 2 HP 1500 RPM-IEFC	788/- per set	19.08	-	2.4	15.0

(1)	(2)	(3)	(4)	(5)	(6)	(7)
9.	Utensil (thal)	44.47 per pc	-	0.84*	1.9	2.0
10.	Utensil (Beda)	128.00 per pc	-	2.87*	2.2	2.0

*Scrap based sheets are used. Therefore, duty element is very low.

Source: Data for representative manufacturers furnished by Collectors of Central Excise.

CONSUMPTION PATTERN-ZINC

24. As in the case of copper, even for zinc, though our production has increased in recent years, we still depend substantially on imports. The following Table gives the consumption pattern, since 1971-72, as also the level of indigenous production and imports.

TABLE 6 - PRODUCTION, IMPORTS AND CONSUMPTION PATTERN OF ZINC SINCE 1971-72

(in tonnes)

Year	Production	Imports	Consumption
1971-72	24,700	69,600	82,600
1972-73	22,700	77,200	97,900
1973-74	20,800	63,400	92,000
1974-75	22,000	66,700	97,400
1975-76	27,000	33,500	64,300
1976-77	26,000	57,500	63,600

Source : Department of Mines, Ministry of Steel and Mines.

As in the case of copper, the consumption of zinc also declined in 1974-75 and 1975-76 for similar reasons.

25. As regards the consumption pattern, the major uses of zinc are for galvanising iron and steel products, in the manufacture of copper and zinc alloys, zinc based alloys for die-castings for automobiles, electrical appliances and other manufacturing industries. In the form of rolled sheets, it is extensively used in the manufacture of dry cell batteries, photo-engraving and lithographic plates, etc. Its other applications include its use in making pigment for rubber, paints,

ceramics and several other materials; as a micro nutrient for plants and for the manufacture of zinc based solders, etc. The following Table indicates the broad consumption pattern during the year 1976 as revealed by our study (based on the sales of indigenous producers and MMTC).

TABLE 7 - OFFTAKE OF ZINC BY USER INDUSTRIES — 1976

Sl. No.	User Industry	Approximate purchase of zinc from indigenous producers & MMTC (Tonnes)	Column 3 as percentage of total purchases of virgin zinc
(1)	(2)	(3)	(4)
1.	Battery manufacturers	22,364	23.5
2.	Steel plants	21,838	23.0
3.	Heavy electrical equipment manufacturers such as transformers, power generators, transmission towers, etc.	6,512	6.9
4.	All others (such as pipes and tubes, alloys and light mechanical industries, etc.)	44,342	46.6
	Total	95,056	100.00

Source: Minerals and Metals Trading Corporation and indigenous primary producers of zinc.

IMPACT ON PRICES

26. As for the impact of the existing duties on zinc on the costs of products of various user industries, the Table below gives an indication of the incidence in respect of a few selected products.

TABLE 8 - IMPACT ON PRICES OF USER INDUSTRIES

Sl. No.	Description of the product using zinc as an input	Ex-factory price/units	Element of duty borne on zinc used per unit		Duty borne on zinc as %age of ex-factory price	Duty borne on finished product
			Customs	Excise		
		Rs.	Rs.	Rs.		
1.	Galvanised sheets (zinc coated)	2345.00 per tonne	-	244.60	10.4	850/- per MT
2.	Dry cell battery	1074.40 1000 pcs	129.95	-	12.1	25% adv.
3.	G.I. Buckets Size 10	138 per doz.	-	11.00	8.0	2% adv.

Source: Data furnished by Collectors of Central Excise for representative manufacturers.

27. In the case of lead, we have had very small production so far and the major part of the total demand has been met by imports. Indigenous production by the only primary producer in 1976-77 was about 6,200 tonnes as compared to the total consumption of about 61,600 tonnes in the same year. (There is also at present production of about 10,000 tonnes by secondary producers). The maximum consumption of lead is in the storage batteries. The other applications include sheathing of cables, especially underground cables as well as telephone cables, paints and varnishes and non-ferrous alloys. The following Table gives a broad indication of its consumption pattern in 1976. This is as per the actual sales effected by MMTC; the details of indigenous manufacturers' sales could not be collected, but the pattern of MMTC sales could be taken as reflecting the total consumption pattern.

CONSUMPTION PATTERN OF LEAD

TABLE 9 - OFFTAKE OF LEAD BY USER INDUSTRIES - 1976

Sl. No.	User Industries	Quantity of lead purchased from MMTC in 1976 Tonnes	Col. 3 as percentage of total purchase of imported metal
(1)	(2)	(3)	(4)
1.	Storage batteries	13,000	34.7
2.	Telephone cables	10,000	26.7
3.	Cables other than telephone cables	4,000	10.7

(1)	(2)	(3)	(4)
4.	Pigment and chemicals	6,000	16.0
5.	Others	4,463	11.9
	Total:	37,463	100.0

Source: Minerals and Metals Trading Corporation.

28. As for the impact of the existing duties on lead, it is not appreciable where indigenous output is used by the consumer industries but the use of imported lead sometimes leads to a significant impact on the costs of consumer industries. The table below gives an indication of this impact for a few selected products.

IMPACT ON PRICES

TABLE 10 - IMPACT ON PRICES OF USER INDUSTRIES

Sl. No.	Description of the product using lead as an input	Ex-factory price/unit	Element of duty borne on lead used per unit		Duty borne on lead as %age of ex-factory price	Duty borne on the finished product
			Customs	Excise		
		Rs.	Rs.	Rs.		
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1.	Storage battery 12V - 13P	426.08 per pc	47.04	-	11.4	17.5% adv.
2.	Storage battery 12V - 19P	619.35 per pc	-	8.51	1.4	17.5% adv.
3.	Power Cable 11 x 3 x 300	218368.27 per km	9145.00	-	4.2	17.5% adv.
4.	Aluminium Conductor Paper Insulated, MIND Impregnated, Lead Sheath Cable	165206.00 per km	12895.00	-	7.8	17.5% adv.

Source: Data for representative manufacturers furnished by Collectors of Central Excise.

29. Apart from aluminium, copper, zinc and lead two other important non-ferrous metals, namely, tin and nickel are also used in the country. The present consumption for each of these metals is about 3,000 tonnes per annum. The entire quantities are imported for want of any indigenous production. The following Tables indicate the consumption pattern (based on MMTC sales in 1976) in respect of tin and nickel:

OTHER NON-FERROUS METALS

TABLE 11 - OFFTAKE OF TIN BY USER INDUSTRIES 1976

Sl. No.	User industry	Purchases from MMTC in 1976	Col. (3) as percentage of total purchases of all industries
(1)	(2)	(3)	(4)
		(Tonnes)	
1.	Tin plates	1200	41.1
2.	Railways	800	27.4
3.	Tin containers	150	5.1
4.	Others	756	26.4
	Total:	2915	100.0

Source: Minerals and Metals Trading Corporation.

TABLE 12 - OFFTAKE OF NICKEL BY USER INDUSTRIES—1976

Sl. No.	User industry	Purchases from MMTC in 1976	Col. (3) as percentage of total purchases of all industries
(1)	(2)	(3)	(4)
		(Tonnes)	
1.	Electroplating	649	24.5

(1)	(2)	(3)	(4)
		(Tonnes)	
2.	Castings	500	18.9
3.	Others including Mints	1500	56.6
	Total:	2649	100.0

Source: Minerals and Metals Trading Corporations.

30. Both tin and nickel are subject to an import duty of 45 per cent like other non-ferrous metals. Even though the quantities imported are relatively small, the value of imports is considerable due to the very high prices which these two metals command in the international market.

STATEMENT - 1

CHANGES IN THE RATES OF EFFECTIVE EXCISE DUTY (BASIC, SPECIAL, REGULATORY, AUXILIARY) LEVIED ON ALUNINIUM IN ANY CRUDE FORM FROM THE DATE OF IMPOSITION TILL 30.11.77

Period	Unit of Assessment	Description of Product	Effective Rate of dDuty				
			Basic	Special	Regulatory	Auxiliary	Total
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1.3.60 to 28.2.63	Rs. per tonne	Aluminium ingots	300	-	-	-	300
1.3.63 to 25. 5.67	-do-	-do-	300	60	-	-	360
26.5.67 to 28.2.70	-do-	-do-	950	190	-	-	1140
1.3.70 to 12,12.71	Advalorem	-do-	25%	5%	-	-	30%
13.12.71 to 16.3.72	-do-	-do-	25%	5%	6¼%	-	36¼%
17.3.72 to 28.2.73	-do-	-do-	30%	-	10%	-	40%
1.3.73 to 28.2.75	-do-	-do-	30%	-	-	10%	40%
1.3.75 to 14.7.75	Advalorem+ Rs. per tonne	Aluminium ingots of (i) commercial grade	30%+ 1500	-	-	10%+500	40%+ 2000
		(ii) Electrical conductor grade	30%	-	-	10%	40%
15.7.75 to 15.10.75	-do-	(i) Levy aluminium ingots	30%+ 2000	-	-	20%	50%+ 2000
		(ii) Other than levy aluminium ingots	30%+ 1500	-	-	10%+500	40%+ 2000

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
16.10.75 to 29.10.75	Advalorem+ Rs. per tonne	(i) Levy aluminium ingots for Cables & conductors for State Electricity Boards	13%	-	-	4-1/3%	17-1/3%
		(ii) Other than levy aluminium	30%+1500	-	-	10%+500	40%+2000
30.10.75 to 15.3.76	-do-	(i) Levy ingots	30%+2000	-	-	20%	50%+2000
		(ii) Other than levy ingots	30%+1500	-	-	10%+500	40%+2000
16.3.76 to 17.6.77	-do-	(i) Levy ingots	30%+2000	-	-	20%	50%+2000
		(ii) Other than levy ingots	30%+600	-	-	10%+200	40%+800
18.6.77 onwards	-do-	(i) Levy ingots	50%+2000	-	-	-	50%+2000
		(ii) Other than levy	40%+800	-	-	-	40%+800

NOTE: 1. Special excise duty of 20% of basic duty imposed in 1963-64 Budget was continued till 1972-73 Budget when it was merged with basic duty.

2. Regulatory duty @ 25% of basic duty was imposed w.e.f. 13.12.71. It was changed to 33-1/3% of basic duty in 1972-73 Budget and replaced by an auxiliary duty of 33-1/3% of basic duty in 1973-74 Budget. It has been merged with basic duty in 1977-78 Budget.

3. Concept of 'Levy and other than 'Levy' metal and differential duties thereon introduced w.e.f. 15.7.75 as a part of integrated plan for the development of aluminium Industry. Though levy metal for cables and conductors pays higher duty of 50% + Rs.2000/- per tonne, a cash subsidy of Rs.3130 per tonne of levy metal used in conductors purchased is given to State Electricity Boards (in the period 16.10.75 to 29.10.75 when lower basic rate of 13% only was applicable, this subsidy was however not available).

STATEMENT - 2

Changes in effective rates of duty (Basic, Regulatory & Auxiliary) levied on Copper from the date of introduction till 30.11.77

Period	Unit of assessment	Effective Rate of duty					
		Copper in crude form (ingots, bars etc.)			Copper Manufactures, namely, plates, sheets, circles, strips and foils		
		Basic	Reg/Aux.	Total	Basic	Reg/Aux	Total
1.3.61 to 23.4.62	Rs. per metric tonne	-	-	-	300	-	300
24.4.62 to 28.2.63	" "	100	-	100	300	-	300
1.3.63 to 28.2.65	" "	300	-	300	500	-	500
1.3.65 to 19.8.65	" "	1000	-	1000	1500	-	1500
20.8.65 to 12.12.71	" "	1500	-	1500	2000	-	2000
13.12.71 to 31.7.74	" "	1500	1125	2625	2000	1500	3500
1.8.74 to 15.3.76	" "	4000	3000	7000	4500	3375	7875
16.3.76 to 17.6.77	" "	4000	1600	5600	4500	1800	6300
18.6.77 onwards	" "	5600	-	5600	6300	-	6300

Note: 1. A regulatory duty @ 75% of basic was levied on copper in crude form and its manufactures w.e.f. 13.12.71 and it was replaced by an equivalent auxiliary duty in 1973-74 Budget. From 1.3.73 till 15.3.76 the auxiliary duty was levied @ 75% of basic duty. From 16.3.76 to 17.6.77 it was subject to auxiliary duty @ 40% of basic duty. The auxiliary duty has been merged with basic duty in 1977-78 Budget.

2. Copper pipes and tubes are also subject to duty. A Basic duty was imposed @ 10% in 1961-62 Budget and raised to 20% adv.w.e.f. 1.8.74. Over & above basic duty, regulatory duty and auxiliary duties have also been levied at the rates indicated in Note.1. With the merger of auxiliary with basic in 1977-78 Budget, these pipes and tubes are now subject to a basic duty of 28% adv.

STATEMENT - 3 (Part-I)

SALES PATTERN OF COMMERCIAL GRADE ALUMINIUM IN 1971 & 1976

S.No.	Name of the user Industry	Quantity sold by primary producers		Col.3 as % of total sales in 1971	Col. 4 as % of total sales in 1976
		1971	1976		
(1)	(2)	(3)	(4)	(5)	(6)
		(Tonnes)			
1.	Utensils manufacturers	22088	22443	33.9	29.3
2.	Bus Body manufacturers automobiles & Motor Vehicle parts units	6930	12083	10.6	15.8
3.	Construction	2142	3042	3.3	4.0
4.	Canning and packaging (pharmaceuticals, cigarettes, food and others)	9660	9620	14.8	12.6
5.	Casting alloys	3596	4243	5.5	5.6
6.	Aluminium paste & Powder	1453	1131	2.2	1.5
7.	Electrical appliances	1224	2183	1.9	2.8
8.	Coinage	442	301	0.7	0.4
9.	Secondary extruders	2378	4274	3.6	5.6
10.	Defence	912	3703	1.5	4.8
11.	Others	14297	13474	22.0	17.6
	Total	65122	76497	100	100

contd.....

STATEMENT - 3 (Part II)

PATTERN OF TAX BURDEN BORNE BY DIFFERENT INDUSTRY GROUPS DUE TO EXCISE DUTY ON ALUMINIUM

S.No.	Name of the user Industry	Excise duty borne on the purchases of aluminium from Primary producers		Col. 3 as % of total duty paid in	Col. 4 as % of total duty paid in
		1971	1976	1971	1976
(1)	(2)	(3)	(4)	(5)	(6)
I.	COMMERCIAL GRADE SALES		(Rs. lakhs)		
1.	Utensil manufacturers	294	969	12.8	9.1
2.	Bus body manufacturers, automobile & motor vehicle part manufacturers	126	602	5.5	5.7
3.	Construction	40	167	1.7	1.6
4.	Canning and Packing (Pharmaceuticals, cigarettes, foods and others)	247	746	10.7	7.0
5.	Casting alloys	45	101	1.9	1.0
6.	Aluminium Pastes and Powder	18	44	0.8	0.4
7.	Electrical appliances	27	126	1.3	1.2
8.	Coinage	11	18	0.5	0.2
9.	Secondary extruders	30	148	1.3	1.4
10.	Defence	17	200	0.7	1.9
11.	Others	262	859	11.4	8.1
	TOTAL FOR COMMERCIAL GRADE SALES	1117	3980	48.6	37.6
II.	ELECTRICAL CONDUCTOR GRADE SALES				
	Wires, cables and conductors and electrical equipment manufacturers	1182	6622	51.4	62.4
	GRAND TOTALI & II	2299	10602	100	100

Note: (i) The category 'others' under col. 2 (of Pt. I & Pt.II of the Statement) include miscellaneous consuming industries e.g., Atomic Research, Indian Oil, Dockyards, Venetian blinds manufacturers, printing/lithographic jobs, parts of boats/ships, furniture manufacturers, consumer durables, heat exchangers etc.

(ii) Exports have been left out.

Source: Data collected from the 4 primary producers i.e. (i) Indian Aluminium Ltd. (ii) Hindustan Aluminium (iii) Bharat Aluminium and (iv) Madras Aluminium.

STATEMENT 4

IMPACT OF THE EXCISE DUTY ON ALUMINIUM ON THE PRICES OF SELECTED FINISHED PRODUCTS USING ALUMINIUM AS INPUT

Sl. No.	Article taken up for study of duty incidence	No. of manufacturers for whom study carried out	Form in which aluminium used	Excise duty on aluminium contained in the article as a percentage of ex-factory price of the article	Excise duty on the finished article	Remarks
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1.	ALUMINIUM UTENSILS					
	(i) Made from old scrap or admixture of old scrap and virgin metal	15	Aluminium scrap and virgin ingots	Nil to 6%	Nil	On scrap or crude metal manufactured therefrom there is no excise duty. Very small units manufacturing aluminium utensils are generally scrap based. They add very little quantity (upto 10%) of virgin metal to improve the quality of the metal used for manufacturing aluminium utensils. The incidence accordingly is nil or very low. Utensils as such were liable to 2% but became exempt in 1977-78 Budget.
	(ii) Utensils manufactured from virgin metal, (e.g. thali, degchi, parat, topes, tava etc.	8	Aluminium circles	18.1% to 28.3%	Nil	Average incidence is about 20%.

(1)	(2)	(3)	(4)	(5)	(6)	(7)
2.	PATENT MEDICINES PACKED AND SOLD IN ALUMINIUM STRIPS	12	Aluminium foils of various dimensions	0.1% to 8.4%	2½% to 12½%	Tablets of low value but high bulk e.g., 'Strepcil' and 'milk of Magnesia' tablets bear higher incidence of around 8%. On other items which include vitamin tablets, and tablets like 'Plusprin', Novalgin', 'Brufane', 'Comicyn', 'Analgin', 'Asprin' etc. the average incidence is about 2%.
3.	PRESSURE COOKERS of varying capacity ranging from 3 litres to 16 litres (such as Hawkins, Paradies, Prestige, Marlex, etc.)	10	Aluminium circles and sheets	6.3% to 16.8%	10%	The average incidence is about 10%.
4.	DOMESTIC ELECTRICAL APPLIANCES:					
	(i) Heat Ovens small or large	2	Aluminium sheets pressed and spun	6.7% to 10.5%	25%	Average incidence about 8.5%.
	(ii) Other appliances such as toasters, mixeres, geysers, cooking range etc.	3	Aluminium sheets	0.9% to 3.9%	25%	Average incidence about 1.7%
5.	ELECTRIC WIRES & CABLES					
	(i) Aluminium winding wires					
	(a) Paper covered	5	Extruded rods	17.7% to 26.3%	10%	
	(b) Enamelled wires	3	Wire rods	14.6% to 18.8%	10%	

(1)	(2)	(3)	(4)	(5)	(6)	(7)
	ELECTRIC WIRES & CABLES (Cont'd)					
	(ii) All aluminium conductors (AAC)	20	Electrical grade wire rods	25% to 45.5%	5%	Average incidence is around 36%
	(iii) Aluminium conductors steel re-enforced (ACSR)	22	Aluminium wire rods/ bars	21.8% to 49.8%	5%	Average incidence is around 31%
	(iv) Power cables	2	Wire rods	6.5% to 19.6%	17½%	
6.	ELECTRIC CEILING FAN	1	Aluminium sheets of 18 SWG	2.3%	15%	
7.	WATER COOLER	1	Aluminium sheets	0.2%	20%	
8.	ELECTRIC TRANSFORMERS OF VARIOUS TYPES AND KVA RATINGS	8	Wires and strips	1% to 8.2%	2%	Average incidence is around 2.5%
9.	ELECTRIC MOTORS	3	Aluminium ingots/ wire rods	0.7% to 2.7%	10% 15% 20%	
10.	ELECTRIC ROTORS FOR MOTORS	1	Aluminium ingots	3.1%	20%	
11.	COMPRESSORS	1	EC grade aluminium and alloy	0.1% to 1.5%	2%	For compressor for refrigerators and air-conditioners the excise rate is 100%

(1)	(2)	(3)	(4)	(5)	(6)	(7)
12.	BUS BODIES	12	Aluminium sheets, extrusions chequered plates, angles etc.	5% to 19%	Nil	(i) The incidence shown under Col.5 is with respect to price charged for constructing bus bodies. It is highest for all aluminium bus bodies for which on an average it works out to 11 to 12 per cent. (ii) With respett to price of buses inclusive of cost of chassis the impact ranges between 2% & 6%
13.	LIFT COMPONENTS (Bottom tracts, supporting profile)	1	Aluminium sections	10.6%	2%	
14.	COINAGE	1	Aluminium ingots			Extent of aluminium in the different coins mentioned under column 2 varies between 2.21 gm. and 0.72 gm.
	10 paise			7.9%		
	5 paise			10.0%		
	3 paise			14.3%		
	2 paise			17.5%		
	1 paise			26.0%		

Source: Ad-hoc data collected on all India basis from Collectors of Central Excise

APPENDIX - 16

TAXATION OF PLASTIC RESINS

The production pattern of different plastic resins from 1971-72 to 1976-77 has been on the lines indicated in Statement 1. The excise duties on plastic resins ever since their inception till to date are shown in Statement 2. This statement also shows the existing import duties levied on different plastic resins.

2. At present plastic resins and certain articles of plastic (which pay duty as indicated in statement 2) contribute about Rs.67 crores by way of excise duty, of which resins contribute more than 70 per cent. Of the revenue realised (i.e. about Rs.50 crores) from plastic resins in 1976-77 the share of different plastic resins is estimated as follows: low density polythene (LDP) 25 per cen high density polythene (HDP) 18 per cent; Polyvinyl chloride (PVC) 25 per cent; polystyrene 12 per cent and other 20 per cent.

3. To have an idea of the major sectors which bear the burden of the duty on plastic resins, we initiated a study of the consumption pattern of 4 most important resins, namely, LDP, HDP, PVC and Polystyrene. We directly collected data from most of the primary producers of these resins on the sales pattern by major industries. The data were collected for the two years 1971 and 1976, to see if there was any shift in the consumption pattern. (As the imports are not fully canalised, this study was restricted to indigenous production; but it can be said that the pattern revealed thereby reflects fairly well the overall consumption pattern of these resins - there are hardly any imports of two of them, while for the other two the indigenous production meets the bulk of the demand.) We give results of this study in the following paragraphs.

4. Our study has shown that plastic resins (in general) find widespread use in different industries which produce household and other utility articles like plastic buckets, jugs, trays, crockery, combs, footwear, spectacle frames, fountain-pens, ball-point pens and other stationery articles, bangles, buttons, beads, toys, brushes and imitation jewellery; for producing various kinds of plastic containers used for packing edible oils, vanaspati, food stuffs and other consumer articles, cosmetics and toilet preparations, kerosene, petrol and other fuels or liquids; for the manufacture of plastic films, lay-flat tubings and bags for packaging foodstuffs, grocery articles, textiles and various other articles. Its industrial applications include production of moisture-proof laminated papers and fabrics, manufacture of woven sacks for packing foodgrains, fertilizers, etc., for producing telephone instruments and insulating materials for wires and cables. Pipes and tubes made of plastics are being increasingly used in plants and machinery as also for irrigation purposes. New uses of these resins are being explored and established, as in green houses having plastic covering to protect crops, lining of tunnels and canals, mulching, that is, covering of soil used for cultivation by plastic films, in the erection of storage houses for foodgrains in rural areas, distribution of potable water to village and rural areas in plastic pipes etc. (some of these uses are yet to catch up in our country). Though for certain applications, more than one plastic resins can and are used, the different plastic resins have their own distinct fields of applications because of differences in their properties.

5. Statement 3 indicates the consumption pattern of two important resins, viz., LDP and HDP, separately for the years 1971 and 1976, according to major consuming industries. It may be seen that plastic films used for packaging consume a substantial part of LDP (about 40 per cent in 1976) while various injection and blow moulding products use from 10 per cent to 11 per cent of this resin. The Statement also shows that the use of LDP in extrusion coatings has shown an increase since 1971 while its consumption by plastic films producers has considerably come down.

LDP CONSUMPTION PATTERN

6. The major use of high density polythene is in injection and blow moulding products - mostly household utilities, containers, etc. The share of these in the total consumption has fallen significantly to 55.5 per cent between 1971 and 1976 as against 71.3 per cent in 1971. The use of HDP for manufacturing woven sacks has, however, shown considerable increase - the share having gone up from 11.8 to 20.6 per cent.

HDP CONSUMPTION PATTERN

7. Though we could not collect the relevant data as in the case of other plastic resins from all the manufacturers, the pattern of sales in respect of 2 manufacturers (out of 5) for PVC and one (out of 2) for polystyrene was obtained, and the share of consumption by the major consuming sectors on this basis is shown in Statements 4 and 5 for these two resins. PVC consumption pattern has shown a considerable change in between 1971 and 1976. Whereas the share has declined in respect of footwear, wires and cables, and flexible PVC sheetings, its consumption has shown a significant increase in the case of rigid pipes and tubes and their fittings, used for industrial and agricultural purposes, as also for producing rigid films and lay-flat tubings and other miscellaneous purposes.

PVC AND POLYSTYRENE CONSUMPTION PATTERN

8. As for polystyrene, the sales pattern shows that whereas for the production of household utility articles the use of polystyrene has declined since 1971, the industrial applications of polystyrene and its use as packaging material have shown an upward trend.

9. To study the impact of the existing duties on plastic resins on various consuming industries, a study was initiated and data collected at all India level from selected representative producers of goods using plastic resins as an input. The consuming industries selected for the study included the packaging industry producing containers and plastic films/bags, footwear producers, household utility article manufacturers, wires and cables units, producers of irrigation pipes and tubes, units producing plastic laminated papers and fabrics, manufacturers of woven sacks and stationery articles and producers of spectacle frames. Statement 6 indicates the impact of the duty on plastic resins on the prices of the finished products containing such resins. The impact is measured as a percentage of the prices of the finished products / both the range for different units as well as the approximate average are given/.

IMPACT ON PRICES OF MAJOR CONSUMER INDUSTRIES

10. As may be seen from this Statement, the impact, which varies from industry to industry, is very substantial, in the case of plastic containers, household utility articles, plastic films and lay-flat tubings. In all these cases, 15 per cent to 20 per cent of the prices of the products and even higher in many cases, are accounted for by the excise duty paid on the plastic resins alone. Even for common man's cheap plastic footwears (which are not wholly made of plastic resins, but

also contain other materials like filiers), the incidence ranges between 5 per cent and 12 per cent. The incidence in respect of industrial applications like insulation of wires and cables is on an average about 5 per cent, on laminated papers it is about 8 per cent and on laminated fabrics it is around 6.5 per cent. The impact on prices as indicated above for different products is with regard to the excise duty as the resins used by the units, selected for study, were mostly indigenously produced. For the manufacturer of these very articles who use imported resins because they cannot get indigenous supplies, the impact on prices would be much higher than that of the excise duties. Our sample study has shown that the incidence of import duties on resins for spectacle frames ranges between 20 per cent and 25 per cent of the ex-factory price and for certain plastic fountain pens it even exceeded 35 per cent of the price when imported CAB resin was used.

11. The above analysis shows that the duties on plastic resins add substantially to the costs and prices of different consumer goods some of which are of special interest to the low income groups, apart from significantly increasing industrial costs wherever they form an important ingredient. Our study of the consumption pattern has also revealed that the off take of plastic resins for utility articles has declined, in some cases considerably, between 1971. This is another example where high duties have contributed significantly to placing products of modern technology beyond the reach of the common man.

STATEMENT 1

PRODUCTION PATTERN OF PLASTIC RESINS

S. No.	Description of resins	No. of manufacturers on DGTD list	Actual production (in tonne)					
			1971-1972	1972-1973	1973-1974	1974-1975	1975-1976	1976-1977
1.	2.	3.	4.	5.	6.	7.	8.	9.
1.	Low Density Polythene	3	28085	28511	27258	26972	27662	26064
2.	High Density Polythene	1	24057	19099	23000	24618	22987	22820
3.	Poly-vinyl Chloride	5	42738	48805	47906	45324	43840	47470
4.	Polystyrene	2	11951	13110	14388	8044	9156	13397
5.	Urea Formaldehyde	3	1787	1766	1834	1218	1762	2035
6.	Phenol Formaldehyde	3	2515	4452	5034	4029	3714	4217
	Total	17	111133	115743	119420	110205	109121	116003

Note: In the case of low density polythene, the data are for the two units which have been in production so far. The IPCL unit in the public sector, having a capacity to produce 80,000 tonne, is expected to go in production before the close of 1977-78.

SOURCE: Directorate General of Technical Development.

STATEMENT 2

PLASTICS - DUTY STRUCTURE

I. CHANGES IN EFFECTIVE RATES OF EXCISE DUTY (BASIC, SPECIAL, AUXILIARY) LEVIED ON PLASTIC RESINS FROM DATE OF INTRODUCTION OF THE LEVY TILL 30.11.1977.

(Effective rate of excise duty)

Period	Basic (Adval.)	Special (Adval.)	Aux. (Adval.)	Total (Adval.)
1.3.61 to 28.2.63	20%	-	-	20%
1.3.63 to 25.5.67	20%	4%	-	24%
26.5.67 to 16.3.72	30%	6%	-	36%
17.3.72 to 28.2.74	40%	-	-	40%
1.3.74 to 31.7.74	40%	-	8%	48%
1.8.74 to 15.3.76	40%	-	16%	56%
16.3.76 to 17.6.77	30%	-	10%	40%
18.6.77 onwards	40%	-	-	40%

NOTE: (i) Special excise of 20% of the basic duty was imposed on resins in 1963-64 Budget. This duty was merged with basic duty in the 1972-73 Budget.

(ii) For polyurethane foam a higher rate of 40% basic duty was prescribed in the 1971-72 Budget (with effect from 29.5.71) which with the special duty of 20% of the basic duty meant a total effective duty of 48%. The basic duty was raised to 50% in the 1972-73 Budget when the special excise was merged with basic. With the levy of auxiliary duties in 1974, the total effective rates went upto 60% w.e.f. 1.3.74 and 70% w.e.f. 1.8.74. The latter is the present effective rate.

(iii) Alkyd resins were exempt w.e.f. 23.9.65 and the exemption has continued since then.

(iv) For maleic and phenolic resins a specific basic duty of 80 paise per kg. was prescribed w.e.f. 23.9.65 which was changed to 10% ad valorem for maleic resins and 15% ad valorem for phenolic resins w.e.f. 1.6.71. A special excise of 20% of the basic duty was also leviable on them till 16.3.72. The total effective duty remained unchanged in the 1972 merger of the basic and special duties - the basic duties being stepped upto 12% and 18% respectively. The auxiliary duty of 20% of the basic duty with effect from 1.3.74 and 40% of the

basic duty w.e.f. 1.8.74 was imposed in the 1974 Budget. In the 1976-77 Budget the basic duty was reduced for the two resins to 9% and 13.5% respectively, and the auxiliary duty changed to 1/3rd of the basic duty. In the 1977-78 Budget, after the merger of the auxiliary duty with the basic duty, the rates on these resins have been fixed at 12% and 18%, respectively.

II. EXISTING DUTY ON ARTICLES OF PLASTIC

Articles made of plastics are also excisable and chargeable to duty under the same tariff item No. 15-A of the Excise Schedule along with plastic resins. Most articles of plastics are presently exempt if they are manufactured out of duty paid synthetic resins. However, in the case of rigid plastic boards, sheetings, sheets and films and flexible PVC sheetings, sheets, films and lay-flat tubings not containing any textile material, the duty is leviable even at the product stage, there being provisions for relief for the resin stage duty. The effective incidence on such boards, sheetings, sheets, films and lay-flat tubings ranges between 28% and 36%. Articles of polyurethane foam are presently taxed at 70% ad valorem.

III. IMPORT DUTIES ON PLASTIC RESINS (AS ON 30.11.1977)

Plastic resins when imported are liable to a basic customs duty of 100% together with an auxiliary duty of 20% apart from the countervailing duty (on price inclusive of customs and auxiliary duties). The basic and auxiliary duties of customs have been effectively reduced by notifications for certain important resins. The current rates applicable for different resins are given in the following table:

T A B L E

Description of resin	Import duty leviable			
	Basic %	Auxiliary %	Countervailing %	Total %
Low density polythene (LDP)	60	15	70	145
High density polythene (HDP)	30	5	54	89
Poly-vinyl chloride (PVC)	30	5	-	89
Polypropylene	60	15	70	145
CAB, ABS, moulding powders and granules	60	15	70	145
SAN, polycarbamate poly-acetals and PTFE				
Others	100	20	88	208

STATEMENT 3

SALES PATTERN OF PLASTIC RESINS BY INDIGENOUS MANUFACTURERS AND THE EXCISE DUTY BURDEN BORNE BY DIFFERENT CONSUMING SECTORS

Sl. No.	User industry	Sales effected (Tonnes)		Duty on sales (Rs. lakhs)		Col. (3) as percentage of total sales in 1971	Col. (4) as percentage of total sales in 1976	Approximate number of units to which sales effected in	
		1971	1976	1971	1976			1971	1976
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
I -	LOW DENSITY POLYTHENE								
1.	Plastic films	20620	18243	341.2	768.9	77.9	69.3	721	1845
2.	Injection moulding goods	2130	2407	35.2	102.7	8.0	9.1	93	125
3.	Blow moulding products	515	527	8.5	22.5	1.9	2.0	13	20
4.	Wires and cables	953	418	15.8	17.9	3.6	1.6	27	50
5.	Extrusion coatings (paper, fabrics, etc.)	929	2232	15.4	95.8	3.5	8.5	14	50
6.	Pipes and tubes	170	166	2.8	7.3	0.6	0.6	NA	NA
7.	Others	1150	2350	19.1	101.2	4.5	8.9	-	10
	Total	26467	26343	438.0	1116.3	100	100	868	2100

cont'd.....

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
II - HIGH DENSITY POLYTHENE									
1.	Plastic films	1000	600	15.2	21.3	4.9	2.7	30	65
2.	Injection moulding goods	10700	7700	162.2	273.8	52.7	33.8	500	1350
3.	Blow moulding products	3790	4935	57.4	175.5	18.6	21.7	300	600
4.	Wires and cables	-	150	-	5.3	-	0.6	-	1
5.	Woven sacks	2400	4700	36.4	167.1	11.8	20.6	50	115
6.	Pipes and tubes	165	1500	2.5	53.3	1.3	6.6	10	15
7.	Sheets	100	100	1.6	3.6	0.5	0.4	2	4
8.	Monofilament strapping cane	2050	3100	31.1	110.2	10.2	13.6	108	350
	Total	20205	22785	306.4	810.1	100	100	1000	2500

Notes: (1) The sales pattern is as per the actual sales data obtained from the two indigenous manufacturers of LDP and the only manufacturer of HDP. In the case of LDP the number of units to which sales were effected, given in cols. (9) and (10) relate to only one producer. The data for the second unit could not be collected.

(2) The excise duty figures under cols. (7) & (8) include basic, special and auxiliary duties on plastic resins.

(3) The data are for calendar years 1971 and 1976. Though one of the units supplied data for the 12-month period different from January to December, a similar sales pattern was presumed and the data have been included in them for the years 1971 and 1976.

(4) Exports have been excluded while indicating the sales pattern.

SOURCE: Actual sales data obtained from the primary producers.

STATEMENT - 4

CONSUMPTION PATTERN OF PVC

Sl. No.	User industry	Percentage share with reference to total	
		1971	1976
1.	Flexible PVC sheets/sheetings	24.9	21.5
2.	Footwear	22.9	11.9
3.	Rigid films and layflat tubings	3.2	8.6
4.	Rigid pipes and tubes and their fittings	7.3	18.4
5.	PVC containers	0.1	Neg.
6.	PVC cables	30.3	20.1
7.	Transport	-	-
8.	Others	11.3	19.5
	Total:	100.0	100.0

SOURCE: · Actual sales data obtained from 2 of the 5 primary producers.

STATEMENT - 5

CONSUMPTION PATTERN OF POLYSTYRENE

Sl. No.	User industry	Percentage share with reference to Total 1971-72	1976-77
I.	Household		
(i)	Bangles	6.1	6.1
(ii)	Buttons	3.4	3.9
(iii)	Toys	6.7	5.3
(iv)	Beads	3.9	3.8
(v)	Other utility and miscellaneous	11.8	3.4
II.	Personal		
(i)	Brushes	0.5	2.3
(ii)	Combs	1.4	1.2
(iii)	Imitation Jewellery	1.9	1.5
(iv)	Stationery	3.4	4.3
(v)	Others (light fixtures, novelties and miscellaneous)	10.2	7.2
III.	Industrial		
(i)	Radio components	8.9	9.0
(ii)	Refrigerators	1.5	4.2
(iii)	Fan components	0.7	2.6
(iv)	Automobile	2.0	2.7
(v)	Miscellaneous (electrical items, air-conditioner, textile components, batteries etc.)	7.4	11.0
IV.	Packaging (Pharmaceuticals, cosmetics industrial and utility)	17.8	25.0
V.	Defence	0.6	1.5
VI.	Miscellaneous	11.8	5.0
	Grand Total:	100.0	100.0

SOURCE: Actual sales information obtained from one of the two primary producers of polystyrene.

STATEMENT - 6

IMPACT OF THE DUTY ON PLASTIC RESINS ON THE PRICES OF FINISHED PRODUCTS CONTAINING SUCH RESINS

Sl. No.	Article taken up for study	No. of manufacturers for whom study carried out	Description of the resin used.	Incidence of the duty on resin (contained in the article) as a percentage of ex-factory price of the article.	REMARKS
(1)	(2)	(3)	(4)	(5)	(6)
1.	Plastic containers for vanaspati				
	1 Kg.	8	H. D. P.	14.4% to 27 %	Incidence is generally around 18%
	2 kg.	3	"	9.5% to 21.4%	
	4 kg.	1	"	14.6%	
2.	Plastic containers for kerosene/petrol				
	½ litre	2	"	17.7%	
	1 "	2	"	20% to 22%	
	2.5 "	1	"	13.1%	
	5 "	3	"	16.4% to 26%	
	10 "	2	"	17.8%	
	18 "	1	"	17.8% to 20.6%	
	20 "	2	"	17.4% to 20.5%	
	30 "	3	"	17.8% to 24.6%	
	48 "	1	"	14.2%	
3.	Plastic containers for cosmetics				
	a) For talcum powder	2	"	20.5% to 23.5%	
	b) Jars	1	"	12.1% to 13.3%	
	c) For lipsticks	1	Polystyrene	2.6% to 4.3%	
	d) For lotions	2	"	21.6%	
	e) For creams	2	"	27.2%	
	f) Soap boxes	1	H. D. P.	13.1%	

(1)	(2)	(3)	(4)	(5)	(6)
4.	Plastic film bags and lay-flat tubings for packaging				
	i) Layflat tubings/bags	17	L.D.P.	17.8% to 27.7%	Average incidence is 23%
	ii) "	4	H.D.P.	19.8% to 23.5%	
	iii) Layflat tubings for toys	2	P.V.C.	6.7%	
	iv) Rigid layflat tubings	1	"	13%	
5.	Plastic footwear	10	"	5.1% to 12.4%	Average incidence is around 9%
6.	Household plastic insulated wires	24	"	1.9% to 10.7%	Average incidence is around 5%
7.	Other insulated wires and cables	17	"	1.2% to 8%	Average is around 4%
8.	Household utility articles				
	i) Plastic buckets	13	H.D.P.	11% to 24.3%	Average is around 15%
	ii) Plastic mugs	10	"	14.6% to 25%	
	iii) Plastic jugs	6	"	11% to 16.6%	
	iv) Plastic trays	5	"	11.8% to 14.3%	
		1	Polystyrene	11.1%	
		1	Melamine formaldehyde	22%	
		1	Polystyrene	22%	
	v) Crockery sets	4	H.D.P.	13% to 17%	
		1	Urea formaldehyde	12.1%	
	vi) Plastic combs	4	H.D.P.	13% to 19.8%	
9.	Plastic irrigation pipes and tubes of various diametres	11	P.V.C.	8% to 18.4%	Average incidence is around 11%
		1	H.D.P.	14.4% to 14.8%	
10.	Plastic laminated paper	16	L.D.P.	2.8% to 10.2%	Average incidence is around 8%
		1	P.V.C.	6%	
11.	Plastic coated fabrics	1	P.V.C.	5.6% to 8.7%	Average is around 6.5%
12.	Woven/HDP sacks	13	H.D.P.	7.3% to 19%	Average is around 16%

STATEMENT - 6

IMPACT OF THE DUTY ON PLASTIC RESINS ON THE PRICES OF FINISHED PRODUCTS CONTAINING SUCH RESINS

Sl. No.	Article taken up for study	No. of manufacturers for whom study carried out	Description of the resin used.	Incidence of the duty on resin (contained in the article) as a percentage of ex-factory price of the article.	REMARKS
(1)	(2)	(3)	(4)	(5)	(6)
1.	Plastic containers for vanaspati				
	1 Kg.	8	H.D.P.	14.4% to 27 %	Incidence is generally around 18%
	2 kg.	3	"	9.5% to 21.4%	
	4 kg.	1	"	14.6%	
2.	Plastic containers for kerosene/petrol				
	½ litre	2	"	17.7%	
	1 "	2	"	20% to 22%	
	2.5 "	1	"	13.1%	
	5 "	3	"	16.4% to 26%	
	10 "	2	"	17.8%	
	18 "	1	"	17.8% to 20.6%	
	20 "	2	"	17.4% to 20.5%	
	30 "	3	"	17.8% to 24.6%	
	48 "	1	"	14.2%	
3.	Plastic containers for cosmetics				
	a) For talcum powder	2	"	20.5% to 23.5%	
	b) Jars	1	"	12.1% to 13.3%	
	c) For lipsticks	1	Polystyrene	2.6% to 4.3%	
	d) For lotions	2	"	21.6%	
	e) For creams	2	"	27.2%	
	f) Soap boxes	1	H.D.P.	13.1%	

(1)	(2)	(3)	(4)	(5)	(6)
4.	Plastic film bags and layflat tubings for packaging				
	i) Layflat tubings/bags	17	L.D.P.	17.8% to 27.7%	Average incidence is 23%
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	iii) Layflat tubings for toys	2	P.V.C.	6.7%	
	iv) Rigid layflat tubings	1	"	13%	
5.	Plastic footwear	10	"	5.1% to 12.4%	Average incidence is around 9%
6.	Household plastic insulated wires	24	"	1.9% to 10.7%	Average incidence is around 5%
7.	Other insulated wires and cables	17	"	1.2% to 8%	Average is around 4%
8.	Household utility articles				
	i) Plastic buckets	13	H.D.P.	11% to 24.3%	Average is around 15%
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	iii) Plastic jugs	6	"	11% to 16.6%	
	iv) Plastic trays	5	"	11.8% to 14.3%	
		1	Polystyrene	11.1%	
		1	Melamine formaldehyde	22%	
		1	Polystyrene	22%	
	v) Crockery sets	4	H.D.P.	13% to 17%	
		1	Urea formaldehyde	12.1%	
	vi) Plastic combs	4	H.D.P.	13% to 19.8%	
9.	Plastic irrigation pipes and tubes of various diametres	11	P.V.C.	8% to 18.4%	Average incidence is around 11%
		1	H.D.P.	14.4% to 14.8%	
10.	Plastic laminated paper	16	L.D.P.	2.8% to 10.2%	Average incidence is around 8%
		1	P.V.C.	6%	
11.	Plastic coated fabrics	1	P.V.C.	5.6% to 8.7%	Average is around 6.5%
12.	Woven/HDP sacks	13	H.D.P.	7.3% to 19%	Average is around 16%

(1)	(2)	(3)	(4)	(5)	(6)
13.	Plastic fountain pens and ball point pens	7	C.A.B.	1% to 14.6%	CAB is imported at present. The incidence shown is only for countervailing duty portion. The incidence of total import duty varies between 2% and 30.4%
14.	Plastic refills	1	Polypropylene	1.5%	1.5% is the impact of countervailing duty on polypropylene which is imported (incidence of total import duty is 3%)
15.	Spectacle frames	4	Cellulose nitrate sheets	13.5% to 24%	The incidence shown is that of countervailing duty on imported cellulose nitrate sheets. The incidence of total import duty varies between 28% and 49.5%

SOURCE: Ad-hoc reports from the Central Excise Collectorates as per survey initiated by the Committee.

APPENDIX 17

INDUSTRYWISE CLASSIFICATION OF MANUFACTURERS ACCORDING TO VALUE OF PRODUCTION/CLEARANCES

To study the pattern of production and duty payment by different class of producers in different industries and to have an idea of the average incidence of excise duties borne, as well as to have an assessment of the extent of the value of production and contribution to exchequer by way of excise duty by the smaller producers - an all India industrywise survey was conducted in the Committee's Secretariat. As normally, assessments and duty payments are linked to clearances rather than production, all Collectors of Central Excise were requested to report for the year 1975-76 in respect of each industry (covered by a tariff item in the excise tariff) the pattern of clearances and duty payments by different units classified by different value slabs ranging from those having clearances not exceeding Rs. one lakh per annum to those whose clearances exceeded Rs. 15 lakhs per annum. The study excluded from its scope a few industries/products, where the collection of information - especially value of clearances - would have been extremely difficult or where the production was almost in the organised sector. Thus, tobacco and tobacco products, loose tea, coffee, petroleum products, cine films and goods falling under item No. 68 of excise tariff were left out of the survey. Likewise units covered under compounded levy or those completely exempt in any industry were excluded.

The data received from all Collectors was carefully scrutinised and various discrepencies which were detected in the Secretariat got rectified. Attempts were also made to cross check the data with that compiled by Directorate of Statistics and Intelligence of C.B.E.&C. and Collectors were requested to reconcile the discrepencies wherever they were significant. Though in most cases the final all India figures as compiled according to Committee's survey came very close to the figures of the Directorate of Statistics, in a few cases the variation (which was somewhat higher but still generally within 10 per cent) could not be explained by the Collectors.

The industry-wise results of the All India survey are given in the Statement appended. For all the industries covered by the survey (subject to the limitations referred to above) the following pattern has emerged:

T A B L E

UNITS CLASSIFIED BY ANNUAL VALUE OF CLEARANCE

Value slab	No. of units	Total value of clearance	Total duty paid
		(Rupees lakhs)	
Not exceeding Rs. 1 lakh	15399	6008	865
Exceeding Rs. 1 lakh but not exceeding Rs. 2 lakhs	2202	3217	431

Value slab	No. of units	Total value of clearance	Total duty paid
		(Rs. lakhs)	
Exceeding Rs. 2 lakhs but not exceeding Rs. 5 lakhs	2553	8359	1340
Exceeding Rs. 5 lakhs but not exceeding Rs. 10 lakhs	1656	11286	1721
Exceeding Rs. 10 lakhs but not exceeding Rs. 15 lakhs.	947	11773	1650
Exceeding Rs. 15 lakhs	5513	1395452	220859
Total	28270	1436095	226866

The above table shows that -

(i) out of above Rs. 2269 crores total revenue the smaller units whose clearances did not exceed Rs. 15 lakhs per annum, contributed only about Rs. 60 crores (i. e. less than 3%). However, in terms of number they were about 81% of the total.

(ii) The average incidence of excise duty borne by all the industries covered by the survey was about 16% of the base.

In this proforma

'A' denotes number of units (Actual)
'B' denotes value of clearances (Rs. lakhs)
'C' revenue (Rs. lakhs)

STATEMENT

COMMODITYWISE PATTERN OF CLEARANCES AND DUTY PAYMENTS BY UNITS CLASSIFIED ACCORDING TO VALUE OF CLEARANCES

(Base: 1975-76)

S. No.	Name of commodity	Units with value of clearances for home consumption during the financial year 1975-76																					
		Not exceeding Rs.1 lakh each			Exceeding Rs.1 lakh but not exceeding Rs.2 lakhs			Exceeding Rs.2 lakhs but not exceeding Rs.5 lakhs			Exceeding Rs.5 lakhs but not exceeding Rs.10 lakhs			Exceeding Rs.10 lakhs but not exceeding Rs.15 lakhs			Exceeding Rs.15 lakhs			Total		
		A	B	C	A	B	C	A	B	C	A	B	C	A	B	C	A	B	C	A	B	C
	1	2(a)	2(b)	2(c)	3(a)	3(b)	3(c)	4(a)	4(b)	4(c)	5(a)	5(b)	5(c)	6(a)	6(b)	6(c)	7(a)	7(b)	7(c)	8(a)	8(b)	8(c)
1.	Sugar	185	94	16	63	92	16	157	382	63	71	111	22	1	11	2	249	78700	22515	726	79390	22634
2.	Confectionery	228	84	Neg	10	13	Neg	6	17	1	2	14	1	1	11	1	15	1683	163	262	1822	166
3.	Prepared or preserved foods	356	81	3	44	66	3	33	102	10	16	95	10	15	189	18	50	6931	687	514	7464	731
4.	Food product	148	47	1	15	23	1	8	22	2	8	60	6	11	141	13	31	3140	714	221	7433	737
5.	Aerated water	2	1	Neg	1	1	Neg	4	16	4	4	23	4	6	79	23	36.	2837	784	53	2957	815
6.	Glucose & dextrose	11	3	Neg	3	4	Neg	4	16	1	3	19	Neg	1	12	1	14	2341	209	36	2395	211
7.	Instant Coffee	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2	814	163	2	814	163
8.	Package tea	194	20	2	8	1	1	11	46	6	10	65	6	9	104	9	18	9752	633	250	9998	657
9.	Vegetable non essential oil*	22	6	Neg	4	7	Neg	12	42	1	9	74	2	5	55	1	100	11303	157	152	11487	161
10.	Vegetable product	-	-	-	1	2	Neg	-	-	-	1	8	Neg	-	-	-	75	40426	1913	77	40436	1913
11.	Soda ash	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	4423	440	4	4423	440
12.	Paints & varnishes	430	163	6	125	186	6	108	396	29	71	505	51	34	445	38	118	15377	1263	886	17072	1393
13.	Chemicals	7	2	Neg	1	2	Neg	3	8	1	3	23	2	5	67	9	28	10797	1822	47	10899	1834
14.	Caustic soda	-	-	-	-	-	-	1	2	Neg	2	14	1	-	-	-	33	7921	791	36	7937	792
15.	Sodium silicate	74	32	5	70	108	15	98	317	44	70	464	68	40	468	65	35	730	91	387	2119	288
16.	Glycerine	2	1	Neg	3	5	1	2	7	2	2	12	2	2	29	4	10	1083	161	21	1137	170
17.	Dye stuff	95	30	8	34	52	12	42	154	40	26	203	51	16	196	50	64	13192	2826	277	13827	2987
18.	Synthetic organic product	24	17	3	2	3	1	3	9	2	1	5	1	2	21	5	10	635	144	42	690	156
19.	Patent or proprietary medicines	456	149	11	94	139	10	96	308	22	82	567	40	32	381	43	192	38172	2572	952	39716	2698
20.	Cosmetics other than perfumed hair oil	620	96	11	16	21	7	21	73	32	3	21	12	3	36	14	28	2085	995	691	2332	1071
21.	Perfumed hair oil	220	23	2	7	8	1	3	8	2	5	18	3	-	-	-	15	438	79	250	495	87
22.	Tooth paste	6	4	-	2	3	Neg	1	4	Neg	2	15	2	-	-	-	6	2000	200	17	2026	202
23.	Acids	9	2	Neg	6	8	1	-	-	-	3	24	3	6	73	7	52	3241	303	76	3348	314
24.	Gases	28	10	2	13	21	4	38	136	36	53	372	56	17	212	33	69	3911	499	218	4662	630
25.	Fertiliser	4	1	Neg	4	5	Neg	7	23	3	3	18	4	2	25	4	51	61680	8141	71	61752	8152
26.	Soap	27	8	Neg	9	15	Neg	6	16	1	4	33	1	4	51	4	41	17608	1674	91	17731	1680
27.	Plastics	119	32	13	38	49	29	33	114	46	25	252	97	19	245	108	86	15399	7121	320	16891	7405
28.	Organic surface active agents	28	9	1	10	15	2	9	26	4	6	41	5	3	38	6	32	6535	980	88	6664	998

Cont'd....2/-

(1)	2(a)	2(b)	2(c)	3(a)	3(b)	3(c)	4(a)	4(b)	4(c)	5(a)	5(b)	5(c)	6(a)	6(b)	6(c)	7(a)	7(b)	7(c)	8(a)	8(b)	8(c)
29. Cellophane	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2	856	170	2	850	170
30. Starch	11	2	Neg	1	1	Neg	2	7	1	2	20	2	-	-	-	2	298	45	18	328	48
31. Tyres & tubes	33	8	3	8	11	4	4	14	2	3	28	4	2	27	7	15	25758	13413	65	25846	13433
32. Rubber products	272	134	45	41	65	17	46	173	49	36	241	71	26	326	125	52	6131	1698	475	7070	2005
33. Synthetic rubber	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1	20	1	1	20	1
34. Plywood	62	17	2	15	20	2	42	144	14	28	190	23	11	137	18	62	4214	850	220	4722	909
35. Paper and paper boards	252	136	12	87	134	14	147	467	49	128	869	76	87	1066	92	247	38959	6930	898	41631	7173
36. Rayon & Synthetic fibres and yarn	90	22	4	28	40	35	44	156	23	45	328	34	26	322	50	176	58001	23597	409	58869	23743
37. Cotton yarn	162	9	40	14	17	2	30	69	6	15	107	8	13	170	15	537	154785	7413	771	155137	7484
38. Woollen yarn	56	7	1	15	23	2	25	86	8	27	195	22	21	258	26	75	4581	406	219	5150	465
39. Jute twist yarn, thread, ropes & twines all sorts	15	4	1	5	7	2	14	47	9	12	89	19	9	101	25	17	1015	328	72	1263	284
40. Yarn, all sorts, NES	45	13	3	23	34	7	41	128	20	26	207	30	19	230	32	154	26257	4698	308	26869	4790
41. Cotton fabrics	124	30	3	53	76	7	49	126	15	36	237	24	28	355	40	382	154412	11675	672	155236	11761
42. Woollen fabrics	10	3	Neg	3	4	Neg	9	29	2	9	68	5	9	118	7	56	8280	1039	96	8502	853
43. Rayon/art silk fabrics	66	21	1	21	35	1	34	127	7	21	152	11	13	163	13	326	69329	3828	481	69827	3861
44. Jute manufactures	4	1	Neg	-	-	-	2	6	Neg	-	-	-	-	-	-	77	31267	4422	83	31274	4422
45. Textile fabrics NES	1	Neg	Neg	2	3	Neg	-	-	-	-	-	-	1	11	2	-	-	-	4	814	2
46. Coated textile fabrics	1	Neg	Neg	1	1	Neg	-	-	-	-	-	-	-	-	-	-	-	-	2	1	Neg
47. Linoleum	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1	114	20	8	114	233
48. Typewriter ribbons	3	2	Neg	2	2	Neg	-	-	-	1	6	1	1	13	1	3	175	18	10	198	20
49. Mineral fibres & yarn	14	6	1	4	7	Neg	6	19	2	1	5	Neg	2	29	2	2	50	7	29	116	12
50. Cement	-	-	-	-	-	-	2	8	1	-	-	-	-	-	-	53	36111	14011	55	36119	14012
51. Glass and glassware	74	31	8	11	17	5	21	69	19	17	154	45	4	45	11	80	7162	2043	207	7478	2131
52. Chinaware & porcelainw porcelainwares	221	85	2	80	111	10	72	212	40	19	132	32	6	78	16	44	4164	1033	442	4782	1133
53. Asbest s cement products	98	41	6	47	65	9	31	92	12	9	71	4	1	12	Neg	19	4556	665	205	4837	696
54. Iron in any crude form	-	-	-	1	1	Neg	2	5	1	1	9	0	-	-	-	9	9086	913	13	9101	914
55. Steel ingots	17	6	1	6	10	2	10	33	6	15	99	15	1	15	3	85	8365	1134	134	8528	1161
56. Copper and copper alloys	120	30	4	28	42	3	52	184	15	61	424	27	33	395	14	141	12402	1391	435	13477	1454
57. Iron & steel products	205	116	9	31	60	3	81	268	22	98	707	45	107	1399	30	335	124080	22437	858	126625	22546
58. Zinc	11	2	1	-	-	-	2	5	Neg	-	-	-	3	37	2	8	4349	867	24	4393	870
59. Aluminium	89	21	7	19	26	9	16	51	9	28	187	40	8	92	15	51	19018	8790	211	19395	8870
60. Lead	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1	359	25	1	359	25
61. Tin plates & tin sheets	232	81	5	5	-	2	38	-	-	-	-	-	-	-	67	8	4834	364	9	4834	364
62. I.C. Engines	232	82	3	28	44	2	36	109	4	15	97	4	5	61	Neg	31	8781	433	347	9174	446
63. Refrigereting & air conditioning appliances & machinery	222	37	29	13	29	12	14	43	28	8	51	37	3	37	22	17	2674	1811	277	2862	1939
64. Electric motor	530	211	27	78	114	15	85	269	34	58	373	52	28	343	50	60	13139	11598	847	14449	1776

Cont'd.....

1	2(a)	2(b)	2(c)	3(a)	3(b)	3(c)	4(a)	4(b)	4(c)	5(a)	5(b)	5(c)	6(a)	6(b)	6(c)	7(a)	7(b)	7(c)	8(a)	8(b)	8(c)
65. Power driven pump	523	133	2	73	101	6	54	171	13	29	206	16	21	297	19	40	2752	240	740	3620	296
66. Motor starters	77	14	Neg	7	13	1	4	14	1	2	14	1	-	-	-	15	1486	149	105	1541	152
67. Electric batteries and parts thereof	199	16	2	1	2	1	17	26	4	5	34	5	4	46	9	24	9727	2073	250	9851	2094
68. Electric bulb and tubes	320	82	26	14	15	2	7	24	3	5	26	3	13	170	19	16	3499	961	375	3816	1014
69. Electric fans	314	96	13	27	35	4	49	147	19	17	122	15	10	110	13	38	6599	800	455	7109	864
70. Wireless receiving sets	88	16	2	6	10	2	20	65	10	17	112	15	15	189	37	30	6511	848	176	6903	914
71. Parts of wireless receiving sets	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2	316	31	2	316	31
72. Electric wires and cables	479	361	15	62	91	9	88	302	22	69	515	30	27	338	26	143	24855	1587	868	26462	1689
73. Domestic electrical appliances	205	44	11	20	26	6	23	76	18	12	91	23	6	72	18	12	400	100	278	709	176
74. Office machines	93	46	7	12	17	3	9	28	4	7	57	9	1	13	2	45	2971	431	167	3132	456
75. Computers	-	-	-	1	1	Neg	-	-	-	-	-	-	-	-	-	2	350	52	3	351	52
76. Electricity supply meters	2	1	Neg	-	-	-	-	-	-	-	-	-	-	-	-	12	1179	118	14	1180	118
77. Motor vehicles	231	66	4	41	59	4	47	158	9	51	276	20	8	100	7	42	56190	6936	420	56849	6980
78. Motor vehicles parts	376	1302	5	23	32	3	23	85	15	11	79	15	4	49	10	40	5867	1073	477	7414	1121
79. Gram-ophone and parts	45	15	4	7	11	3	7	29	8	2	15	4	1	13	4	8	860	179	70	941	202
80. Foot-wears	6	3	Neg	2	3	Neg	2	5	1	3	25	3	3	38	2	17	4934	485	33	5008	491
81. Electrical stampings and laminations	145	51	1	15	20	1	17	54	5	13	83	8	9	114	11	25	4805	480	224	5127	506
82. Work trucks	3	1	Neg	-	-	-	-	-	-	-	-	-	1	14	1	6	352	35	10	367	36
83. Tape recorders	13	8	1	4	6	Neg	1	4	Neg	-	-	-	-	-	-	3	55	5	21	73	6
84. Cinematograph projectors	20	10	2	2	3	1	3	8	2	1	5	2	2	29	4	4	92	18	32	147	29
85. Photographic apparatus and goods	17	4	Neg	1	2	Neg	4	13	1	1	10	Neg	4	48	4	10	1630	93	37	1707	98
86. Matches	2500	643	449	113	171	87	116	422	328	61	410	318	24	298	223	41	3317	2098	2855	5261	3503
87. Mechanical lighters	16	2	1	2	3	1	-	-	-	-	-	-	-	-	-	-	-	-	18	5	2
88. Steel furniture	1533	484	3	56	75	5	33	111	18	9	66	12	4	48	10	20	1809	358	1655	2593	406
89. Crown corks	12	2	1	2	3	1	1	5	2	3	27	9	2	25	9	5	434	178	25	496	200
90. Pilfer proof caps	52	17	2	3	4	Neg	10	29	7	5	32	4	2	22	5	13	932	140	85	1036	158
91. Wool tops	-	-	-	1	2	Neg	2	7	1	1	8	1	1	14	1	11	6284	477	16	6315	480
92. Metal containers	315	114	7	111	157	15	75	257	39	66	473	79	37	461	67	120	11182	1689	724	12644	1896
93. Slotted angles and channels	38	8	1	3	3	Neg	1	3	Neg	1	7	1	3	40	4	2	51	5	48	112	11
94. Safes and strong boxes	81	17	1	2	2	Neg	2	5	1	1	7	1	-	-	-	2	556	111	88	587	114

1	2(a)	2(b)	2(c)	3(a)	3(b)	3(c)	4(a)	4(b)	4(c)	5(a)	5(b)	5(c)	6(a)	6(b)	6(c)	7(a)	7(b)	7(c)	8(a)	8(b)	8(c)
95. Rolling bearings	80	54	4	9	14	1	9	29	5	8	52	8	5	62	9	14	4947	744	125	5158	771
96. Welding electrodes	4	Neg	nil	3	5	Neg	-	-	-	1	6	Neg	-	-	-	20	3603	540	28	3614	540
97. Coated abrasives and grinding wheels	18	6	1	14	21	3	2	6	1	1	9	1	4	45	7	12	1832	275	51	1919	288
98. Cutting tools	41	12	Neg	16	26	2	12	40	4	8	61	6	6	71	7	25	1274	192	108	1484	211
99. Bolts, nuts and screws	1140	328	2	276	397	2	214	814	19	14	90	6	12	149	20	32	2095	309	1688	4873	358
100. Zip and slide fasteners	13	6	Neg	2	3	Neg	7	21	5	5	101	8	3	40	8	2	86	17	32	257	38
101. Pressure cookers	18	3	Neg	3	4	Neg	5	17	2	3	21	2	3	38	4	7	622	61	39	705	69
102. Vacuum flasks	2	Neg	Neg	3	4	1	2	6	2	3	21	4	-	-	-	10	246	44	20	277	51
103. Playing cards	39	29	-	2	3	Neg	7	24	5	5	40	8	1	13	3	6	245	45	60	354	61
104. Camphor	3	Neg	Neg	-	-	-	-	-	-	-	-	-	-	-	-	2	313	31	5	313	31
105. Menthol	16	6	Neg	1	2	Neg	2	8	1	3	23	2	2	22	2	3	315	32	27	376	37
106. Electric insulating tape	14	6	1	4	6	1	20	65	6	3	20	2	2	21	2	4	164	16	47	282	28
107. Adhesive tapes	12	6	Neg	10	16	2	25	76	7	4	20	2	3	41	4	6	411	41	60	573	56
108. Tool tips	2	1	Neg	-	-	-	-	-	-	-	-	-	-	-	-	3	1005	201	5	1006	201
109. Wire ropes	3	2	Neg	-	-	-	3	12	1	1	8	Neg	1	34	3	10	1670	167	20	1726	171
110. Carbon black	1	1	-	-	-	-	1	3	Neg	-	-	-	-	-	-	3	2440	244	5	2444	244
111 Rubber processing meteriels	4	Neg	Neg	-	-	-	1	3	Neg	1	9	Neg	-	-	-	5	1210	121	11	1222	121
112. Permanent magnets	1	Neg	Neg	-	-	-	1	4	1	-	-	-	-	-	-	2	222	56	4	226	57
113. Graphite electrodes	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2	1047	157	2	1047	157
Grand total :	15399	6008	965	2202	3217	431	2553	8359	1340	1656	11286	1721	947	11773	1650	5513	1395452	220859	28270	1436095	226866

Note: (i) Data for tobacco and tobacco products, petroleum products, coffee(cured), tea(loose), cinematograph films and products covered under tariff item No.68 have been excluded.

(ii) Data for Units working under "compounded levy scheme" and those which are completely exempted from payment of duty because of any of the criteria like "power", "investment", "number of workers employed" have been excluded. However, data for units which enjoy complete or partial exemption subject to the value of their clearances or out-turn remaining within a prescribed limit and which are under effective administrative control of the Central Excise Department have been included.

(iii) The base of the data is 1975-76, except for paper and paper board and cotton fabrics in respect of which the data have been estimated for 12 months on the basis of data for the first six months of 1976-77.

(iv) Value in respect of items assessed on ad valorem basis relates to value as per Section 4 of the Central Excises and Salt Act, 1944 or tariff value wherever fixed. In respect of items assessed on specific rates of duty actual invoice value (excluding duties) wherever available, or estimated ex-factory (ex-duty) price have been shown.

SOURCE: Data furnished by Collectors of Central Excise.

APPENDIX - 18

PROFESSION TAX - SOME CONSIDERATIONS

1. Article 276 of the Constitution and Entry 60 of the State List deal with the taxes on professions, trades, callings and employment. Such taxes can be levied for the benefit of the State or a municipality, district board, local board or other authority. Article 276(2) enjoins that the tax payable in respect of any person under that Entry shall not exceed Rs. 250 per annum. However, where, before the commencement of the Constitution, there was in force in any State or municipality etc. a tax on professions exceeding Rs. 250 per annum, such tax will continue to be levied until provision to the contrary is made by law.

2. There is no definition of the term professions, trades, callings/or employment in the Constitution. Courts have ruled that: (i) profession involves the idea of an occupation requiring either purely intellectual skill or any manual skill, as in painting and sculpture or surgery, skill controlled by the intellectual skill of the operator as distinguished from an operation which is substantially the production or sale or arrangements for the production or sale of commodities; (ii) the word "vocation" is analogous to "calling", meaning the way in which a man passes his life. A practice of religion may amount to a vocation and politics may be a profession; (iii) trade is not only in the etymological or dictionary sense, but in legal usage, a term of the widest scope; it may mean the occupation of a small shop-keeper equally with that of a commercial magnate and may also mean a skilled craft.

3. According to Concise Oxfor Dictionary, employment means 'one's regular trade or profession.'

4. The Local Finance Enquiry Committee, 1951 and the Committee of Ministers constituted by the Central Council of Local Self-Government (which submitted its report in 1963 regarding augmentation of financial resources of Urban Local Bodies) had made the following recommendations in the field of Profession Taxes:

(1) Local Finance Enquiry Committee

"PROFESSION TAX'

49. Government should advise local bodies to revise their schedules of profession tax so as to correspond to the limit permitted by the Constitution.

(Para 498)

50. We consider that the present limit of Rs. 250 in the Constitution is very low and should be raised to Rs. 1000.

(Para 512)

51. Where the municipal or local board Acts do not contain any provision for the levy of profession tax, such provision should be made. We are, however, not in favour of the tax being made compulsory in the case of all local bodies. It

may be possible in the case of many local bodies raise sufficient funds by the levy of octroi and house tax. In such cases it may not be necessary to compel the local bodies to levy a profession tax. We recommend the compulsory levy of profession tax under the orders of the State Government only in cases where only one of the other taxes, namely, house tax or octroi or terminal tax is being levied.

52. The basis of actual income would be the ideal one, but in view of the very great practical difficulties in the way of its adoption, we recommend that local bodies should have the choice to adopt all or any of several basis according to their convenience.

(Para 514)

53. The assessment and collection of profession tax should be done by the municipalities themselves, but they should not have the power to call for accounts."

(2) Committee of Local Self-Government Ministers (1963)

5) The maximum limit of profession tax in the case of an individual should be raised from Rs. 250 to Rs. 500 and in the case of companies to Rs. 2000 by suitably amending the Article 276 of the Constitution. The levy of profession tax should be made obligatory.

5. The Government of West Bengal have submitted in its memorandum to the Indirect Taxation Enquiry Committee that the Constitutional limit of Rs. 250 under Article 276(2) should be raised to Rs. 1000 so as to improve the resource base of local bodies.

6. The Government of Assam feel that the tax is not elastic. It can be made so only if more employment opportunities are generated, and trades, industries, agriculture, etc. are developed.

7. The tax was abolished in Punjab and Haryana with effect from 1st April, 1967. The levy is, however, in force in the Union Territory of Chandigarh. The Union Territory Administration has reported that with the abolition of Profession Tax in the neighbouring States of Punjab and Haryana, officers of these two Governments posted at Chandigarh are adversely affected by the levy. However, the levy has been struck down with effect from 1.11.1966 by the Punjab High Court on the ground that the receipts from this tax are credited to the Consolidated Fund of India and as such the test laid down in Article 276 of the Constitution for such a levy, namely, that it should be for the benefit of the State/municipality etc. is not fulfilled. The Chandigarh Administration is in appeal to the Supreme Court.

8. The basis of levy of profession tax can be a classification of the assessees according to profession or income or both. The practice differs from State to State.

9. In West Bengal, the yield from this tax within the limits of the Calcutta Municipal Corporation was Rs. 90.79 lakhs for financial year 1975-76. The number of assessees is 187200 (approximately). Trades are assessed either on rental or paid up capital basis and not on return or income basis.

10. The Corporation of Calcutta also continues to levy under the proviso to Article 276(2) of the Constitution a tax at the rate of Rs. 500 per year only from companies with a paid up capital of Rs. 20 lakhs or more. Whilst adopting the rental basis, different rates of profession tax are levied depending upon the amount of rent paid by the person exercising the profession. For this purpose, the monthly rent paid is subdivided into five categories. For each category, a different amount of profession tax is fixed. The tax ranges from Rs. 25 to Rs. 250. Doctors, lawyers, brokers, etc. are assessed with reference to income (Gross annual income of not less than Rs. 10000, annual income of Rs. 5000 and above, and annual income below Rs. 5000. The respective tax amounts payable are Rs. 250, Rs. 200 and Rs. 50). There is no tax on the salaried class.

11. Municipalities and other local bodies in West Bengal also levy this tax and they also follow the above principles.

12. The Maharashtra State Tax on Professions, Trades, Callings and Employments Act, 1975 came into force with effect from 1.4.1975. The tax, which was earlier levied by local bodies etc. has since been taken over for being levied by the State Government. The village panchayats have, however, been left undisturbed. The responsibility for collection of the tax from salary and wage earners has been placed upon the employers who are required to get themselves registered, collect the tax from the employees, pay it into the treasury and file a return by the due date. As regards professions, trades and callings, the responsibility has been fixed on the person in the particular profession, etc. and he has to get himself enrolled and pay the tax in time. The local bodies, such as corporations, municipal councils and zilla parishads, and some Government officers have been entrusted with the work of collection of tax in regard to specified classes of assessees. In so far as the quantum of tax is concerned, it varies from Rs. 2 per month to Rs. 20 per month in different salary slabs, ranging from Rs. 400 to Rs. 1500 and beyond per month. Salaried employees and wage earners earning less than Rs. 400 are exempted from payment of the tax.

13. The tax extends to legal practitioners, medical practitioners including consultants, technical and professional consultants, architects, accountants, etc. In such cases the quantum of tax is fixed with reference to the number of years of standing in their particular professions, and varies from Rs. 150 per annum to Rs. 250 per annum. For dealers registered under the Bombay Sales Tax Act, the tax varies from Rs. 50 to Rs. 250 depending upon the turnover. The owners of oil pumps and service stations, foreign liquor vendors and hoteliers pay a flat rate of Rs. 250 per annum.

14. Barring the salaried class, liability to tax on other assessees is determined either with reference to turnover, standing in profession, number of workers employed, number of vehicles used, etc. or a flat rate as in the case of companies, firms, hoteliers, etc. A variation in rates exists between corporation areas and other areas in the State only in respect of money-lenders and co-operative societies. There is also a residuary class of assessees who are required to pay Rs. 150 per annum provided a notification is issued in respect of them.

15. There is no comprehensive tax on trade, professions, callings and employments in Tamil Nadu. However, profession tax in a limited way is levied by all the local bodies, namely, corporations, municipalities and panchayats. The tax in general covers all persons exercising any profession, art, or calling and transacting business or holding any private or public employment. Exemptions are, however, given in some cases on the basis of income and persons earning below

Rs. 3600 per annum have been exempted in the Madras Corporation area while persons earning below Rs. 600 are exempted from this levy in other areas. The rates of profession tax vary from place to place depending on the basis of half-yearly income. The half-yearly rate of tax varies from Rs. 9 to Rs. 125 in respect of the Corporation and Rs. 0.50/1.00 to Rs. 100/125 in respect of Panchayats and Municipalities. The revenue from profession tax during 1975-76 was Rs. 184.46 lakhs (approximately).

16. It will be convenient to broadly classify the issues arising for consideration as below:

A - Does adequate justification exist to increase the ceiling fixed by Article 276(2)?

B - Within the existing framework under which this tax operates, can some areas be identified for bringing about a measure of uniformity?

17. Before taking a final decision, the following aspects can be kept in view:

A. INCREASE IN THE CEILING

(i) As there is a fall in the value of the rupee since the existing ceiling was fixed, it could be argued that the limit requires to be revised upwards. However, as we have indicated earlier, the flaw in this argument is that in the absence of a proper incidence study, it will not be possible to assess the impact of this tax on various income groups. The tendency may also be to impose the increased burden on the fixed income groups, as they are capable of easy identification. There is also no information as to (i) the cost of collection incurred by State Governments and local bodies and (ii) the extent of evasion.

(ii) If the ceiling were to be increased, it will hit the salary earners in another way. There will be a further erosion in their carry-home pay. Prior to 1974, profession taxes were being allowed as a deduction for income tax purposes against salary income. The Income tax law was amended in 1974 whereby the deduction got merged in the overall deduction now being allowed as incidental to employment. (At present a salaried employee is entitled to a general deduction upto Rs. 3500 on a graded basis.) When the overall deduction was fixed at Rs. 3500, due note was taken of the fact that the profession tax limit was Rs. 250. If the ceiling of profession tax were to be raised, it would only be equitable to make corresponding adjustments in the Income tax Act to the figure of Rs. 3500 as well as the percentages of deduction. If this is not done, the impact on the fixed income groups will be adverse.

(iii) Even as at present, profession tax is allowed as a deduction against business income, etc. Consequently, any increase in the collections from profession tax as a result of the increase in the ceiling will be partly offset by the reduction in the income tax reverues which are also divisible with the States. However, the corporation tax is not divisible. There will, therefore, be a diminition of the corporation tax revenues accruing to the Centre.

(iv) The effect of the increase in profession tax will be directly felt by the small traders, artisans and other professionals.

(v) Reliable statistics about the collections from profession tax are not available with the State Governments. Most of the State Governments have not been able to supply them. Consequently, it is very difficult to make any reliable estimate of additional revenue if the rates were

revised or if the ceiling prescribed by the Constitution were to be enhanced. It is desirable to constitute special cells who can collect statistics, profession-wise and trade-wise, so that there is a firm foundation for evolving policies. In this context, the following recommendation made by the Committee of Ministers constituted by the Central Council of Local Self-Government (November 1963) is reiterated.

> "There should be proper coordination between the municipal authorities and the income tax authorities, so that if any information on this behalf is required by the local bodies, the Income Tax Department should supply the same. In Corporation cities, the profession tax may even be collected through the Income Tax Department in accordance with a settled procedure and the proceeds may be handed over to the Corporation after deducting, if necessary, a nominal collection charge."

(vi) If a tax on services were to be imposed, it would more or less have an identical spectrum. The levy on services would be collected at certain stipulated percentages of the gross earnings/turnover, etc. As and when such a tax is imposed, it will become necessary on the analogy of similar provisions in the Estate Duty Act — for grant of credit of gift tax and probate fees not exceeding the Estate duty payable — to give credit for profession tax. In that event the accretion to revenue by the increase in the ceiling of the profession tax is not likely to be considerable.

(vii) In the absence of supporting statistics, which some of the State Governments who have sent replies have said it will be difficult to furnish, it will be difficult to make any recommendation as to whether a case exists for increasing the ceiling. Before the ceiling is increased it is necessary to precede it by incidence studies, as also by a clear appraisal of the cost of collection, extent of evasion and about the existence of a proper machinery for enforcement. It is therefore difficult to take any positive view in this matter. It may, however, be pointed out that the same kind of reasoning could be applied to argue for a rise in the exemption limit, as has been done in the case of income-tax.

B. UNIFORMITY

(i) In Maharashtra, the levy is made by the State. In other States, municipalities and local bodies levy it. If the law made by the State prescribes the criteria and the ceilings, that will pave the way for some uniformity. The actual levy could be left to the concerned local authority.

(ii) The basis on which profession tax could be levied is varied. It can be either with reference to income or with reference to a classification based on profession. As we saw, in some States the rental paid to the premises where the profession, etc. is carried on is taken as the basis. The local bodies should have the choice to adopt any reasonable basis for the levy of profession tax. However, there should be some uniformity in the matter of classification and the rates of tax imposed. As of now, wide divergences exist in this regard. For example, in West Bengal, the keeper of an unsophisticated hair dressing saloon is levied profession tax on the basis of the rental the saloon pays for its premises. In Bombay, the saloons fall within the Shops and Establishments Act and the tax varies according to the number of workers. There should be some uniformity in the selection of criteria. Whilst no absolute sanctity can be attached to any one of the criteria, a deciding factor could be the income test. For example, a saloon situated within Corporation limits may not have a large number of workers. It may, however, have sophisticated equipment. In such an event, the level of income will be maintained as in places specialising in

coiiteurs, despite the fact that the number of workers is not large. In other words, there should be a blend of considerations like location, income and number of workers in making classifications for the purpose of the levy.

(iii) The responsibility for collection of tax from salary and wage earners is fastened upon the employers in Maharashtra. This is not the position in other States.* The procedure adopted in Maharashtra will make the collection easy.

(iv) Salary earners are not liable to profession tax in West Bengal. In Maharashtra, all salaried employees and wage earners are liable to profession tax. Only persons earning a gross income below Rs.400 per month are exempted. It is desirable to have some uniformity.

(v) No distinction is generally made between the area falling within the limits of a corporation and other areas for the levy of this tax. The distinction between a corporation, municipality and village panchayat is a well defined one. In structuring the tax, this distinction has to be kept in view. For example, in the case of money-lenders, the tax rates in Maharashtra are different for those within the corporation areas, whilst it is less for those in other areas. This differential need not, however, be applied to juristic persons, like companies, firms, etc.

(vi) Suitable follow up action will have to be taken after the judgment of the Supreme Court is available against the judgment of Punjab and Haryana High Court, in the case of Madan Tarlok Singh & Others Vs. The Union of India, holding that as the revenue from profession tax is credited to the Consolidated Fund of India in respect of Union Territories, the tests laid down in Article 276 that it is for the benefit of the State, municipality etc. is not satisfied. Otherwise it may become difficult to levy profession tax in Union Territories, if some of them decide to do so.

APPENDIX 19

CERTAIN FEATURES OF VAT IN OPERATION IN EUROPEAN AND OTHER COUNTRIES

To study the feasibility of introducing VAT in India, the Secretariat tried to collect material about its working in other countries from various sources including the local Embassies but not much information was forthcoming. Most of the information which could be gathered was in a language other than English. It was, accordingly, decided to seek the assistance of our Embassies abroad. Indian Ambassadors in about 25 countries, where some form of VAT was understood to be operating, were addressed and requested to send information on various aspects of VAT. A detailed questionnaire was also forwarded in this regard (Schedule 1).

2. Replies were received from a number of countries some of which were quite comprehensive. Schedule 2 gives in a summary form the information received on certain important aspects of VAT as operating in Denmark, West Germany, Netherlands, Luxembourg, Ireland, Belgium, Italy, Austria, Chile and Argentina.

3. Schedule 3 gives certain basic features of VAT (collected from different sources) as operating in Brazil - at State and Federal levels.

4. For small tax payers special schemes have been devised in countries where VAT is operating - forfait arrangement being one of the most widely used. Schedule 4 outlines certain features of this scheme.

SCHEDULE 1

QUESTIONNAIRE ISSUED TO INDIAN EMBASSIES ELICITING INFORMATION ON VARIOUS ASPECTS OF VAT

(1) TAXATION POWERS

Allocation of powers of taxation by Constitution or otherwise between Centre, States and local municipalities, if any. (Please indicate the exact legal/constitutional provisions).

(2) GENERAL

(i) The year when it was decided to introduce VAT and the intention made public.

(ii) Actual date of introduction of VAT.

(iii) Basic reasons for the adoption of VAT - whether based upon any Committee's recommendations and if so, the gist of the recommendations.

(iv) What tax system was replaced by VAT - that is, whether sales taxes/turnover taxes, excises on manufactured goods or taxes on services etc.

(v) Whether VAT also used to substitute or reduce corporate taxes?

(vi) Stage upto which VAT introduced-

- (a) manufacturers' level,
- (b) wholesalers' level,
- (c) retailers' level.

In case VAT restricted upto manufacturers'/wholesellers' level, whether any taxes are levied at wholesale/retail level on commodities subject to VAT - if so, the authorities levying such taxes.

(vii) Treatment of services - whether not covered or covered in general? In the latter case, what services are exempt from VAT liability? If only selected services are taxed under VAT - the list of such services.

(viii) What type of public education was conducted and official guidance given to assessees/ Departmental officials before the introduction of VAT?

(3) RATE STRUCTURE

(i) The VAT rate(s) applicable at the time of introduction.

(ii) Major changes in the VAT rate structure made thereafter. Please indicate the details of commodities and services subject to and covered under different rate categories, if there is a multiple rate structure.

(iii) The list of commodities which are completely exempt from VAT -

- (a) where refund of VAT paid on inputs is available; and
- (b) Where no such refund is permissible.

Please also indicate, if possible, the basic rationale for such exemptions.

(4) MANNER OF ASSESSMENT

(i) Whether tax credit or other methods are used for calculating VAT liability?

(ii) The periodicity of tax payments and submission of returns - whether monthly, quarterly or yearly.

(iii) How the tax liability is worked out, if some of the supplies of a VAT licensee are exempt from VAT?

(5) TREATMENT OF SMALL SCALE SECTOR

Please indicate the taxation provisions relating to small scale sector somewhat in detail as they would be of special interest. It should, inter alia, indicate:

(i) Whether units upto certain out-turn are exempt from VAT liability - if so, the value limits.

(ii) Whether there is any other system of payment of taxes for certain category of smaller producer e.g. contract/forfait/compounded basis?

(iii) Is there any provision for mitigation of VAT paid on inputs used by a smaller producer not working under VAT, when his goods are sold to a manufacturer/wholesaler/retailer working under VAT? Whether any credit (on notional or other basis) allowed - if so, the basis thereof.

(iv) In what manner the rigours of usual VAT formalities have been relaxed for smaller producers?

(6) TREATMENT OF INVESTMENT GOODS AND LIMITATIONS ON USE OF TAX CREDITS.

(i) Whether rebate/tax credit of VAT allowed in respect of all investment goods or for certain categories no such deductions are permissible? Please indicate the exceptions.

(ii) Whether there are any limitations on the use or refund of credits of tax either borne or paid at earlier stages on inputs including investment goods.

(7) ADDITIONAL INDIRECT TAXES -

Whether certain commodities, subject to VAT or otherwise are subject to any other indirect additional tax (like traditional excises) along with or in lieu of VAT? If so, please give the list of such commodities and the rates of indirect taxes at present in force. Please indicate specifically all the taxes levied on petroleum products (e.g. Motor spirit, Kerosene, HSD, Furnace Oil etc.), Electricity and Coal.

(8) DOCUMENTATION

Essential features of statutory records required to be maintained and invoices issued by

(a) manufacturers;
(b) wholesalers; and
(c) retailers.

Specimen copies of invoices and other such records/returns (in English version) may please be enclosed.

(9) DATA COMPILATION AND CHECKS

Please give a brief note on the system of data compilation and checks of various returns and documents including the extent of use of computers. Also indicate the provision in the system to check/detect evasion including the role of physical verification by revenue officers.

(10) IMPACT ON PRICES

Whether any assessment of the impact of VAT on general level of prices was made after the introduction of VAT and if so, the extent of price rise attributed to VAT?

(11) MAJOR PROBLEMS

Please indicate in brief, the major administrative problems or problems of technical nature (such as those relating to valuation, assessment of goods and services, etc), faced after the introduction of VAT and the way solutions found out to these problems.

(12) ADMINISTRATIVE BURDEN

(i) Approximate number of licensees -

(a) under tax net before the introduction of VAT substituting certain indirect taxes;

(b) working under VAT;

(c) out of units in (b) above, please also indicate the number of bigger licensees which contribute major part (say about 90%) of the yield from VAT.

(ii) Approximate number of small scale licensees not working under VAT but paying taxes on compounded or other basis.

(iii) Estimated cost of collection (as percentage of total revenue collection) in respect of indirect taxes replaced by VAT vis-a-vis estimated cost of collection for VAT.

(13) REVENUE STATISTICS

Please furnish the detailed revenue statistics, for the last available financial year, from all indirect and direct taxes - broken up tax-wise, such as income-tax, corporate tax, VAT, excises, tax on services (if levied separately) etc.

(14) REVIEW OF WORKING

Please indicate, if any official review of the working of VAT made after its introduction - if so, the major findings, the changes recommended and action taken thereon.

SCHEDULE 2

(PRINCIPAL FEATURES OF VAT IN CERTAIN COUNTRIES)

BASIC REASONS FOR THE ADOPTION OF VAT - WHETHER BASED UPON ANY COMMITTEE'S RECOMMENDATIONS AND IF SO, THE GIST OF THE RECOMMENDATIONS

GIST OF INFORMATION

The following were the main considerations for adopting VAT:

(a) Redistribution of the tax burden with the social aim of redistributing income not only at a personal but at an original level.

(b) Rationalisation and systematization of the tax regime in order to provide contributors with appropriate and simplified means for the fulfilment of their fiscal duties, where certainty must be the guiding rule to exclude any arbitrariness, at the same time enabling a controllable fiscal regime.

(c) Harmonization of Central and local jurisdictional tributary system.

International trends in turnover taxation as well as translucence of the VAT system.

The factor bearing on the Government's decision to introduce VAT was Ireland's application for membership of the EEC. Membership involved the adoption of a value-added tax system on the lines laid down in EEC Directives. Another reason was that VAT was a more flexible form of turnover taxation than the existing system and could be used to provide a system of indirect taxation with progressive characteristics.

Italy, France, Germany, Holland and Luxembourg decided to introduce it by the Treaty of Rome in 1956. The basic reason was to eliminate customs barriers to create a system of same price of all items in the markets of all these countries. It was, therefore, decided to replace all commodity taxes levied by one tax called the added value tax (IVA or VAT).

Second Directive of the EEC was the main reason for adoption of VAT by Luxembourg.

Netherlands

The basic reason for the introduction of VAT in Netherlands was the EEC decision to adopt the value-added tax as the common system of turnover tax; in addition it was felt that the value added tax was also preferable from a national point of view in that VAT can be considered as neutral, both with respect to the tax burden on imports, and exports (exports can be wholly exempt from domestic turnover tax so that tax is imposed only in the country of destination, and imports can be subjected to tax at the frontier at exactly the same rate as domestic products) as well as with respect to the internal economy (the former multiple stage cumulative turnover tax was favouring integrated concerns and hampered specialization, because transactions within a concern were normally tax free).

West Germany

Before the introduction of VAT in the FRG, there was the so-called All-Phase-Gross-Turnover Tax. This tax system had many defects. This was because of the cumulative effect emanating from this system; the gross turnover tax was basically levied on the full price at every stage of economic transaction. The result was a differentiating tax burden on commodities, according to the intermediary stages which had to be covered till they reached the consumer. The undertakings, therefore, tried to reduce the tax burden on their products by combining the various intermediary stages. For example, a shoe factory avoided the whole-sale and retail trade in as much as they sold their products in their shops directly to the consumers. This development could no longer be tolerated, specially because of the effect of concentration in the industrial sector and the resultant disturbances in the competition, to the disadvantage of small and medium undertakings, Moreover, an exact customs equilisation (refund on exports) was not possible in the old system of turnover tax. With the help of VAT these defects of the gross-turnover tax were sought to be eliminated.

From 1959 the Federal Minister for Finance had entrusted to various committees, comprising of taxation experts, the work of enquiring into a reform of the Gross Turnover tax. The Experts Committee, in the Federal Ministry of Finance, dealing with this question last suggested in the year 1962, introduction of a Value Added Tax, with pre-sale deduction.

Chile

Main reasons for adopting VAT were to remove the distortions of the earlier purchase and sales taxes and to ensure its uniformity and lesser chances of tax evasion.

	2. THE YEAR WHEN IT WAS DECIDED TO INTRODUCE VAT AND THE INTENTION MADE PUBLIC.	3. ACTUAL DATE OF INTRODUCTION OF VAT.
Argentina	1974	1.1.1975
Austria	1969	1.1.1973
Belgium	1967	1.1.1971
Denmark	31.3.1967	3.7.1967
Ireland	The decision to introduce VAT was announced by the Government in July, 1970. This decision was preceded by a survey of various types of sales tax systems in other countries and the results of the survey were published by the government in June, 1968 in a White paper entitled "Added-Value Tax" without any decision in favour or against the VAT.	1.11.1972
Italy	1956	1.1.1973
Luxembourg	1968	1.1.1970
Netherlands	On April 14, 1966 a first announcement was made by the government concerning the implications of the forthcoming tax harmonization within the European Communities, including the introduction of VAT as the common turnover tax system. The draft bill to introduce VAT was presented to Parliament on October 4, 1967.	1.1.1969
West Germany	The thinking on VAT originated in FRG in 1951 when a serious discussion started on the abolition of the gross turnover tax. In suceeding years a number of recommendations and drafts by parliamentarians and scholars were prepared. In 1963 the first draft of a VAT was presented in the legislature, but it could not go through due to expiry of its term. In the subsequent term of the legislature it was taken up again and finally decision to adopt VAT was taken in 1967.	1.1.1968

4. WHAT TAX SYSTEM WAS REPLACED BY VAT - WHETHER SALES TAXES/ TURNOVER TAXES, EXCISES ON MANUFACTURED GOODS OR TAXES ON SERVICES ETC.

Argentina	Sales taxes.
Austria	Usual turnover tax at the rate of 5%
Belgium	VAT replaced Belgium Purchase tax which was a complicated one having as many as 30 multiple rates.
Chile	VAT replaced purchase and Sales taxes.
Ireland	Turnover taxes ("turnover tax" and "wholesale tax").
Italy	IGE tax (general tax on exchanges). It was the only tax levied on goods and services before IVA was introduced.
Luxembourg	Multiple stage turnover tax.
Netherlands	Multiple stage turnover tax, under which all transaction (goods and services) between primary producer, manufacturer, wholesaler, retailer and consumer were subject to turnover tax at various (low) rates, except that sales of goods by a retailer to consumers were exempt.
West Germany	All phase gross turnover tax, which was levied at all stages of economic transactions. This was applicable to commodities and services.

5. WHETHER VAT ALSO USED TO SUBSTITUTE OR REDUCE CORPORATE TAXES

None of the countries have used VAT for this purpose.

6. STAGE UPTO WHICH VAT INTRODUCED - (a) MANUFACTURERS' LEVEL (b) WHOLESALERS' LEVEL (c) RETAILERS' LEVEL.

All countries have VAT operating upto retail level.

7. TREATMENT OF SERVICES - WHETHER NOT COVERED OR COVERED IN GENERAL? IN THE LATTER CASE, WHAT SERVICES ARE EXEMPT FROM VAT LIABILITY? IF ONLY SELECTED SERVICES ARE TAXED UNDER VAT - THE LIST OF SUCH SERVICES.

Argentina	Encumbered services are covered taxably. The taxed services are listed (adjoined to Act No. 20.631).
Belgium	Services are covered by VAT with exemptions for professional, recreational, educational and cultural types.

Chile — Services are covered in general. Some services exempted from VAT are: water, electricity, gas, oil, transport of passengers, post office and telegraphic services, hospitals, national services of health. Some of these are levied to a special kind of tax in place of VAT.

Ireland — Services in general are within the VAT system. Some of the exempt services are supply of stocks shares and other securities, delivery of water by local authorities, professional services of medical or educational nature rendered by hospitals, schools etc, services of solicitors, accountants, actuaries, veterinary surgeons, barristers, banking and insurance etc.

Italy — All services are covered by IVA.

Luxembourg — VAT covers services in general. Banking services, insurance services and doctors services are exempt from VAT.

Netherlands — VAT applies, in principle, to all types of services. However, certain services are exempt (without credit for VAT paid by the entrepreneur rendering the services) whereas some other services are zero-rated (i.e., exempt with credit for VAT paid by the entrepreneur). Some examples of exempt services (without credit are: services rendered by doctors, midwives, nurses, dentists, ambulances, etc.: most services rendered by banks, insurance, postal, telephone and telegraph services, radio and television broadcasts (except commercials) and services in the field of arts and social care, and education.

West Germany — Basically all services are covered by VAT.

Exceptions: Granting of Credit, renting plots (with exceptions), services of doctors and other services connected with curing of diseases, services of statutory social insurances, services of most of hospitals and homes for old people, services of welfare associations, services of private schools, theatre, crohestra, museums, zoos as well as institutions for the promotion of young people.

For the services of independent occupations (e.g., solicitors, taxation consultants, auditors etc.) reduced tax rate is applicable. Besides, certain services in the sector of Copy Rights are taxed at reduced rates. Services meant for foreign countries are exempt.

8. THE VAT RATE(S) APPLICABLE AT THE TIME OF INTRODUCTION

Argentina — At the time of introduction two rates were established, a general one, 13%, and a discriminating one, 21%.

Austria — The introductory rates had been 16% for general purposes, 8% for all energy supplies (petrol, electricity, heating oils etc), food and agricultural products, cultural services and 6% for small farms upto a land value of ASch. 600, 000/-.

Belgium	Original law provided 4 rates: 25%, 20%, 15% and 16%.
Chile	20% for goods. At first some services only paid 8%. Others did not pay anything.
Denmark	10%
Ireland	Zero, 5.26%, 16.37% and 30.26%.
Italy	Varying from 6% to 18%
Luxembourg	Two rates i.e. 8% and 4%, - the former being for luxury and semi-luxury items.
Netherlands	At the time of introduction in June, 1968, there was a general rate of 12%, a reduced rate of 4% and zero-rate (with limited application). Moreover, a number of services were exempt (without credit for input tax).
West Germany	At the time of introduction of VAT on the 1st January, 1968 the general tax rate was 10% and the reduced rate 5%.

9. MAJOR CHANGES IN THE VAT RATE STRUCTURE

Argentina	It is now a uniform 16% rate.
Austria	A major change in rate structure took place on 1.1.1976 when the general rate was raised to 18%. Others originally taxed at 6% or 8% were made liable to uniform 8%.
Belgium	The current rates are 25%, 18%, 14% and 6%. These rates are in operation since 1971. Newspapers are exempt with credit for input taxes.
Chile	The tax is uniform 20% but for some exempt services.
Denmark	On 1st April, 1968 raised to 12.5% and on 21st June, 1970 raised to 15%. Due to the overall economic recession in Denmark, VAT was lowered to 9.25% from 29.9.1975 until 29.2.1976, after which period it was raised to 15% again. Ships, aeroplanes and newspapers are exempt.
Ireland	Food, oral medicines, clothing and certain fuel became liable at the zero rate after the introduction of VAT.
Italy	Presently it is varying from 3% to 25%.
Luxembourg	These rates were stepped up in 1973-74 to 15% and 10% at which level they stand currently. On certain food items a very low (2%) rate of tax is charged.

Netherlands — Increases in the general rate to 14% as of January 1, 1971, to 16% as of January 1, 1973 and to 18% as of October 1, 1976. In addition, certain goods (for example electricity) were moved from the 4% rate to the general rate. The reduced rate of 4 per cent has not been changed.

West Germany — As from 1.7.1968, the tax rates were raised to 11% and 5.5%. The Federal Parliament is presently discussing the question of increasing the rates to 12% and 6%.

10. COMMODITIES, SUBJECT TO OTHER INDIRECT ADDITIONAL TAX (LIKE TRADITIONAL EXCISES) ALONG WITH OR IN LIEU OF VAT. LIST OF SUCH COMMODITIES AND THE RATES OF INDIRECT TAXES AT PRESENT IN FORCE.

Austria — An additional 10% (before VAT) is levied on all alcoholic drinks which is shared between the Central and the State (Provincial) Governments. (The ratio being 84:16). In addition to this "alcohol tax" all municipal administrations are entitled to levy also 10% on all drinks, including non-alcohlic refreshments.

Belgium — In addition to VAT, there are some minor excise taxes levied on beer, alcoholic beverages, cigarettes and sugar.

Denmark — For financial and political reasons, a special purchase tax is imposed on wine, spirits, car, radio and TV appliances. The VAT is calculated on these goods on the following basis:-

Import price, plus duty plus special purchase tax. On the total of that VAT is calculated.

Ireland — Excise duty is chargeable on the following goods in addition to VAT:

(i) Bear, Cider or Perry, Wine, Table Waters, (ii) Matches, (iii) Petroleum products, (iv) Perfumes, (v) Tobacco, (vi) Passenger motor vehicles with a capacity of less than 16 persons, (vii) Other motor vehicles and (viii) Tyres.

Italy — Nil.

Luxembourg — Small excise duty is levied on special items like spirits, beer, imported wines, tobacco and sugar.

Netherlands — Passenger cars are subject to a special car tax in addition to VAT, in order to compensate for the abolition of the luxury rate of turnover tax imposed on such cars under the former multiple stage turnover tax. The rate of this tax is currently 16 per cent for cars with a list price not exceeding Hfl. 10, 000; this tax is computed on the list price reduced by the amount of VAT (18 per cent) included in such list price.

A succinct survey of the various excise duties are as follows:

i) beer: between Hfl. 17.56 and Hfl. 34.62 per 100 litres;

ii) soft drinks: Lemonades: Hfl. 14.50 per 100 litres; Mineral waters: Hfl. 7.25 per 100 litres;

iii) sugar: Hfl. 4.34 per 100 Kilogrammes;

iv) wine: approx. Hfl. 85, _____per 100 litres

v) other alcoholic beverages:
Hfl. 2100 per 100 litres of 100 per cent strength;

vi) tobacco:

(i) Cigarettes 52.3% of retail sales price, plus Hfl. 2, per 1000 (aggregate minimum tax Hfl. 34.43 per 1000)

(ii) Cigars 8.43% or 14.43% of retail sales price, according to size.

(iii) Pipe tobacco and other tobacco — 28.43%, 34.43% or 35.83% of retail sales price, according to price.

West Germany

The products listed in the following Table are, in addition to VAT, subject to special consumption (excise) duty, which is applicable on a federal level. The excise duties are administered by the Federal Finance Authorities. The tax revenues (except duty on beer) belong to the Federal Government. The tax revenues from beer go to State Governments. There are no excise duties for electricity and coal. (However, electricity has an equalisation levy).

Description	Rates of duties
1. Tobacco duty	
Tobacco products	There are different rates of duty for individual products. The most important are: Cigarettes 4.92 pf./pce. +24.3% of the retail price Cigars – (minimum retail price 12.5%p..., pce. 18.58% of the retail price minimum 2.6 pf./pce; -Smoking tobacco: a) fine (minimum retail price DM 34/Kg. 4.70 DM/Kg. +18.27% of the retail price, minimum DM 11.90/Kg. b) Pipe tobacco: DM1.30/Kg. +16.97% of the retail price, minimum DM 7.30/Kg. The retail price – the basis of proportional tobacco duty or its proportional share – is decided by the manufacturers and importers

	Description	Rates of duties
West Germany (Cont'd)	2. Duty on Coffee	
	Raw coffee, roasted coffee, coffee extracts and essences; certain products having content of coffee, duty is levied proportionally for the portion of coffee contained.	The most important rates of duty are - for raw coffee, not freed of caffeine DM 3.60 per Kg. - for roasted coffee, not freed of caffeine DM 4.50 per Kg. - for coffee extracts not freed of caffeine DM 10.80 per Kg.
	3. Duty on Tea	
	Tea of Tariff Nr. 09.02 as well as tea extracts and essences, certain imported products having content of tea.	There are three rates of duty for tea. - for tea 4.15 DM per Kg. - for dry extracts of tea DM 10.40 per Kg. - for liquid extracts or essences of tea DM 10.40 for 1 Kg. of the dry measure contained therein.
	4. Duty on Sugar	
	Cane sugar, glucose, and sugar out of chemical combination of these kinds of sugar.	The important rates of duty are: For cane sugar powder DM 6, per 100 Kg. Duty on glucose, depending on the degree of purity: of more than 95% DM 5.40 per 100 Kg. in the case of lesser purity, DM 2.40 per 100 Kg.
	5. Duty on Salt	DM 12 per 100 Kg. of Salt. The tax burden is mainly on the consumption of common salt.
	6. Duty on Spirits Ethyl alcohol	Differing rates. Duty for 1 hectolitre ethyl alcohol: (i) for spirits, for drinking and other purposes, other than those indicated below: DM 1,950. (ii) for spirits for medical purposes by doctors and hospitals DM 1,200;

	Description	Rates of duties
West Germany (Cont'd)		(iii) for spirits for manufacture of medicaments for external application; and cosmetics, so long as the spirit is made inedible - DM 600; (iv) for spirits for the manufacture of vinegar DM 50.
7.	Duty on sparkling wine Champagne and similar drinks	The duty for a 0.75 litre bottle of champagne: DM 1.50 or DM 2 per litre of champagne. For a 0.75 litre bottle of drink similar to champagne the duty is DM 0.30 which is equivalent to DM 0.40 per litre. For smaller or bigger bottles the duty is correspondingly lower or higher.
8.	Duty on vinegar	At present the duty is DM 96.60 per Kg. [illegible] free, from water. Vinegar for industrial, technical purposes is exempt from duty.
9.	Duty on match boxes and similar articles	For 100 pcs. 1 pfg. 1 packet of "Household goods" with 10 boxes each of 50 sticks - 5 pfg.
10.	Duty on illuminants Electric bulbs and discharge lamps	Different rates of duty. Generally graded according to the different capacities of lamps.
11.	Duty on playing cards	Different rates, according to the material with which the cards are made of and the number of cards comprising a card play. The duty for pack of cards with 25 to 48 cards; varying from DM 0.30 to DM 1.50. For pack of cards with 24 or less number the duty is reduced by half and for game with more than 48 cards the duty increased by half.

		Description	Rates of duties
West Germany (Cont'd)	12.	Duty on Beer	
		Beer and similar drinks	Ranging from DM 12, to DM 15, per hectolitre. For ordinary beer, the duties are reduced by half, for drought beer by one-forth. For strong beer the rates of duty are increased by half.

Over and above the excise duties, the following taxes are raised, in place of the VAT.

a) Insurances tax while making payment of insurance premium (Rate of duty 5% of the amount).

b) Incorporation tax on first acquisition of company rights in joint stock companies or on certain services of partners. (Rate: 1% of the value consideration).

c) Sales tax on stock exchange transactions in cases of business in acquiring securities (from second acquisition). (Rate of duty according to the value of the securities, 1.2% or 2.5% of the agreed price or of the security).

d) Transfer tax while acquiring land or comparable legal transactions. (Rate of tax 7% of the purchase price or of the value of land).

e) Tax on racing, lottery etc. (Rate: $16\frac{2}{3}\%$ of the amount or of the price).

f) Tax on bill of exchange. (Rate: 15 pfenning for each DM 100, - exchange amount).

11. THE PERIODICITY OF TAX PAYMENTS AND SUBMISSION OF RETURNS - WHETHER MONTHLY QUARTERLY OR YEARLY.

Belgium	If the total annual sale is more than 10 million BFs., declaration and also payment of tax is monthly. If on the other hand total sale is less than 100 million BFs., declaration is quarterly and the payment is monthly.
Chile	Tax payments and submission of returns are done monthly.
Denmark	The VAT is paid every quarter, except in agriculture and fisheries where it is paid semi-annually.
Ireland	Two monthly.

Italy	Basic return is monthly. Each tax payer has also to submit quarterly, half yearly and annual returns.
Luxembourg	There are no exemptions from VAT and the very small enterprises having annual sales of BF 250,000 send their returns yearly; if sale is upto BF 3.5 million, the return and payment of tax is on quarterly basis while for enterprises having sales higher than BF 3.5 million, the declaration and payment of tax is on monthly basis.
Netherlands	The normal interval for submitting VAT declarations is three months, usually coinciding with the calendar quarter year. Both the tax-payer and the tax inspector, however, may insist on monthly declarations. The declaration must be sent to the inspector not later than one month after the end of the declaration period.
West Germany	The period of taxation (advance declaration period), for which the entrepreneur has to give advance notice and has to make advance notice and has to make advance payments depends on the extent of tax. If the tax liability in the previous calendar year amounted to DM 2,400, - and more, tax declaration and payments are to be made monthly. In case the tax liability in the previous calendar year is less than DM 2,400, - the tax declaration and payments are to be made on a quarterly basis. If it is expected that for the current year, tax amount will not exceed DM 600, - declarations and payments can be made annually. At the end of calendar year each tax-payer has to submit an annual tax return. After adjusting the advance payments already made, the difference in amount is either to be paid or is refunded, as the case may be.

12. HOW THE TAX LIABILITY IS WORKED OUT, IF SOME OF THE SUPPLIES OF A VAT LICENSEE ARE EXEMPT FROM VAT?

Belgium	No one is exempted from VAT.
Denmark	There is no correlation between tax liability and VAT exemption.
Ireland	Credits are calculated on the basis of the ratio which taxable turnover bears to total turnover or on any other basis agreed between a taxpayer and the Revenue Department. The latter might include apportionment by time (for computers), by area (for buildings) or by usage (for machines). Any apportionment may be reviewed and adjusted annually.
Italy	Not applicable as nothing is exempt from IVA.
Netherlands	Input VAT referable to taxable supplies (including zero-rated supplies) is creditable, whereas for input VAT paid on purchases related to both taxable and exempt supplies, a proportion of such input tax is creditable in the ratio which the amount of taxable supplies bears to the amount of exempt supplies.

West Germany — If the entrepreneur is effecting tax-free sales, deduction of prior stage tax will be limited to a certain extent.

(Note: In all countries 'Tax Credit' method is used for computing duty liability under VAT.)

13. TREATMENT OF INVESTMENT GOODS

Argentina — When it is a case of consumer goods investments the computation of the "fiscal credit" will be in three yearly consecutive quotas as from the period of validation of the goods.

Austria — There are no exceptions at present and credit is allowed for investment goods also.

Belgium — Regarding capital goods there is no complete refund of VAT. Only partial refund is allowed.

Chile — There are no rebates of any kind as regards investment goods.

Denmark — The VAT paid on all goods, including investment goods, can be deducted.

Ireland — Credit for purchases of capital goods (or indeed any other creditable goods) may be taken once the taxpayer is in receipt of the necessary invoice. Where the taxpayer carries on both taxable and exempt activities (e.g. a bank which is exempt for ordinary banking services but taxable for services such as tax advisory services, property dealings and registration of securities) the credit has to be apportioned. Credits may be apportioned on the basis of the ratio which taxable turnover bears to total turnover in the taxable period in which the credits arise, or on any other basis agreed between a taxpayer and the Revenue Commissioners. There are other basis of apportionment too. Any such apportionment may be reviewed and adjusted on the basis of annual turnover. To meet EEC requirements review and adjustment will have to cover a five year period.

West Germany — The prior tax amounts falling on investment goods can in principle be deducted to the full extent at the time of acquisition of these goods and in the event of exceeding the tax for own sales, the same can be refunded. In order to avoid transitional difficulties in the introduction of VAT system, the entire prior tax deduction for investment goods was introduced stage by stage over a period of 5 years. Thus, there was only a partial prior tax deduction, according to which the deductible share of the total pre-stage tax amounted in the 1st year 20%; 2nd year 30%; 3rd year 40%; 4th year 60%; and 5th year 80%.

14. LIMITATIONS ON THE USE OR REFUND OF CREDITS OF TAX PAID ON INPUTS.

Argentina

There is a limit according to which the tax which is discounted from the fiscal debit is the tax which, at the close of the fiscal period, would have been billed to them for purchase or final import of goods, leases and rendering of services and up to the limit of the amount which will be obtained by applying, on the total net amount of servicing, purchases or leases or, where appropriate, the total amounts of final imports, the aliquot to which those operations would have been subject at the time, or those which it is pertaining to apply to operations which are settled "whichever is the lesser".

Austria

Does not apply.

Denmark

None.

Ireland

In computing his tax liability for an accounting period a registered person is entitled to deduct the tax properly invoiced to him in respect of most goods or services purchased by him for the purposes of his taxable business. To be entitled to the deduction he must have received a proper tax invoice - he is not obliged to have paid his supplier.

2. A deduction is not allowed for tax charged on any of the following:-

(i) the provision of food, drink, accommodation or other personal services for an accountable person, his agents or employees, except to the extent that such provision constitutes a rendering of services in respect of which he is accountable;

(ii) entertainment expenses incurred by an accountable person, his agents or employees;

(iii) the acquisition (including hiring) of passenger motor vehicles otherwise than as stock-in-trade (that is, for re-sale) or for use in a vehicle hire business;

(iv) the purchase of petrol otherwise than as stock-in-trade (that is, for re-sale);

(v) goods or services connected with any activity of an accountable person which is either an exempted activity or is outside the scope of his business.

3. In the case of goods which are chargeable at the high rate (passenger motor vehicles, TV and radio sets, record players and records) the amount which may be deducted may not exceed the equivalent of the low rate of tax. This is so whether the goods are imported or purchased within the State. The only exception is for manufacturers or assemblers of such goods. These traders are normally entitled to the full deduction but they are, of course, liable for tax at the

high rate when they dispose of the goods. There is also a limitation on the amount of tax which may be deducted by a manufacturer or assembler who uses high rate goods in a hiring business.

4. A deduction or credit of tax is, of course, allowable only for goods purchased or imported for the purposes of a person's taxable business. Having regard to the restrictions at paragraph 2(iii), the deduction in the case of passenger motor vehicles, even at the restricted rate, will normally be confined to dealers in motor vehicles and vehicle hire firms. Even though a registered person may not have been entitled to any credit on the purchase of a car for use in his business he is liable for tax at the low rate on the sale of the car.

5. As stated in paragraph 2(v) no deduction of prior tax is allowable for any exempt or non-business activity. If a person carries on both a taxable and an exempt business tax on goods and services used in both activities will be apportioned and only the amount appropriate to the taxable part of the business will be deductible. The apportionment is to be made in the first instance on the basis of the relation of the turnover from taxable and exempt activities in the taxable period in which tax is borne; and it is subject to review later by reference to the full year's turnover. In certain cases the inspector of taxes may, if he considers it reasonable, accept an apportionment based on some other yardstick such as the allocation of floor space, the numbers of staff, or the usage of machines.

6. If the computation for any accounting period shows that the deductible tax exceeds the tax payable, the excess will be repaid direct to the registered person by the Collector-General. This will normally take two to three weeks from the date of receipt by the Collector-General of a VAT return form properly completed. The Collector-General may be prepared to accept monthly returns from persons, such as exporters, who are in a permanent repayment position.

Nil.

There are no such limitations.

In case the entrepreneur makes use of purchases, imports or services for tax-free sales, such of those prior tax amounts accruing on these inputs, are excluded from the deduction or refund. This is also applicable for prior tax amounts on investment goods. If only a portion of the input is used for tax-free sales, the corresponding share of the pre-stage tax is excluded from the deduction. The exclusion of prior tax deduction does not exist, if it relates to tax-free sales of the entrepreneur for export business.

15. TAX PROVISIONS RELATING TO SMALL SCALE SECTOR

Argentina — There are no exemptions on the basis of outturn or no special payment system for small entrepreneurs. However, there is no obligatory registration for certain types of contributors if the amount of operation does not surpass certain specified limits which are periodically up-dated. In that case, when a registered tax-payer sells to a non-registered contributor the tax corresponding to the latter must also be received for which a supposed added value is calculated for the non-registered one equivalent to 40% of its sale price and according to that increase the registered contributor calculates the tax and charges from his buyer. Thus, as against the 16% normal tax charged by a registered taxpayer for sales to another registered buyer he charges 6.4% additional tax when his sales are to un-registered buyers who are exempted from the provision of registration, though liable to tax on the basis of small turnover.

Austria — All small units having a turnover of Asch. 40,000 per annum are exempt from VAT. There is no other special provision for payment of tax on compounded or other basis nor there are provisions for relieving them from tax paid on inputs. There is no relaxation for smaller units if their turnover exceeds the limit stated above.

Belgium — Under the Belgium Code no one is exempted though there were transitional provisions whereunder the tax on small retailers for deliveries of goods or traders in the course of their business were levied on a standard basis in the form of equalisation tax upon deliveries of goods to them or the importation of goods by them - the tax being collected by the suppliers. The system has been abolished gradually beginning January, 1974. However, special tax arrangements exist for small enterprises having a yearly sale of less than 10 million BFs - which account for 80 to 85 per cent in terms of assessees but contribute 15 to 20 per cent by way of tax revenue.

Chile — There are no special provisions for small entrepreneurs. VAT does not make any difference regarding the size of the industry and smaller producers are not relaxed from VAT formalities.

Denmark — Companies with a turnover of less than Dkr. 5,000 are exempt from VAT liability. The number of such companies in Denmark is said to be absolutely negligible. There are no other special provisions for smaller entrepreneurs or provisions for mitigating the VAT paid on input.

Ireland — The licensees whose turnover is below certain limits are not obliged to register and account for VAT. The limits are:-

(i) £ 2,000 in a taxable period of two months for persons selling goods liable at zero and/or 10%.

(ii) £ 1,000 in a taxable period of two months for persons selling other goods.

(iii) £ 3,00 in a taxable period of two months for persons providing services.

There is no other special provision of payment of taxes for smaller producers. However, for smaller traders/producers simple account books are available.

Italy — Small scale sector is treated at par with other sectors as far as application of value added tax (called IVA) is concerned.

Luxembourg — There are no exemptions from VAT for small enterprises. However, very small enterprises having annual sale upto BF 2,50,000 are allowed to be assessed on yearly basis and they send their returns yearly. Where the total yearly sale exceeds BF. 2,50,000 but does not exceed BF 3.5 million; the enterpriser submits the return on quarterly basis and pays taxes quarterly, while for enterprises having sales higher than BF 3.5 million the declaration and payment of tax are on monthly basis.

Netherlands — The basic principle regarding the so-called "small entrepreneurs" is that they are fully liable to VAT, i.e., they must charge VAT on their sales and services so that their customers may get credit of such VAT if he is also an entrepreneur. In computing VAT liability, the small entrepreneur may credit his input tax in the usual way. However, if the amount of VAT due by the "small entrepreneurs", that is, VAT charged less creditable input tax, does not exceed Hfl 2,500 per annum, the amount due is reduced by Hfl 2,050 or the amount due, whichever is less. If the amount of tax due exceeds Hfl 2,500 but does not exceed Hfl 4,150, the amount due is reduced by the difference between Hfl 4,150 and the amount due. For example, if the amount due, apart from these special provisions, is Hfl 2,050 or less, no VAT is payable by the small entrepreneur; if the amount due would be Hfl 2,400 the amount payable is Hfl 350 (Hfl 2,400 minus Hfl 2,050); if the amount due is Hfl 3,000, his actual liability is restricted to Hfl 1,850 (Hfl 3,000 minus the difference between Hfl 4,150 and Hfl 3,000).

In this way, the reduction diminishes as the tax due increases so as to avoid a sudden transfer from exemption to tax liability. These special rules for 'small entrepreneurs' apply to individual tax payers only and do not apply to corporations and other entities. The limit for exemption and the reduced liability are expressed in terms of tax due rather than in terms of turnover.

There are no other system for payment of VAT for smaller entrepreneurs. The normal rules apply to such units as regards input tax payable. Each entrepreneurs must keep proper books of accounts which implies that a smaller unit can keep books in a more simple form than large enterprises.

West Germany — There is a special provision beyond VAT system for small undertakings whose total turnover on sales does not exceed DM 60,000. The rate of tax for these undertakings is 4% as against the standard rate of 11%. Besides, in cases where the total sales amount does not exceed DM 40,000 a basic abatement of

DM 12, 000 is granted; thereby entrepreneurs with a total sale of not more than DM 12, 000 need not have to pay any turnover tax to the Tax and Revenue Officer. A small entrepreneur does not have to show the 4% turnover tax separately in his bills/invoices and is not allowed any prior tax deduction. Alternatively, these units can, however, opt for the VAT. This optional provision is specially advantageous for such of those small entrepreneurs as are exclusively or mainly effecting sales to other undertakings.

Besides the two alternative provisions there is another provision for smaller undertakings. For groups of small entrepreneurs who are not subject to above-mentioned special provision but to normal taxation according to the VAT system, average rates can be fixed up for the calculation of deductible pre-stage tax or for the calculation of the tax payable. The average rates should lead to a tax which does not greatly deviate from the amount which would accrue without the application of the average rates. Those who take advantage of the average rates are exempt from the obligation to keep records.

16. ESSENTIAL FEATURES OF STATUTORY RECORDS REQUIRED TO BE MAINTAINED AND INVOICES ISSUED BY (a) MANUFACTURERS; (b) WHOLESALERS; and (c) RETAILERS.

Chile	There is a cash-book. Invoices are issued by "Impuestos Internos".
Denmark	The companies registered under the VAT system are obliged to keep their records and conduct their accounts in accordance with the Danish legislation and every purchase and sale must be accounted for. On the basis of the VAT paid on purchase and the VAT collected from sales, the difference plus or minus will be paid or refunded respectively.
Italy	Detailed records of purchases, investment and sales supported by relevant invoices are required to be maintained.
Netherlands	No distinction is made, in principle, between manufacturers, wholesalers or retailers. Each entrepreneur liable to VAT must keep proper records, from which his VAT liability can be computed. For small entrepreneurs the requirements are less extensive than for larger enterprises. Creditable input tax is only acceptable if shown on invoices, containing the name of the client, the amount charged and the amount of VAT charged. The charge to VAT is effected by way of self assessment. The relatively simple return forms mainly contain the amount of VAT charged by the entrepreneur and the amount of creditable input tax. The resulting net amount due must be paid to the Collector of Taxes. If the creditable input VAT exceeds the amount of VAT charged, a refund may be claimed.
West Germany	In accordance with the Fiscal code, the entrepreneurs are generally obliged to maintain records. Furthermore § 22 of UstG (Umsatzsteuergesetz- Turnover Tax Law) lays down a special obligation on the entrepreneurs to keep records

with a view to clearly indicate the turnover tax and the basis of their calculation. The entrepreneur is, however, not obliged to keep separate records of sales for purposes of taxation. He can fulfil his obligations of keeping records as per turnover tax law by maintaining books or records, which he is using for other purposes in compliance to other stipulations or maintaining on his own (for example, within the scope of sales accountancy).

The records must be maintained in such a manner that an expert third person will be able to get an idea of the business transactions within a reasonable time, specially on turnover tax due and the deductible prior-tax amounts. One should be able to follow the beginning and conclusion of business transactions. The entrepreneur has to maintain the records completely and in proper order with relevant vouchers (for example, copies of outgoing bills, incoming bills). He must keep the records for 10 years and the vouchers for 6 years.

The obligation to maintain records in terms of turnover tax law is equally applicable to all entrepreneurs. The rules may vary as may be applicable for certain entrepreneurs or groups of entrepreneur.

According to the general rules relating to obligation to maintain records the following must be indicated in the records.

1. The payment agreed upon and received by the entrepreneur for the supplies effected and other services (including the value of own consumption), separately for taxable sales and tax-free sales, and in the case of taxable sales, according to the tax rates.

2. The payment for taxable supplies received and other services as well as the values of products imported by the entrepreneur and the turnover tax amounts accruing on these sales (prior tax).

There is no obligation to keep records for services received and goods imported as well as for prior tax payments, so far as the entrepreneur is not entitled to prior tax deduction. In cases of prior tax apportionment records have to be maintained only for the deductible prior tax amounts.

Entrepreneurs in the agricultural and forestry sector are exempt from maintenance of records, so long as the average ta..ation is taken up according to § 24 UstG (Umsatzsteuergesetz).

Proof as shown by books: For a number of turnover tax concessions - for example, exemption of tax payment for export deliveries - proof is to be given by maintenance of books. Such proof is a necessary condition for these concessions. The absence of such proof or great deficiencies in the maintenance of books will lead to loss of the concessions in question.

Rendering of Accounts: The system of Value Added Tax with prior tax deduction necessitates a special regulation for the rendering of accounts. The entrepreneur, who executes taxable services, is authorised to issue bills, in which the VAT is shown separately. The entrepreneur, in cases of services to other entrepreneurs, is obliged to issue bills separately indicating the tax, if the other entrepreneurs demand this.

No specimen forms are prescribed for bills. In principle bills can be issued according to usual commercial practice. For the purpose of Turnover tax an additional column is prescribed for separately indicating the turnover tax amount in the bill.

In the case of bills for small amounts (total amount not over DM 100) instead of the tax amount, only the tax rate is to be given.

Small entrepreneurs, who, as per §19 UstG applies gross taxation, shall indicate neither the turnover tax amount nor the tax rate in their bills.

17. SYSTEM OF DATA COMPILATION AND CHECKS OF VARIOUS RETURNS AND DOCUMENTS INCLUDING THE EXTENT OF USE OF COMPUTERS. THE PROVISIONS IN THE SYSTEM TO CHECK/DETECT EVASION INCLUDING THE ROLE OF PHYSICAL VERIFICATION BY REVENUE OFFICERS.

Austria — A standing order of the Federal Finance Ministry for all revenue officers prescribes a physical verification at least every three years of the big and medium sized units. Physical checks of small units are left to the initiative and personal assessment of the revenue officer. The extent of use of computers varies from place to place and so far no records exist about it.

Belgium — Computer is being used extensively for analysing tax returns and maintaining tax statistics.

Denmark — There is a general control with registered companies, but of course, one can easily incorporate a control system in the computerised data system making the CDS point out every company deviating from the average.

Ireland — Registered persons are issued with a return form at the end of each two-monthly taxable period (Jan - Feb etc.) They are required to send the form to the Collector-General, with any tax payable, by the 19th of the following month (i.e. by 19 March for Jan/Feb). The taxpayer's calculation of his liability is checked by computer and any discrepancy in the calculation is queried with him. The returns are later sent by the Collector-General (within two months of receipt) to the inspectors of taxes who use them together with a yearly computer-produced summary of returns, to check that taxpayers are accounting for the tax properly.

Where tax on purchases made exceeds tax on sales, repayment is made by the Collector-General. About one taxpayer in four claims repayment each period. These are mainly cases who import or sell zero-rated goods or provide zero-rated services. The repayment claim is made in a prescribed return. Cheques are mostly (70%) produced by the computer. These are posted to the taxpayers within 3 weeks of receiving the claims with the exception of cases which have to be investigated by the inspectors of taxes or held up pending lodgement of overdue returns for other periods. In such cases the cheques are sent out manually. (£46 million VAT was repaid as against £175 million (net) collected in 1975)

Every registered person (with the exception of non-remitting members of groups) is issued with a return form (VAT 3). Where a return remains outstanding two reminders are sent, usually two weeks and four weeks, respectively, after the due date. If there is still no return, the tax liability is estimated, based either on the highest previous payment or on the inspector's estimation. (The estimated amount, once determined, applies to any period in default until it is revised). A notice of estimation is issued to the defaulting taxpayer (approx. two weeks after the second reminder). This is followed by a further request, if necessary, before sending the case of enforcement proceedings. If a return is received it replaces the estimate. In the larger cases, the papers are usually referred to the country registrars or Sheriffs or collection of the estimate amounts outstanding. Certain taxpayers are not suitable cases for the Country Registrars or sheriffs e.g. those with no seizeable goods or foreign companies. These cases are dealt with through the Revenue Solicitor if in default.

"Big Cases", i.e. taxpayers who pay £5,000 or more in a taxable period, are dealt with specially. If they have not paid by the due date an estimate of the tax due is made immediately (without the reminders being sent). The taxpayer is contacted on the telephone and informed of the estimate. He is also told that unless the return and tax is received within twenty-one days (the time allowed by law to appeal against the estimate on the grounds that the taxpayer is not an accountable person) the papers will be referred to the Revenue Solicitor for the institution of legal proceedings. Interest is charged at the rate of $1\frac{1}{2}$ per cent of the tax for each month or part of a month during which the tax remains unpaid. There is a minimum charge of £5. The rate, being higher than the normal overdraft rate charged by the commercial banks, is an effective deterrent against late payments, especially in the bigger cases.

Legal proceedings are also taken for failure to send in returns against taxpayers who are persistently late in making their returns or who fail to send them in. Penalties at the rate of £20 a day for every day on which a return remains outstanding are provided for in the law. About half the taxpayers send their returns without having to get a reminder. Estimates have to be made in about a third of all the cases. The amount of the estimate is calculated by reference to the previous highest tax for a taxable period or figures supplied by the local inspector.

Enforcement action has to be set in train for about 5,000 cases for each taxable period (out of 45,000). In many of these cases a letter which the sheriff or country registrar sends prior to taking action will bring in the return or payment of the estimate. The number of cases where goods are seized is relatively very few. About 72% of the tax is paid in the due month, 85% by the end of the second month, 90% by the end of the third month.

Each local inspector is schemed to visit as many cases as possible in the time available after the completion of his duties in relation to repayment claims, estimates, dubious returns, and queries, etc. from head office and traders. The schemes generally are on a geographical basis i.e. each town in a particular area is done street by street; priority being given to cases in which reliable accounts are not submitted for income tax purposes. In Dublin VAT District (which deals with 50% of the country's cases) appointments for visits are made by indoor staff three weeks in advance there-by maximising the number of visits which can be made by the outdoor officials. It is expected that this should enable each official to do at least eight visits per week.

An Audit Branch is attached to the head office of the VAT Administration in Dublin and is separate from, and independent of, the local inspectors, although, in the practical discharge of its duties, the Branch inevitably overlaps with the local inspector to some extent. Its role is countrywide and is not circumscribed by district boundaries as is local inspector. The Branch specialises mainly in the investigation of fraud in certain specific areas (e.g. building, furniture, jewellery etc.) or in certain tax areas, e.g. imports, exports, etc. Its activities are mainly self-generated. Very close liaison is kept with the VAT head office and also with the various Tax Districts; and these also generate work for the Audit Branch.

Computer auditing is used and a number of the audit officers have undergone specialised courses on Data Processing and auditing on computers.

West Germany

The processing of an advance notice and tax declaration and their evaluation are mainly done with the help of machines. For this purpose the tax and revenue officers are provided with Data Collection Centres, in which the details from the advance notices and annual declarations are transferred to the data carrier and thus ready for evaluating for ED - machines (Electronic Data Processing Computing machines). There are ED - Machines in the Central Accounting Centres, which have been set up by the State Governments for their tax and revenue officers. After evaluation, the Accounting Centres forward the necessary intimations about taxes directly to the entrepreneurs. The tax intimations will, however, be sent, if there are discrepencies from the details of the entrepreneur.

A central compilation of details of all entrepreneurs is done for statistical purposes, in every second year. For this purpose, the Accounting Centres send the data carriers with the feed-up particulars of the entrepreneurs to the State Statistical Offices. The particulars compiled by each particular state are sent to the Federal Statistical Office.

The control of tax payers is made in principle within the scope of general periodical audits, whereby tax declarations, account books and vouchers are examined. Over and above this, in special cases, turnover tax special auditing will be conducted by experts, experienced in turnover tax law. If there are indications of a tax evasion the tax preventive service is called upon.

18. PUBLIC EDUCATION CONDUCTED AND OFFICIAL GUIDANCE GIVEN TO ASSESSEES/DEPARTMENTAL OFFICIALS BEFORE THE INTRODUCTION OF VAT

Belgium	Publicity was given on radio, television, by issue of brochures and also by establishing telephone services. The Belgian Government had established separate "green telephone" service to which people could ring up and ask any clarifications about VAT. So far as officials dealing with VAT are concerned, the Belgian Government had short training programme for them.
Chile	Public education was given through conferences and other forums, publications, speeches etc.
Ireland	Public meetings were held throughout the country at which Revenue officials explained the proposed new tax. Additionally, seminars and other educational forums were conducted in conjunction with representative bodies such as chambers of commerce, and associations of manufacturers, wholesalers and retailers. Explanatory literature was produced and widely distributed. The most important of these was the booklet entitled "Guide to the Value-Added Tax" which was issued in July, 1972, four months before the tax came into operation.
Italy	Extensive courses were introduced for officers who were to apply or levy IVA. Books and other literature was brought out for public.
Luxembourg	In the initial stages, publicity was given regarding the introduction of VAT in place of Turn Over Tax through the media of radio, television, pamphlets and lectures. Symposia and discussions were also organised through chambers of commerce and trade organisations. They also had established telephone service at the Tax office to which people could ring up for clarifications.
Netherlands	Public education was carried out through advertising campaigns, a course on television, and extensive possibilities to submit questions to the tax authorities. The media of telephone answers, and publication of books/pamphlets was also used.
West Germany	Before the introduction of VAT the Federal Ministry of Finance published a booklet entitled "Mehrwertsteuerfibel" copies of which were supplied to interested entrepreneurs free of cost. This brochure contained a description of VAT, on the basis of examples. For the consumers a booklet called "Verbraucherfibel" was distributed in which the consumers were informed of the likely effects of VAT on the prices.

In addition to the Finance Administration's efforts, the individual industrial associations also had taken up the task of getting the undertakings acquainted with the new tax system. The associations had organised meetings on the subject of VAT and explained to their members the new tax through the medium of circular letters.

The local tax and Revenue officers were informed about VAT in the following manner. The Federal Ministry of Finance informed the "Oberfinanzdirektionen", who, in their turn, educated the officials of tax and revenue offices by arranging various meetings.

In addition to this, the Press had continously reported about the introduction of VAT. Also in special journals a number of articles appeared on questions relating to VAT.

19. MAJOR ADMINISTRATIVE PROBLEMS OR PROBLEMS OF TECHNICAL NATURE (SUCH AS THOSE RELATING TO VALUATION, ASSESSMENT OF GOODS AND SERVICES, ETC.) FACED AFTER THE INTRODUCTION OF VAT AND THE WAY SOLUTIONS FOUND OUT TO THESE PROBLEMS.

Austria

The major administrative problem after introduction of VAT had been the verification of relevant pre-value added tax. This was due to some confusion among the tax licensees but has been solved after a period of clarifications by the tax authorities.

Belgium

Since the VAT is charged on the real price i.e. charged to the customer, the Belgian Tax authorities do not face any problem of evaluation.

Denmark

There have been no major problems partly due to the introduction of Computerised Data System and partly due to the fact that the administration was extended with 200 employees in 1967 and partly due to the fact that Danish companies registered do submit qualified annual reports.

Ireland

Ireland's experience of a sales tax which applied right down to the retail level was of great value for administrators and traders alike in easing the introduction of VAT. There were problems, nevertheless, and the more important of these are discussed below:

(a) Multiple Rates: This gives rise to difficulties of classification and, most importantly since the rates apply down to retail level, to special difficulties for persons selling mainly to the consumer, such as retailers. The latter difficulty has been resolved by allowing retailers to estimate their sales liability by reference to their purchases in accordance with approved "schemes". The "schemes" cannot hope to produce a precisely accurate result of sales liable at the three different rates which apply at retail level. They are, however, the best solution that can be devised.

(b) Goods liable at 35/40 per cent: Goods liable at 35 per cent, are passenger road vehicles, and goods liable at 40 per cent are radio and TV sets, gramophone records and record players. The rate of 35/40 per cent is payable only at importation and at the manufacturing stage; at all subsequent stages tax at the rate of 10 per cent is payable. The amount of credit which may be passed from the importation or manufacturing stage to distributors and retailers is limited to 10 per cent, 25/30 per cent being "trapped" at the earlier stages. This, of course, produces the effect of tax on tax but the more serious problem concerns the amount on which tax is chargeable at the manufacturing stage. This amount may be artificially reduced by the creation of non-manufacturing companies which buy goods from the manufacturer at special prices. When this practice became more pronounced the law was suitably amended.

(c) Imports: Under the law a person who is registered for VAT is entitled to import most goods for business purposes free of tax. This arrangement (which was intended to facilitate importers and to relieve the Customs of the fruitless task of charging tax which would become a credit in the hands of a registered person) is open to abuse and for this reason it is now receiving the special attention of the Audit Branch. An expected development of computer programmes related to import statistics will be to provide important information concerning importers and importations which will do much to tighten control.

(d) Exports: Exports qualify for the zero rate of VAT. Goods which are handed over to buyers in the State do not qualify for zero rating even if the goods are subsequently exported. Strict adherence with the law is difficult in the case of transactions with traders in Northern Ireland because of the troubles there. Too great a relaxation of control cannot be allowed because of the danger of all trade with Northern Ireland, including personal shoppers from Northern Ireland, being regarded as meriting special treatment. As a compromise, zero rating is allowed if evidence of importation into Northern Ireland can be produced.

Italy — Initially, some administrative and technical problems were faced. (detail not furnished).

Netherlands — There have been very few technical problems after the introduction of VAT, due to the extensive advertising and information campaign from the Government, and may be also due to the fact that even the small shopkeepers in the country are well organized and were fully aware of the implications of the new tax.

There is however a problem of tax evasion, particularly in small service industries which do not use many materials subject to input tax, which implies that hardly any control is possible regarding the extent of their activities. Especially, services rendered to non-entrepreneurs (private individuals) may often escape tax, since the individual customer cannot credit any input VAT and, therefore, is not interested in receiving a VAT invoice.

West Germany — Before the introduction of Added Value Tax in Germany, there was prevalent in Germany, since 50 years, a gross turnover tax. The requirements under this tax system for the revenue and tax offices as well as for the entrepreneurs (submission of turnover tax advance declarations, turnover tax declarations, obligation to maintain records) are in principle the same as those in the case of the Value Added Tax. The introduction of Value Added Tax in the FRG was possible without great difficulties because of the above fact and also due to the detailed training imparted to the tax officials and the information disseminated to the various undertakings. The difficulties which had cropped up were in the sphere of new calculation of prices by the entrepreneurs. The entrepreneurs had to be made clear that the Value Added Tax cannot be charged on the old prices, but at first, old gross turnover tax was to be calculated out of the prices, and to this "Net Price" the VAT had to be added.

20. IMPACT OF VAT ON GENERAL LEVEL OF PRICES AFTER THE INTRODUCTION OF VAT.

Austria — Between one and two index points.

Belgium — It was estimated at the time of introduction of VAT that the impact of VAT on consumer prices would be to the extent of 2.7 per cent only. This was calculated on the basis of detailed analysis.

Denmark — The VAT is supposed to be neutral towards consumer and manufacturer and seller alike. There is no impact on price apart from the fact that one noted a short stagnation in price during the introduction of VAT.

Ireland — The initial VAT rates (5.26, 16.37 and 30.26 per cent) were calculated so as to correspond as precisely as possible with the rates of turnover tax/wholesale tax in force at the time of the change. The change to VAT was, therefore, not to affect the general level of prices. The Advisory Council on the Transition to VAT endorsed the point in their advertisements. The National Prices Commission carried out an examination of the effect of VAT on prices before and after the change. (Impact not indicated)

Italy — Prices on certain items did go up in general after the introduction of IVA. In some cases, they were directly due to the introduction of IVA. In others they were made up.

Luxembourg — A mechanical increase expected in the cost of living index was calculated at 1.5% to 2%.

Netherlands — At the time of introduction, the Government estimated that the net impact on the consumer price index would be 1% notwithstanding the fact that the yield of VAT would be about equal to the yield of the former multiple stage turnover tax. This was mainly due to a shift in tax burden from certain goods and services to other

goods and services with a more direct impact on the consumer price index. In actual fact, the true rise in prices during the first year of operation of VAT has been much higher than 1%, but it is virtually impossible to isolate the impact of VAT from other factors. In particular, the year VAT was introduced showed a considerable upturn in the national economy, and so a part of the total price rise may well be attributed to economic factors.

West Germany

Assessments on the impact of VAT on the general level of prices are not available. However, it can be said that because of the introduction of VAT, there has been no additional price increase. This will be clear from the following figures of cost of living:

Year	Increase in cost of living of all private households - % -
1966	3.7
1967	1.7
1968	1.6
1969	1.9
1970	3.4

SCHEDULE 3.

VAT IN BRAZIL

Apart from European countries, a few countries in Latin America (including Brazil) are also having the principle of taxation of value added embodied in their tax system. The experience of Brazil is of special interest to us because that country too has a Federal Constitution.

Brazil effected a constitutional amendment for national tax reform in December, 1965 when tax powers were divided between the Union and the States. In the case of commodity taxation the Federal Government were given the powers to tax all industrialised products while the State Governments, the power to tax transactions relating to circulation of merchandise. Under this division of powers taxes are levied (since 1967), by the Federal and State Governments, incorporating value added tax principles whose basic features are briefly indicated below:

VAT AT THE STATE LEVEL - ICM

A tax on transactions relating to circulation of merchandise (called ICM) is levied by State Governments. ICM (which substituted the old turnover and consignment tax) is attracted in the following events:

(a) The shipment of merchandise from commercial industrial or manufacturing concerns (agriculture products);

(b) The receipt in a commercial or industrial establishments or manufacturer of merchandise imported from abroad by the owners of the company; and

(c) The supply of food, beverages and other goods to restaurants, bars, cafes and co-related.

However, there are some cases where no levy is attracted, for example, shipment of industrialised products for exports, receipt of merchandise imported from abroad to be used as raw materials in industrial processes at the importers factory where the finished products in which these raw materials are used are subjected to payment of the tax.

The ICM is a non-cumulative tax, i.e. on each operation the amount paid in the previous ones is subtracted either by the same State or by any other. The total amount due to one State is the result of the excess difference that accrues during a certain period of time (usually one month), counting from the day the product leaves the company of origin and the day the products received are paid for. The balance due to the contributor is transferred to the next period until it is absorbed by tax incorporated on additional shipment of merchandise.

The rate for the calculation of the ICM is the same for all merchandises as well as for every operation. The current rate is 14% for States located in the south east or South region of the country (where the most developed areas are located) and 15% for other States. In the case of export operations within the States (except in the case of industrialised goods) the rate is 13%. In the case of transactions free of charge the ICM is calculated on a pre-established basis. The ICM

is included in the price of the merchandise and cannot be dissociated from it.

The amount corresponding to the IPI (Federal VAT) is not included in the basis for calculation of the ICM when both taxes are charged on an operation.

The general policy on which the ICM system is based - determining factors, non-cumulativeness, basis of calculation, and even rate structure - are settled by the Federal Government while the State Governments make provisions for the application of these general principles in their respective territories.

When goods are exported to foreign countries the entire amount of ICM is rebated to the producers. When they are despatched from one State in Brazil to other States, as indicated above the exporting States levy ICM at a rate which is on the average about 2 percentage point lower than the normal rate on the goods transacted within the State, while the tax rate in the importing State is charged at its full rate. There is no tax gain in avoiding to pass through State Border Tax Post as the indicated 2% differential is rebated at those points. There is no duplication as the taxes paid on earlier transactions are always subtracted in the calculation of ICM.

VAT AT FEDERAL LEVEL - IPI

At federal level a tax is levied on industrialised products known as IPI or Industrialised Products Tax (IPI). IPI is attracted on fabricated or imported products; the fiscal incidence accruing when the products are released for consumption. Thus IPI is payable when products of foreign origin are released by customs; when a product leaves an industrial or importers' establishment or commercial firm supplying raw materials for industries, and when a product confiscated or abondoned is auctioned. In other words the levy is attracted when they are put into circulation for consumption. For the purposes of IPI, the product is considered industrialised when it undergoes any process which modifies it or perfects it for consumption.

The IPI is a non-cumulative tax and the due amount in any taxable period is the difference between the tax on goods removed from the establishment and the tax on those received in the same period. The tax is determined every month and wherever the tax payer is eligible for a balance, it is not refunded but transferred to the next period till it is entirely absorbed by the taxes due on other clearances. It may be noted that only the industry that uses the industrialised products as raw material are eligible to subtract IPI paid on the previous operations.

In the case of commercial concerns which buy industrialised products from the industry for selling purposes, the IPI is added to the cost and when the products are resold, the ICM is charged over the total - including the IPI paid. Therefore, in such cases, there is no compensation of the Federal Tax when it is subject to State VAT. The IPI in contrast with the ICM is not included in the price of the merchandise. In cases of operations for which no price is charged, a pre-determined basis applies.

The IPI is levied at different rates depending on the essentiality and importance of the products. The incidence varies from 3% to 365% depending upon the goods. Food stuffs in general are exempted. Essential products like medicines pay 3% and clothings pay 4%. Imported products like cigarettes attract 365,63% while liquor and perfumes also attract IPI which is 50% or higher.

SCHEDULE 4

THE FORFAIT SYSTEM

Where the body of small traders has great difficulty in maintaining an adequate system of book-keeping for tax purposes a forfait arrangement is often approved by the tax authorities. By this arrangement, a contract is made between the individual traders and the tax office to pay tax, not by reference to actual sales for the taxable periods but in a fixed sum for each period, based on the sales of an earlier year with whatever adjustments are agreed as being appropriate, taking into account general factors affecting all businesses and also any factors which might have relevance only to the particular trader.

The forfait system originated in France where the cascade sales tax introduced in 1920 was strongly resisted by businessmen, especially by the small retailers and artisans. This resistance was due in part to the additional book-keeping which the tax entailed but more to the efforts being made by the authorities to combat tax evasion. In 1923 the Government exempted small artisan craft workers, on the grounds that their receipts were primarily the earnings of labour, and in the following year an extensive forfait system was established for small traders. Under a major reform of the French sales tax in 1936 the cascade tax was replaced by a production tax and the forfait arrangements were terminated. During and after the Second World War the French sales taxes underwent a number of changes and the production tax was supplemented by two other changes, a services tax and a local sales tax, the latter of which applied to artisans and retailers. With the strengthening of tax enforcement after 1950 the artisans and retailers pressed strongly for a return to the forfait system that had been terminated in 1936. The matter became a major political issue and the forfait system was re-established for retailers and artisans in 1955. It has remained a feature of the French system following the extension of the value-added tax to the retail level in 1968. The extent of its use may be gauged from the fact that it applied to 1.6 million of the 2.1 million persons liable to tax for that year.

Under the French forfait system the computation made on the basis of the trading results for year 1 governs the tax payable for years 2 and 3. Early in year 4, however, a new calculation is made on the actual figures for year 3 and this applies for years 4 and 5. If the new figures are materially different from what has already been charged for year 3, a revision of the liability for that year is also carried out. The French system is followed in its oversea territories of Guadeloupe and Martinique. Forfait systems are also used in many other countries including Brazil, Guinea, the Upper Volta, Mexico, the Niger and Tunisia. In Brazil the forfait system is similar to that in France but the revision is made annually instead of every two years.

In the course of the period covered by the forfait arrangement special circumstances might call for an adjustment in the amounts of the agreed payment. Automatic changes would arise if the rate(s) of tax were altered or possibly if there were major movements in currency values. Likewise, if a trader's business declined seriously he would be justified in asking for a downward adjustment in his tax but he would not normally be granted such an adjustment for a purely seasonal fall. If it became apparent, through an audit or otherwise, that the material on which the forfait payments were fixed was not correct, a reassessment of the position would be made at once. Very small businesses might continue to make the agreed payment beyond the normal period if neither the trader nor the tax office sought to have them amended.

The forfait system, as its history indicates, represents a compromise in meeting the difficulties of compliance and control in operating a tax affecting large numbers of small traders with limited records and an attitude of suspicion or even hostility towards the tax authorities. In the countries in which forfait systems are applied it is improbable that even if more detailed accounts were required the results would be very much better. In establishing the payments on the forfait basis the tax official takes into account the sales of the previous year and sometimes also such criteria as the size of the business premises, the rent, the number of employees, the nature of the trade carried on etc. Moreover, the trader is required to keep all invoices of purchases and, if he is providing services, cash book showing his takings day by day, A reasonably accurate estimate of sales should, therefore, be possible. The effectiveness of the system in any country depends, however, on the frequency and thoroughness of the periodic reviews undertaken by the tax office.

APPENDIX 20

A SUMMARY OF THE REPORT ON THE OPERATION OF THE VALUE ADDED TAX (VAT) IN THE UNITED KINGDOM AND BELGIUM

In September, 1976, the Chairman and the Member-Secretary of the Committee visited the U.K. and Belgium to make an on-the spot study of the operation of VAT in both the countries.

INTRODUCTION

The study broadly covered the background leading to the introduction of VAT in both the countries, the existing rate structure and the various transitional and other problems that arose in the course of adoption of VAT in the two countries. During the course of the visit, discussions were held with the tax authorities of both countries as well as representatives of the business interests. The first section of this summary relates to the operation of the VAT in U.K. while the second refers to the VAT system as in operation in Belgium.

SECTION I - VAT IN OPERATION IN U.K.

2. The origin of VAT in the U.K. may be traced to the suggestion made in the Report of the National Economic Development Council (NEDC) in April 1963 that a VAT to replace other taxes might be one of the instruments that would help in securing a better economic performance in Britain. The suggestion was based on three objectives:—

(i) Shifting the tax falling on productive activity towards taxing more heavily the pay roll and less heavily the employment of capital equipment.

(ii) Spreading out the narrowly based purchase tax more uniformly over consumption expenditure, including expenditure on services, and

(iii) transferring part of the weight of taxation away from taxes that entered into export costs on to the taxes that could be remitted on exports and charged on imports.

3. As a follow-up, the Richardson Committee was set up, which did not favour adoption of VAT. It, however, felt that the objectives outlined in the NEDC report could be better secured by widening the base of purchase tax. As to the first objective of shifting the tax from productive activity, the Committee felt that the same could not be achieved by the VAT, because industrialists may not take into account the equivalent reduction of taxes on employment of capital, as a factor reducing costs. Subsequently, the NEDC again turned its attention to the question and in its report published in 1969 recorded that "the views expressed about the general desirability, or the specific effects, of a VAT were diverse and inconclusive and there was no unanimity for or against the introduction of the tax, or about its general industrial and economic impact".

4. The first move towards introduction of VAT in U.K. arose out of the commitment made by the Conservative Party for the abolition of selective employment tax introduced by the Labour Party, "possibly involving the replacement of purchase tax by VAT". Soon after the Conservative Government took office after the Election, the introduction of VAT was announced and the Green Paper on VAT was published in March 1971 with the announcement that VAT would be introduced in April 1973. The White Paper on VAT was published in March 1972 along with the budget papers which included the proposal to introduce VAT. The registration under the VAT (General Regulations) Act started on 1st October, 1972 and the tax came into force from 1st April, 1973.

5. At the time of introduction, VAT was levied at a uniform rate of 10%. This was reduced to 8% by the Labour Government. In November 1974, a process of multiple rates was initiated by an enhancement of the tax on petrol to 25 per cent. In May 1975, a large number of other items, like, domestic appliances, radio and television sets, small boats and aircrafts, caravans, photographic equipments, binoculars, fur, garments, jewellery, gold and silver wares etc., were brought to the higher rate. In the budget of 1976, these items were again brought down from 25% to $12\frac{1}{2}$%.

6. The VAT in the U.K. requires the registration of all persons whose supply of goods and services exceeds or expected to exceed £ 5000 in a year. Registered assessees number approximately to 1.25 million of which as many as 3,50,000 are "Repayment traders" i.e., 1/3rd of the assessees get net refund of tax. It is the balance of about 9 lakh assessees who pay net revenue of about £ 3,000 million. Even out of these, only 600 assessees account for 90% of the payments. Thus, assessment and collection of tax from a vary large number of so called small traders has been posing a major administrative problem.

7. The tax collection machinery is wholly centralised and located in a place called South End on Sea. All the processes starting from that of registration, issue of notices of tax demands ending with the recovery proceedings are centralised in the VAT Central Office in South End. Nevertheless it has been found necessary to combine this centralised operation with programmed visits to assessees by officials from local VAT offices (LVO) and sub-offices which number in all 150. At present there is a phased programme of such visits to each assessee once in 3 years. These spot checks are reported to have on an average yielded an additional revenue of £ 30 million per year. The frequency of visits for spot checks by LVO is unrelated either to the period of limitation for recovery of short assessments or to the time period within which the assessee can safeguard himself against demands for short payments where these are due to bonafide errors. Such ad hocism in treatment of spot check is based more on consideration of cost benefit ratio.

VAT ADMINISTRATION

8. The VAT Central Unit is the focal point of the VAT organisation and is highly mechanised in its functioning. Organisation of the unit and the flow chart of all the operations done on VAT returns issued and received back duly filled in are contained in Exhibits 1 and 2 to this report. High degree of centralisation and mechanisation of operations has become necessary to cope with the enormous increase in the number of assessees from 60,000 under the old system to 1 million under VAT. This has obviated the need for the local VAT offices to make routine visits for

getting the quarterly or monthly returns from the assessees and checking them for arithmetical accuracy before the tax due is paid into the Bank of England or refunded where such refund is due. All the operations starting from the issue of notices in appropriate forms for filling in details of "input" and "output" taxes upto the stage of programmed checking of the returns filed and print out of the final results including the "credibility check" of the assessee's return is done in this unit. The main operations in their sequential order are as follows:—

(i) Post Office functions, namely, of mechanical issue of quarterly or monthly returns to the registered traders and receipts sorting and distribution of posts to the different sections.

(ii) Banking operations of sorting out the cheques and payments made in other forms like postal orders, currencies etc. followed by reconciliation of tax due on returns with remittances made to the Bank of England.

(iii) Micro-filming of returns and maintaining library of all micro-filmed material.

(iv) Computer operations involving key to disc punching of data from each of the returns received, transfer of data punched from disc to magnetic tapes which pass through the computers for accounting, compilation and "credibility check".

9. The Computer print out forms the basis for the final closing of the quarterly or monthly return filed by the assessee which may result in a payment of tax due or refund of tax where the input tax exceeds the output tax. Where the computer print out indicates some failure of the credibility check then each such entry is subjected to preliminary scrutiny in the VAT Central Office and only those cases are referred to the local VAT office which need spot enquiry and/or verification by personal contact of the trader assessee. As many as 24,000 returns are handled on an average every day and about 6 million per annum. As mentioned earlier, 90% of the total revenue from VAT is accounted by 600 large assessees a feature not peculiar only to U.K. but is also to be found in France and West Germany.

10. Apart from the assessment function, the VAT Central Office has an Enforcement Division which takes follow-up action against the recalcitrant assessees who fail to submit returns despite warning notices issued by the Computer system. Normally, the large assessees pay up the due in time. In the case of small traders,

ENFORCEMENT OF VAT

assessees, after issue of the final notice, a notice of demand is sent setting out the tax due which is worked out by the Computer on programmed inputs of previous payments or the dues calculated on the cases of analogous traders taking into consideration their past and current performance. The demand is withdrawn if the assessee files a return. If he does not, then the amount so demanded is recoverable as a debt subject to a right of appeal to the VAT Tribunal. About 30 days are spent in the recovery proceedings during which time the officers of LVO are asked to make personal contact with the trader/assessee which action, in a large majority of cases, results in the assessee filing the return or paying up the demand raised. If in spite of such personal contact

the return is not filed or tax demanded is not paid notice is issued by the Collector for attachment and sale of property and chattel. If, however, the assessee has no assets or they are insufficient to meet the demand raised, then bankruptcy proceedings are taken. In the event of third or fourth non-filing of returns, steps are taken to prosecute the assessee.

ADMINISTRATIVE PROBLEMS

11. One of the major administrative problems being faced by the VAT administration in U.K. is assessment and collection of tax from the large number of so-called small traders. Even though special schemes have been evolved for retail traders, apparently no norms for defining the small traders, have been evolved. The reluctance of the U.K. Tax Authorities to adopt a simplified procedure (known as Contract procedure in France) is perhaps traceable to the vast differences in the "Value added" of each groups industry, trade and services and consequently to the fact that unlike the French system in the U.K. the machinery does not co-ordinate its activities with the tax collection machinery of the inland revenue(i.e., income and corporation tax.)

DISCUSSIONS WITH TAX OFFICALS

12. During the course of the visit, meetings were held with senior Government officials, representatives of business interests and other individuals, whose names appear in the list appended to this summary. Discussions with senior Government officials revealed that the switch-over to VAT in U.K. had created many problems which were further complicated by numerous exemptions and zero-rating. It was felt that the small traders resented the tax because it involved considerable time and effort for them to maintain proper accounts and file the returns correctly and in time. Administratively, the vastly increased number of assessees had created problems regarding visits of the officers and the small trade had not taken kindly to these visits of the local VAT officers to their premises. However, the general feeling was that the tax system is broadly setting down and the computers had considerably helped in the process of collection.

DISCUSSION WITH BUSINESS INTERESTS

13. Discussions with the representatives of business interests revealed that the switch-over to VAT has the full support of the organised sector of the industry. In fact the Confederation of British Industries has been advocating a further extension of it as a replacement to direct taxation which is very high in U.K. at 83% for earned income and 93% for unearned income. On the question of the rigour of account keeping under VAT the Confederation was of the view that the purchase tax was worse in this respect than VAT because of variable rates and that VAT was better in terms of being a broad based tax, easily collected through computerisation. The Confederation did not, favour introduction of VAT in stages selectively since it felt that the co-existence of too many tax systems would be rather cumbersome. The Confederation was of the view that a universal coverage is a must for VAT since it is a self-enforcing tax system. It was felt that for a more effective administrative control the exemption limit should be fairly high.

VIEWS OF ECONOMISTS

14. In the course of discussions with economists of eminence, it was understood that the VAT in U.K. had affected only 40% of the consumer expenditure, the balance of 60% was accounted for mostly by food and transport which are zero rated or exempted. Unlike other countries in the E.E.C., U.K. had zero-rated most items of food which was a major

source of revenue to the rest of the E.E.C. This, however, was sought to be made good by a high level of traditional excise on hydro-carbon oils, tobacco and cigarettes. A view was also put forward that in an economy where there was need to monitor constantly the demand by putting a higher tax burden on consumption or vice versa, undoubtedly the VAT, being a widely covered tax system, will have an all-pervasive effect. In that sense, one could say that such an exercise might be counter productive but it depends on the magnitude of the tax increase and the multiplier effect it might have on the level of prices. A suggestion was made to the effect that the VAT system could be thought of as an alternative re-distributive form of direct taxation in the sense that one could consider lowering the income-tax and make up the revenue by levying a Value Added Tax. As regards the objective of helping the exports because of their being zero-rated, the view expressed was that VAT has not helped substantially because a large number of incentive schemes were in operation even before its introduction.

VAT REVENUES

15. In the first year of the introduction, VAT accounted for 23½ per cent of total revenue which went up to 34 per cent in 1974-75. The Excise duties accounted for 54 per cent of the total revenue in 1974-75, as against 58 per cent in 1973-74. The proportion of Customs protective duties remained the same during these two years at 7 per cent. It may be added that before introduction of VAT, in 1972-73, the Excise duties accounted for nearly 66 per cent, purchase tax about 24 per cent and protective Customs duties 6 per cent of the total revenue.

IMPACT OF VAT ON PRICES

16. Another important question relating to introduction of VAT is its impact on prices. Prior to introduction, it was anticipated that a 10 per cent rate of VAT would lead to a little more than one per cent increase in consumer prices. However, no definite conclusion could be made as to the impact on price structure, though some articles in the 'Economist' suggested a rise of as much as 10 per cent. This was discounted by the Government and a guide to the VAT price changes was issued free to the consumers, with a distribution of nearly 5½ million. In any case, the fact that Excise and Customs duties are levied along with VAT and form a formidable 61 per cent of the total revenue makes it difficult to draw any comparison as to the impact of VAT on prices in countries which may or may not continue with such high means of other indirect taxation. One of the reasons of industry advocating VAT was to shift the burden of taxation from capital investment to pay roll and this by itself would suggest that adoption of VAT would mean increase in consumer prices. This does not, of course, discount the fact that in some of the countries, inelasticity of demand and shortage of supply coupled with monoply control may enable suppliers specially the producers to shift even the increases in excise duties to the consumer.

SECTION II - VAT IN OPERATION IN BELGIUM

HISTORICAL

17. The VAT code was enacted by the Belgium Parliament in July, 1969 and was originally scheduled to take effect on January 1, 1970. But due to inflationary pressures and the fear that VAT could contribute to further increases in domestic prices and also the time needed for technical and administrative preparation and implementation, the effective date was postponed to January 1, 1971. The switch-over VAT constituted a far-reaching reform of Belgium indirect taxes which was estimated to account for approximately 38% of the total tax revenue in 1970.

The code sought to abolish most turnover taxes, in particular the transfer taxes on important and domestic transfers, the invoice tax on transfers and service contracts, the luxury tax, the lease tax, the transportation tax and the tax on the renting of safes. The origin of VAT in Belgium in fact took into account European Common Market directives as well as the business needs of the country.

VAT RATES & EXEMPTIONS

18. Belgium has four rates for operation of VAT, namely, 6%, 14%, 18% and 25% - 18% being the general rate of tax. All exports from Belgium like all the other Community countries were zero-rated. The Belgian system of VAT also allowed certain exemptions in terms of lower rates. In order to remove hardships of small retail traders a system of compounded levy of VAT is adopted which combines the value of the total sales and their total profit over the year as the base for calculating VAT.

VAT COLLECTION

19. Much of the routine connected with assessment and collection of the tax is computerised in Belgium. The operation are, however, not centralised to the same extent as in the U.K. For example, issue of notices (quarterly or monthly) to the assessees and receiving the VAT form duly filled in, is done by the local VAT offices and not by the Computer unit. Perhaps the object is to maintain continuous contact with the assessees by the local VAT offices and to rectify all errors in form-filling before the returns are taken for computer processing.

PROBLEMS

20. It was indicated during discussions with tax officials that the VAT was being accepted and complied with without much difficulty by larger traders who have the necessary equipment of computers and trained accountants. The small traders, however, have been increasingly facing the problem of maintaining the accounts which is very necessary for the working of VAT. It was felt that management of the VAT particularly in its effect on small traders would be quite arduous and administrative problem involved is also quite considerable, for example, U.K. had before the introduction of VAT a purchase tax and an employment tax both of which were easy to administer. About the degree of tax evasion/avoidance in respect of VAT alone it was indicated that taking all the tax systems of the country the evasion/avoidance of tax may be about 5 per cent.

List showing the names of officials/individuals with whom discussions were held

(a) Meetings held in London

1. Mr. Phelps, Deputy Chairman, U.K. Board of Customs and Excise.

2. Mr. Knight
3. Mr. Webb

Officials of the U.K. Board of Customs and Excise.

4. Sir Donglas Allen, Head of British Civil Service.

5. Sir Douglas Wass, Permanent Secretary, Treasury.

6. Sir William Denis Pile, Chairman, Inland Revenue.

7. Sir Norman Kipping (Retired) Chairman, CBI.

8. Mrs. D. Johnstone (Retired) Commissioner, H.M. Customs.

9. Mr. John Methven, Director General, Confederation of British Industries, (CBI).

10. Sir Donald Medougall, Chief Economic Adviser. (CBI).

11. Mr. C.L.S. Cope, Overseas Director, (CBI).

12. Mr. Richardson, Governor, Bank of England.

(b) Meetings held in Brussels

13. Mr. Peter Hogg. An officer of the Directorate of Financial Institutions and Taxation, E.E.C.

14. Mr. R. Lagnau Inspector General of Taxes.

15. Mr. L.J. Haris, Incharge Customs and Excise in the Permanent Representation of the U.K. to E.E.C.

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EXHIBIT-1

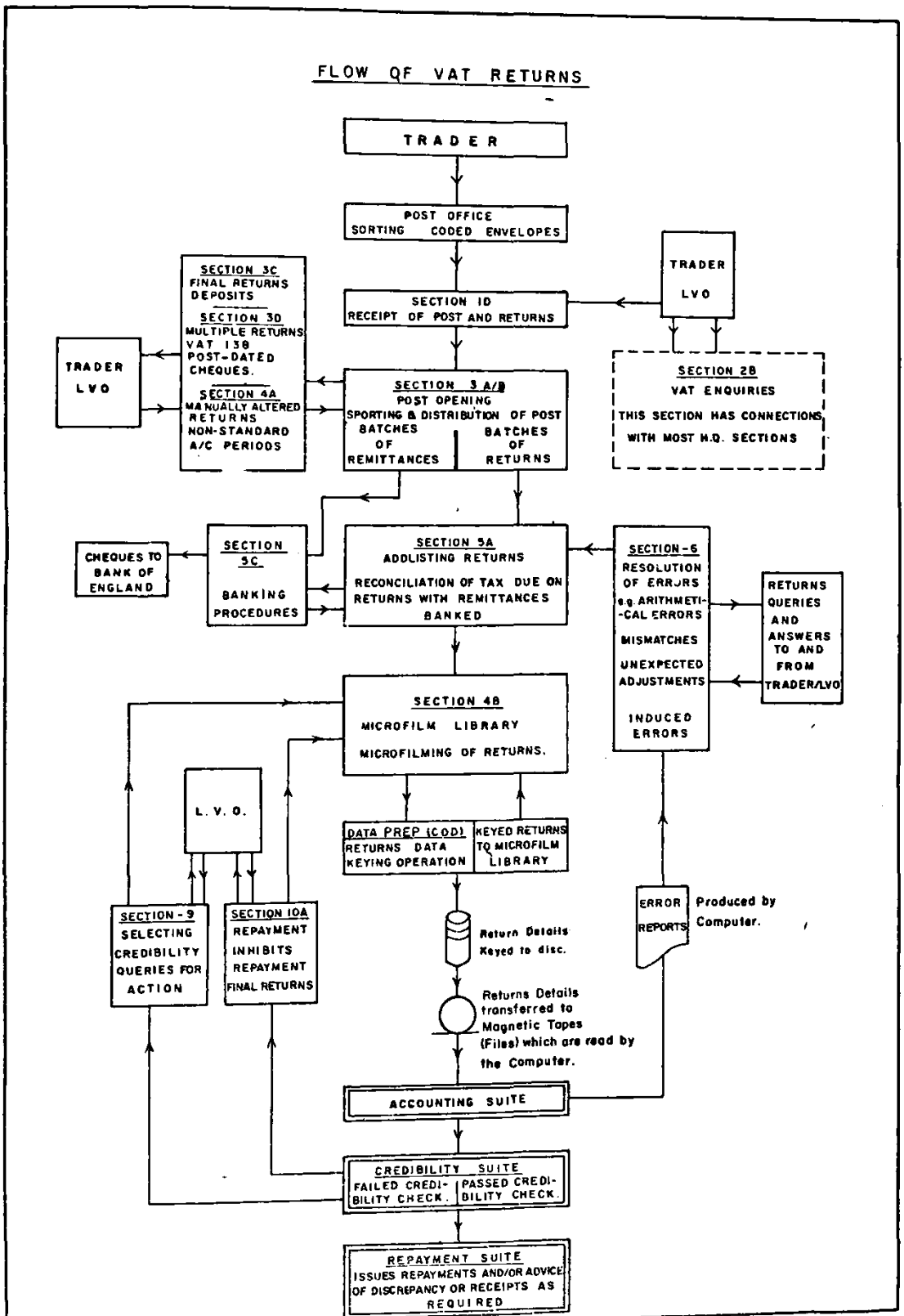
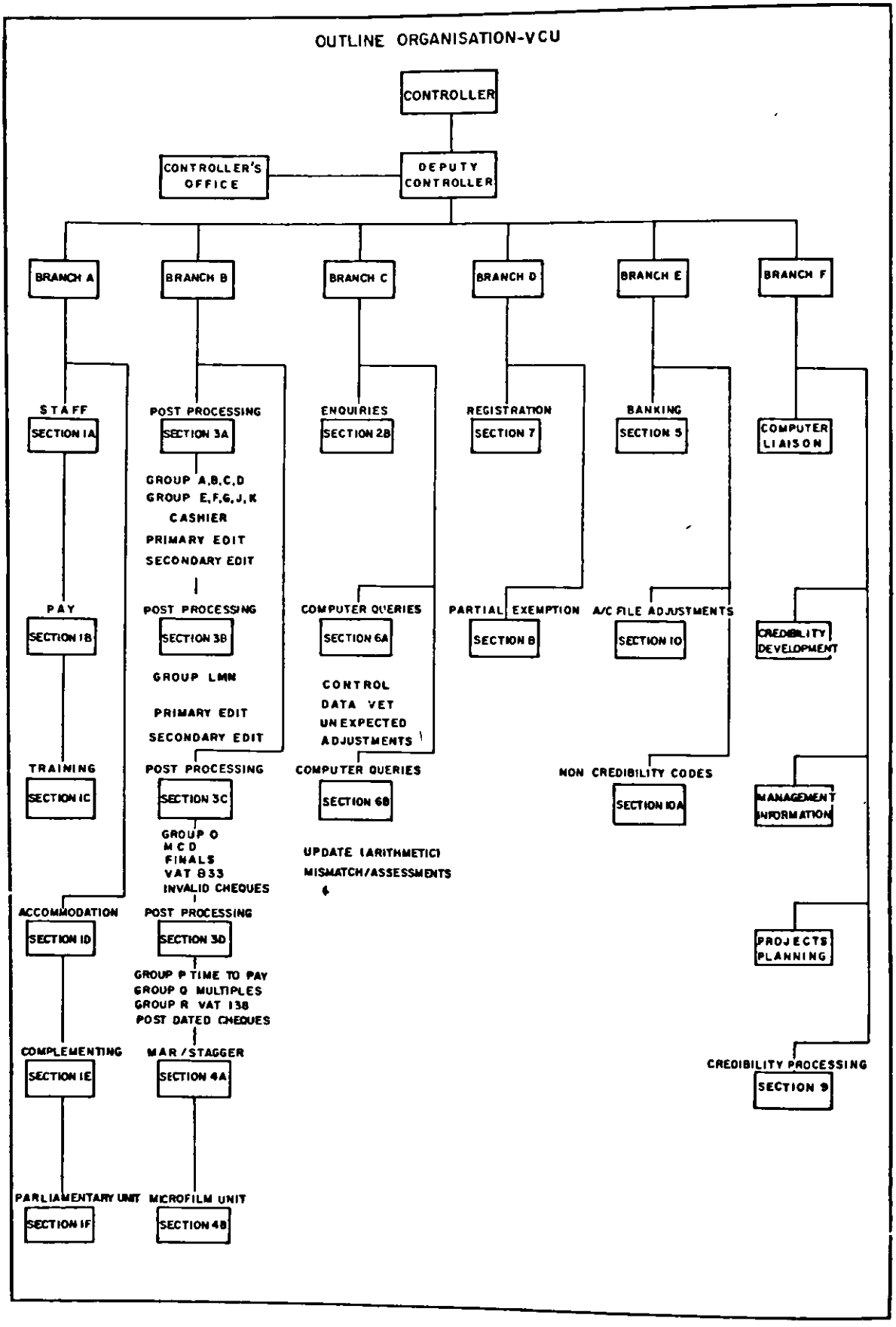

FLOW OF VAT RETURNS
TRADER
POST OFFICE SORTING CODED ENVELOPES
SECTION 3C FINAL RETURNS DEPOSITS
SECTION 3D MULTIPLE RETURNS VAT 138 POST-DATED CHEQUES.
SECTION 4A MANUALLY ALTERED RETURNS NON-STANDARD A/C PERIODS
TRADER LVO
SECTION 1D RECEIPT OF POST AND RETURNS
TRADER LVO
SECTION 2B VAT ENQUIRIES THIS SECTION HAS CONNECTIONS WITH MOST H.Q. SECTIONS
SECTION 3 A/B POST OPENING SPORTING & DISTRIBUTION OF POST
BATCHES OF REMITTANCES
BATCHES OF RETURNS
CHEQUES TO BANK OF ENGLAND
SECTION 5C BANKING PROCEDURES
SECTION 5A ADDLISTING RETURNS RECONCILIATION OF TAX DUE ON RETURNS WITH REMITTANCES BANKED
SECTION-6 RESOLUTION OF ERRORS e.g. ARITHMETI-CAL ERRORS MISMATCHES UNEXPECTED ADJUSTMENTS INDUCED ERRORS
RETURNS QUERIES AND ANSWERS TO AND FROM TRADER/LVO
SECTION 4B MICROFILM LIBRARY MICROFILMING OF RETURNS.
L. V. O.
DATA PREP (COD) RETURNS DATA KEYING OPERATION
KEYED RETURNS TO MICROFILM LIBRARY
SECTION-9 SELECTING CREDIBILITY QUERIES FOR ACTION
SECTION 10A REPAYMENT INHIBITS REPAYMENT FINAL RETURNS
Return Details Keyed to disc.
Returns Details transferred to Magnetic Tapes (Files) which are read by the Computer.
ERROR REPORTS
Produced by Computer.
ACCOUNTING SUITE
CREDIBILITY SUITE
FAILED CREDI-BILITY CHECK.
PASSED CREDI-BILITY CHECK.
REPAYMENT SUITE ISSUES REPAYMENTS AND/OR ADVICE OF DISCREPANCY OR RECEIPTS AS REQUIRED

EXHIBIT-2


OUTLINE ORGANISATION-VCU
CONTROLLER
CONTROLLER'S OFFICE
DEPUTY CONTROLLER
BRANCH A
BRANCH B
BRANCH C
BRANCH D
BRANCH E
BRANCH F
STAFF
SECTION 1A
PAY
SECTION 1B
TRAINING
SECTION 1C
ACCOMMODATION
SECTION 1D
COMPLEMENTING
SECTION 1E
PARLIAMENTARY UNIT
SECTION 1F
POST PROCESSING
SECTION 3A
GROUP A,B,C,D
GROUP E,F,G,J,K
CASHIER
PRIMARY EDIT
SECONDARY EDIT
POST PROCESSING
SECTION 3B
GROUP LMN
PRIMARY EDIT
SECONDARY EDIT
POST PROCESSING
SECTION 3C
GROUP O
M C D
FINALS
VAT 833
INVALID CHEQUES
POST PROCESSING
SECTION 3D
GROUP P TIME TO PAY
GROUP Q MULTIPLES
GROUP R VAT 138
POST DATED CHEQUES
MAR/STAGGER
SECTION 4A
MICROFILM UNIT
SECTION 4B
ENQUIRIES
SECTION 2B
COMPUTER QUERIES
SECTION 6A
CONTROL
DATA VET
UNEXPECTED
ADJUSTMENTS
COMPUTER QUERIES
SECTION 6B
UPDATE (ARITHMETIC)
MISMATCH/ASSESSMENTS
&
REGISTRATION
SECTION 7
PARTIAL EXEMPTION
SECTION 8
BANKING
SECTION 5
A/C FILE ADJUSTMENTS
SECTION 10
NON CREDIBILITY CODES
SECTION 10A
COMPUTER LIAISON
CREDIBILITY DEVELOPMENT
MANAGEMENT INFORMATION
PROJECTS PLANNING
CREDIBILITY PROCESSING
SECTION 9

APPENDIX 21

FEASIBILITY OF A VALUE ADDED TAX AT MANUFACTURERS' STAGE FROM THE ACCOUNTING ANGLE - A STUDY

I. INTRODUCTION

With a view to studying the feasibility of a value added tax at the manufacturers's stage (MANVAT) in lieu of Central excise, a small sample study was undertaken by the Committee's Secretariat. The main purpose of the study was to assess the extent of documentation obtaining in manufacturing (small, medium and large) units with reference to their purchases, stocks, production and sales, make a comparative study of such documentation with that required under a normal VAT system and identify the major problems likely to be faced in the case of a switch over to MANVAT. A detailed questionnaire was prepared and units selected at random were visited for eliciting information on various aspects of the study as well as views on the adoption of MANVAT.

2. COVERAGE OF THE STUDY

The study covered a small sample of 25 manufacturing units which are engaged in producing different commodities. Nine of these units are situated in Bombay and the remaining in Faridabad. The units included in the sample study could be broadly broken up into following turnover categories:

Category	Turnover	No. of units
A-1	Exceeding Rs.1 crore	5
A-2	Rs.50 lakhs to Rs. 1 crore	4
A-3	Rs.20 lakhs to Rs. 50 lakhs	4
B-1	Rs.10 lakhs to Rs. 20 lakhs	4
B-2	Rs.2 lakhs to Rs. 10 lakhs	4
C	Less than Rs. 2 lakhs	4
	Total	25

A major limitation ofthe study is the smallness of the sample. However, since the emphasis was on making a qualitative assessment of the present documentation, the extent and nature of gap, if any, between the present system and a VAT system and identifying at the same time some of the major problems, we found the sample to be sufficiently indicative of the general practice obtaining in industry.

II. PRESENT DOCUMENTATION - AN ACCOUNT

3. MAGNITUDE OF DOCUMENTATION REQUIREMENT

We have noticed that by an large units whose turnover is less than Rs. 20 lakhs per annum have only one or two products in their manufacturing line whereas units whose annual turnover exceeds Rs. 20 lakhs usually have a wider product mix and also produce goods of different varieties and specifications within the same class of products. This brings out the fact that in the case of small manufacturers

the problem of accounting and documentation with reference to the final products is somewhat limited in as much as it has to deal with one or two products along. On the other hand, in the case of larger producers the problem of linking inputs and the final products and accounting thereof asumes some proportions.

4. The sources of purchases as between units of different categories does not fall into a distinc pattern. A broad generalisation of the position could however, be made category-wise, though there are cases of small manufacturers getting their inputs directly from manufacturers, and bigger manufacturers procuring inputs for their use from dealers. A category-wise analysis of the pattern of purchases is as under:—

Category	Imported inputs	Indigenous inputs
A-1	Direct purchase of through canalising agencies	Mostly from manufacturers of whom 10% to 20% are small manufacturers. There are also purchases from dealers of consumable and small items
A-2	Direct purchase or through canalising agencies	Broadly, purchases from manufacturers account for about 60% and purchases from dealers account for about 40%. About 20% of the purchases from manufacturers are from small scale industries
A-3	Direct purchase or through canalising agencies	There are purchases from manufacturers as well as dealers. About 10% to 20% of purchases are from small manufacturers
B-1	Nil (The units included in the sample do not get imported input)	Purchases are from both manufacturers and dealers. The quanta of purchases from small scale industries vary from 10% to 50%
B-2	Direct imports as well as purchases from local importers; the latter is more common	There are purchases from manufacturers and dealers, the latter forming a greater proportion
C.	Purchases from intermediaries	Most of the purchases are from dealers

5. The broad picture that emerges from these results is that, by and large, the bigger manufacturers (A-category) prefer to get their indigenous inputs directly from the manufacturers of the inputs themselves. In the case of imported inputs a big manufacturer is usually in a position to get either direct supplies or from canalising agencies like MMTC and STC. As a source of supply of indigenous inputs we find that small scale industries meet even the requirements of bigger manufacturers. The quantum of purchases from this sector, however, varies from industry to industry. Purchases of inputs from dealers form a sizeable proportion of total purchases in the case of units whose turnover is upto Rs.1 crore. Particularly, in the case of small manufacturers (of turnover upto Rs.10 lakhs) their purchases of inputs from dealers, in fact, constitute the major part of their purchases. An interesting point of detail revealed by the study is that in some cases (which even covered a unit of category A-1) the manufacturers preferred to purchase their inputs from dealers since the original manufacturers of such inputs take a long delivery time, as against quick delivery from dealers, and also generally insist on early payment while the dealers give credit upto three months, give high discounts, as well as pass on a part of their commission.

6. PURCHASE DOCUMENTATION

The documents that are available with manufacturers in support of their purchase of inputs of various kinds could be broadly divided category-wise as follows:

Category of manufacturers	Commonly found documents	Additional documents found in specific situations
A (i.e. A-1, A-2, A-3)	Purchase order, Seller's invoice, Delivery challan and Sales tax declaration	Excise gate pass, Bill of entry, Bill of lading and C-form
B (i.e. B-1 and (B-2)	Seller's invoice, Delivery challan and Sales tax declaration	Excise gate pass: Bill of Entry and B-form
C	Seller's invoice/ Cash memo, Delivery challan and Sales tax declaration	Excise gate pass

Note:- Excise gate-pass is found in the case of direct purchase from manufacturers. Bill of Entry is available in the case of imports and C-Form in the case of inter-State purchaser

Broadly, the documents relating to purchases are more (they serve in fact different purchases) in the case of units whose turnover exceeds Rs.20 lakhs. The most common purchase document is the 'invoice', which we came across in all units but one in category 'C', in whose case, we found stamped receipts for purchases in lieu of invoices. In the case of units of categories 'A' and 'B' purchases covered by documents other than invoices are practically 'all' whereas in the case of units of category 'C' a bigger proportion of purchases are made on cash memos/petty cash vouchers. Normally, these memos/petty cash vouchers merely mention the value of the purchase and date. The name of the purchaser does not usually get mentioned.

PARTICULARS SHOWN IN PURCHASE INVOICE

7. Among the various documents evidencing purchases, the 'invoice' can be regarded as the most common and typical. Though, in general, the details shown in these invoices vary not with reference to the purchaser, since units of categories 'A' and 'B' purchase more from manufacturers and bigger dealers, minimum details appearing in most of the invoices are —

(i) description of goods;

(ii) quantity;

(iii) rate/value of purchase;

(iv) amount of sales tax paid;

(v) purchaser's name; and

(vi) sales tax registration number.

Wherever the invoice is issued by a manufacturer, we find that in addition to the above, particulars of excise gate-pass number, delivery challan and excise amount are mentioned. There are cases where even when invoices are issued by the manufacturers, the excise amount is not separately shown but is included in the sales realisation. As for the invoices which are obtained by units of 'C' category, the particulars commonly noticed are —

(i) date of purchase;

(ii) description of goods;

(iii) quantity; and

(iv) value.

MANNER OF RECORDING PURCHASES

8. The recording of purchases on the basis of the documents received is normally on the same pattern in the case of units of categories 'A' and 'B'. Units of both categories maintain register or a ledger which is also required to be produced for sales tax purchases. The minimum particulars entered in this record are - date of purchase, quantity and description of goods. In majority of cases, the value of goods purchased is

also indicated and so is the sales tax amount paid on the consignments. Excise paid in respect of inputs purchased is not, however, recorded in this register/ledger . In some cases, the purchase invoice number is indicated. The normal periodicity of the entries in the purchase register or ledger is either daily or as and when purchases are made. In cases where the facilities of electronic data processing are available the recording of purchases is done on a monthly basis and where purchases made by bigger producers are centralised to cater to more than one unit of manufacture, the practice adopted is one of allocation on the basis of requirements or of direct purchase. In any case, every purchase made by the unit is recorded in the general registers or ledgers with the particulars mentioned above.

9. As for the 'C' category units the minimum particulars that are recorded in their purchase records are —

(i) date of purchase ;

(ii) quantity; and

(iii) value.

Excise duty amount is not mentioned in the register while the sales tax amount paid on the purchase gets mentioned especially when it is required to be shown for sales tax purposes. Normally, the entries in this register are made by these units either monthly or when they are required to be produced to the sales tax authorities.

10. MANNER OF RECORDING STOCK OF INPUTS

Apart from the recording of purchases as indicated above it is noticed that almost all manufacturing units maintain a record which shows the stock of inputs as well as finished goods. In units of category 'A', this record either takes the form of a stock card or a ledger or a computerised statement. The common particulars included in these records are —

(i) date;

(ii) opening balance;

(iii) receipts;

(iv) issues; and

(v) closing balance.

In majority of cases the value as well as suppliers' name are indicated. The entries in this record are made usually on day-to-day basis. In the case of category 'B' units the stock ledger indicating the following particulars is more common:

(i) date;

(ii) receipts;

(iii) issues; and

(iv) closing balance.

In their case, value of consignment is usually not recorded. So is the case with suppliers' name. The pariodicity of entries in this ledger is either daily, or fortnightly or monthly. In this category of units, a case where no record of stock of inputs is maintained was also noticed. As for category 'C' units, where a record of stocks is maintained, particulars regarding —

(i) date of receipt;

(ii) issues; and

(iii) closing balance,

are indicated. Here again, we came across a case in which stocks are not recorded.

11. INVENTORY HOLDING TIME

Though the inventory holding time for different materials as also between indigenous and imported raw materials varies, it is seen that the average inventory holding time is about two to three months, while the minimum and maximum are a fortnight and six months respectively.

12. PRODUCTION RECORD

The production of finished products is usually recorded in a register. In most of the units both statutory records as well as manufacturer's own private records are maintained for this purpose. As for statutory records (required under excise law) it was found that all units maintain them. The principal production record, namely, "RG-1" contains, among other things, the following particulars :

(i) date;

(ii) opening balance;

(iii) quantity produced;

(iv) quantity removed;

(v) closing balance;

(vi) value of goods (where required to be shown);

(vii) gate pass number; and

(viii) details of re-processing returned goods etc.

Entries in this record are made either on day-to-day basis or as and when transections are there, the latter being a relaxation of procedural requirements. As for the private records of production,

we find that units of categories 'A' and 'B' do maintain them (and are known as production Report/ Slip) usually in a form different from RG-1. These indicate either batch-wise, product-wise or shift-wise production and show the kind of break-up which the manufacturer himself requires for his own control purposes. Normally, the details shown in them are —

(i) date;

(ii) production reference number; and

(iii) quantity produced or packed as the case may be.

Value of the goods is not generally indicated in such reports/slips. In the case of units of 'C' category, however, no separate private record is maintained; the statutory RG-1 record is itself used to indicate the production on a day-to-day basis or as and when there is production.

13. RECORDS FOR BANK FINANCE PURPOSES

In general, where goods are hypothocated to banks, it is found that no special records are maintained by the manufacturing units but some bigger manufacturers do maintain stock records for their own convenience, which are made available for inspection by banks. In one or two cases, we found that the manufacturers have pledge facilities. The manufacturers have been found to maintain a pledge register showing stocks and also indicating —

(i) the opening balance;

(ii) receipts;

(iii) issues;

(iv) closing balance; and

(v) value of goods.

14. DOCUMENTATION RELATING TO SALES

An analysis of the documentation relating to sales shows that, in general, the units of 'A' category prepare a greater number of documents which serve different purposes. The sales documents in common use are —

(i) excise gate pass;

(ii) delivery challan;

(iii) sales tax declarations;

(iv) invoice/cash memos; and

(v) bank documents.

In the case of 'B' and 'C' category units, however, we find that only three documents are in common use, namely,

(i) the excise gate pass;

(ii) the delivery challan; and

(iii) the invoice.

Where cash sales are involved, we find that the invoice and the excise gate pass are the minimum documents prepared. This is so with all manufacturing units.

15. The particulars which are usually indicated in the invoice issued by category 'A' units are —

(i) date;

(ii) description of goods;

(iii) quantity;

(iv) value;

(v) sales tax registration number;

(vi) sales tax amount; and

(vii) consignee's name.

In a majority of cases we find that the invoice contains a mention of the excise amount and in others excise is included in the sales realisation amount. In some cases, delivery challan number and 'C' form number are indicated. In the case of units of 'B' and 'C' categories, where the invoice is more or less on a similar pattern, the particulars recorded are —

(i) date;

(ii) description of goods;

(iii) quantity;

(iv) value;

(v) sales tax amount;

(vi) excise amount; and

(vii) consignee's name.

16. Sales invoices are generally found to be serially numbered though in some units they are in a loose leaf form as against the normal practice of issuing invoices from bound books. In all cases, it was found that at least two copies of the invoice were made.

17. The normal time lag between invoicing and receipt of payments is found to vary between different categories of manufacturers. In regard to 'A' category units, the normal time lag is one of three months, the maximum being one year and the minimum a fortnight. With reference to 'B' category units, the normal time lag is three months as against $1\frac{1}{2}$ months to three months in the case of 'C' category units.

18. After the issue of invoices, again, a record thereof is generally required to be produced for sales tax purposes. Thus, we find all the categories of manufacturers maintaining a record either invoice-wise or customer-wise. The particulars entered in such a record vary as between units of different categories. Normally, it is found that the particulars recorded are —

INVOICE RECORD

(i) date;

(ii) invoice number;

(iii) name of the party;

(iv) amount; and

(v) particulars of payment.

In a good number of cases, the sales tax amount payable under each invoice is indicated. In only very few cases, it was found that the excise amount has get mentioned in such records. While the bigger units make entries in a record of this kind more or less on a day-to-day basis, the smaller ones have the entries in this record made one in a fortnight or a month.

19. The study reveals that some of the major records maintained for assessment of excise, sales tax and income tax are as under:

RECORDS MAINTAINED FOR ASSESSMENT OF OTHER TAXES

Category of units	Excise	Sales Tax	Income-tax
	RG-1, Form IV (Raw material account),	Sales Register,	Cash Book,
	RG-23 (proforma Credit Account),	Purchase Register,	Sales Book,
	Personal Ledger A/c and Excise gate pass book	Record of 'C' forms and list of registered dealers.	General Ledger, Debtor Register and Stock Register.

Category of units	Excise	Sales Tax	Income-tax
B	RG-1, Form IV (Raw material account), RG-23 (proforma Credit Account), Personal Ledger A/c and Excise gate pass book	Sales Register and Purchase Register	Cash Book, General Ledger and Debtor Ledger
C	RG-1 or simplified A/c. Personal Ledger A/c, gate pass Book.	General Sales Book and Purchase Register	Cash Book and General Ledger.

In the case of 'A' category, units, in addition to records maintained as indicated above, there are also other records required to be maintained under import Trade Control or Drug Central regulations or for Cost Audit purposes which have a bearing on purchases, stocks and sales.

20. FINANCIAL ACCOUNTING

Both in the case of 'A' and 'B' category units the financial accounts are maintained on a mercantile basis and are audited, though the periodicity of audit as between 'A' and 'B' categories varies. Similarly, trial balances are also prepared though the frequency thereof as between the two categories varies. In the case of 'C' category units, however, the practice is far from uniform. The more common practice is to draw up annual accounts. It is seen that auditing is also not done on a regular basis.

21. RELIEF FROM INPUT TAXATION

Out of the units surveyed some are beneficiaries of tax set off under rule 56-A or full tax exemption under Chapter X of the Central Excise Rules. While no serious misgivings about the procedural requirements were expressed it was noticed that the benefit accruing to them under this provision under rule 56-A was not substantial. It is seen, however, that the amount of tax credit (viz. proforma credit) given to the manufacturers in respect of inputs is usually not taken into account while pricing the final products. In other words, the net cost of an input is arrived at after deducting the proforma credit amount from the cost of raw materials for working the cost of production and providing a mark-up thereon. Thus, we find that the profit mark-up does not generally fall on the tax element of such of these inputs which are eligible for proforma credit facility. The normal time lag between the procurement and utilisation of inputs brought under proforma credit is seen to be varying between one month to three months. The utilisation of proforma credit is, however, seen to be made a little earlier than this period.

22. A study of the tax compliance costs for excise purposes reveals the following position - TAX COMPLIANCE

Category	No. of persons employed	Cost (Kg.) per annum
A	2 to 9	12000 to 1,44,000
A-2	1 to 4	6000 to 35,000
A-3	1 to 2	5000 to 15,000
B-1	1	3000 to 5,000
B-2	Proprietor/partner himeself part-time employee	Not available
C	Proprietor partner himself	Not available

A distinct feature is that in the case of smaller manufacturers the proprietor or one of the partners looks after the work of compliance. On the other hand, the bigger manufacturers are able to employ persons to look after the work of compliance with the various excise regulations.

23. VIEWS ON MANVAT

As mentioned earlier, the opinions of manufacturers on VAT in lieu of excise was also ascertained. In general, it was found that smaller manufacturers had very little idea of how the VAT oparates. In fact, their plea was for shifting excise to basic inputs stage rather than finished products or else for having very minimum checks for tax purposes. While they could not give their views on the suitability of a VAT system they mentioned that even the present system of accounting as required under excise and sales tax laws imposed a great strain on them. It was urged that whatever the system it should be made simple in operation involving the minimum of checks. The opinion among bigger manufacturers on the accounting rigours under a VAT system and the benefits that may accrue under the VAT system was somewhat divided. Some felt that VAT in lieu of excise would certainly be an improvement on the existing system. As for accounting requirements, they felt that the present excise and sales tax requirements together entail maintenance of records of different nature which could well be adopted under the VAT system also without any difficulty. One view was that the cost advantage that may be derived from a switch over to VAT would far out weight its other disadvantages like counting requirements etc.

24. There was also the other view expressed by a Chief Executive of one of the bigger manufacturers who felt that the VAT system did not have any advantage over the existing system. In fact, he felt that the system would not only add to complications for smaller units but also for bigger units and lead to higher prices to the consumers. It was opined that there would be no guarantee that the manufacturers would reduce their ex-factory prices even if provision for credit of inputs was made. This is so, because pricing is not as much dependent on the tax paid on inputs or on profit margins as on competition and marketing factors. Doubts were also expressed on delays likely to occur in claiming appropriate credits under the VAT system.

III.- DEGREE OF DOCUMENTATION AND GAP - AN EVALUATION

25. DOCUMENTATION UNDER VAT

Under the VAT system the invoice is the key document. In concrete terms, therefore, an invoice under the VAT system must contain the following details:

(i) date of invoice ;

(ii) name, address and registration number of suppliers;

(iii) purchaser's name;

(iv) description of goods;

(v) price charged for the goods - separately for each rate category; and

(vi) rate and amount of tax payable on the total.

Further, each invoice is required to be serially numbered and prepared in duplicate. A specimen copy of the invoice which has been prescribed under the Irish VAT system is appended as Exhibit 1.

26. In addition to the invoice, to comply with the basic requirements of the scheme and also maintain control internally, both sales and purchases need to be listed in some form of permanent record though not statutorily prescribed. First, details of each sale should be recorded invoice-wise. There must be an analysis to show the value of the goods and the tax charged for each of the rates of tax under the scheme. At the end of each accounting period, (or less for internal requirements) a reconciliation is required to be made between the tax and the sales for each rate category and these brought together to agree with the total invoice values charged to customers. The reconciliation of the tax can be taken by finding the tax percentage due on the total sales and this shows the need to separate the various charging categories. Each entry in this list must bear a separate number, preferably in series, and this same number should also appear on every copy of the invoice. This is to allow the original documents to be found easily should it be required to trace back from the book record.

27. Secondly, the purchases are also required to be listed but the entries need not be so detailed. The columns which are needed for tax purposes are to show the tax paid, the actual purchase

value of the goods and the total of the invoice. There should generally be no need to split this information into separate tax-rate categories. A specimen of the purchase record maintained under the Irish system is given in Exhibit 2.

28. At the end of each accounting period, an assessment return has to be submitted by the taxpayer. A copy each of the return presently in operation in the United Kingdom and Denmark is given in Exhibits 3 and 4. The simplest of the returns is the Danish VAT form since the rate applicable there is only one. In the other cases, the return is more detailed on account of rate differentiations. However, in short, the return seeks to estimate the tax due and the tax deductible to arrive at the net tax payable. The information to be recorded in summary form in this return bears a relation to the purchase and sales invoices and the two basic records relating to purchases and sales.

29. Summing up, the main documentation requirements under a VAT system are the invoices for both sales and purchase, the purchase record and the sales records and submission of a periodic return showing the details of purchases, sales tax charged to customer, the tax credit claimed etc.

30. Comparing the present documentation which has been detailed in Section II of this study and the documentation required under VAT, we reach the following conclusions:

A COMPARISON OF THE DOCUMENTATION UNDER THE EXISTING SYSTEM AND VAT SYSTEM

(a) In general, manufacturers whose turnover exceeds Rs. 15 to Rs. 20 lakhs per annum get most of their inputs under cover of regular invoice.

(b) These invoices evidencing purchase of various types of inputs contain, by and large, particulars which, are required in an invoice under the VAT system. However, while in respect of supplies received from manufacturers the invoice and the excise gate pass together contain more than adequate particulars, the invoices for purchases made from dealers fall short of one basic requirement under VAT i.e., they do not show the excise duty amount.

(c) In the matter of accounting of purchases, production, sales and stocks and level and extent of coverage would appear to be adequate for VAT purposes also.

(d) In the case of manufacturers whose turnover is less than Rs.15 to Rs.20 lakhs our assessment is that accounts maintained in regard to purchases, production and sales give reasonable details though the system of accounting itself does not have the level of sophistication that larger manufacturers have. This category of manufacturers maintain what may be said to be adequate accounts but it may be necessary for them to make them more detailed to comply with the book-keeping requirements under VAT. In their case, a large portion of their purchases are from dealers who do not indicate the excise amount separetely in their invoices. A major documentation gap arises in this area which would need to be rectified if these manufacturers are to be subject to normal VAT system.

31. FEASIBILITY OF MANVAT

From the foregoing comparative study, it can be reasonably concluded that the basic functional requirements under VAT, namely, the issue of invoice, the maintenance of record relating to purchase and sales are not likely to place a heavy burden on manufacturers whose annual turnover is in excess of Rs.15 to Rs.20 lakhs.

In the case of those having a turnover less than Rs.15 - Rs.20 lakhs, per annum, a switchover to VAT may mean more elaboration of their existing records if they are required to comply with the regular VAT requirements. Considering the fact that under the VAT we would only have an invoice, the present excise gate pass and the sales invoice could be suitably merged into one document and to that extent the effort on the part of the manufacturers could be minimised.

32. But for both bigger and small manufacturers the problem of making the dealer's invoices meet the basic requirements of a VAT system is one that needs serious consideration since presently the excise duty paid on the product is not indicated in them, with the result, availing of tax-credit and entering in the purchase records of tax paid at earlier stage will present difficulty to the manufacturers who buy their inputs from dealers more particularly the smaller manufacturers.

VALUE-ADDED TAX

No special form of invoice is prescribed for use in relation to value-added but an invoice must contained the following details:—

date of invoice,
name, address and registration number of supplier,
description of goods or services,
amounts of consideration, and
rate and amount of tax payable on the total consideration for each tax category.

An invoice must be issued by very accountable person in respect of every taxable transaction with any other accountable person.

A copy of the invoice must be retained by the seller and the actual invoice must be retained by the purchaser for six years except where a lesser period is authorised by the inspect of taxes.

INVOICE

Number 000121

Date.....

From:	To
WHOLESALE LTD 1820 MAIN ST. CORA Registration Number VAT	Retail Sales Ltd., 35-41 Main St., Dublin.

Goods or Services		Cost exclusive of value added tax	Rate of V.A.T. applic-able	Amount of V.A.T.
Quantity	Description	£	%	£
4	CARTONS OF SOAP	6.54		
2	CASES OF DETERGENT	5.24		
		11.78	16.37	1.93
4	BOXES OF BISCUITS	6.20		
6	CARTONS OF CEREALS	12.00		
		18.20	5.26	0.96
		29.98		2.89
TOTAL AMOUNT PAYABLE		£32.87		

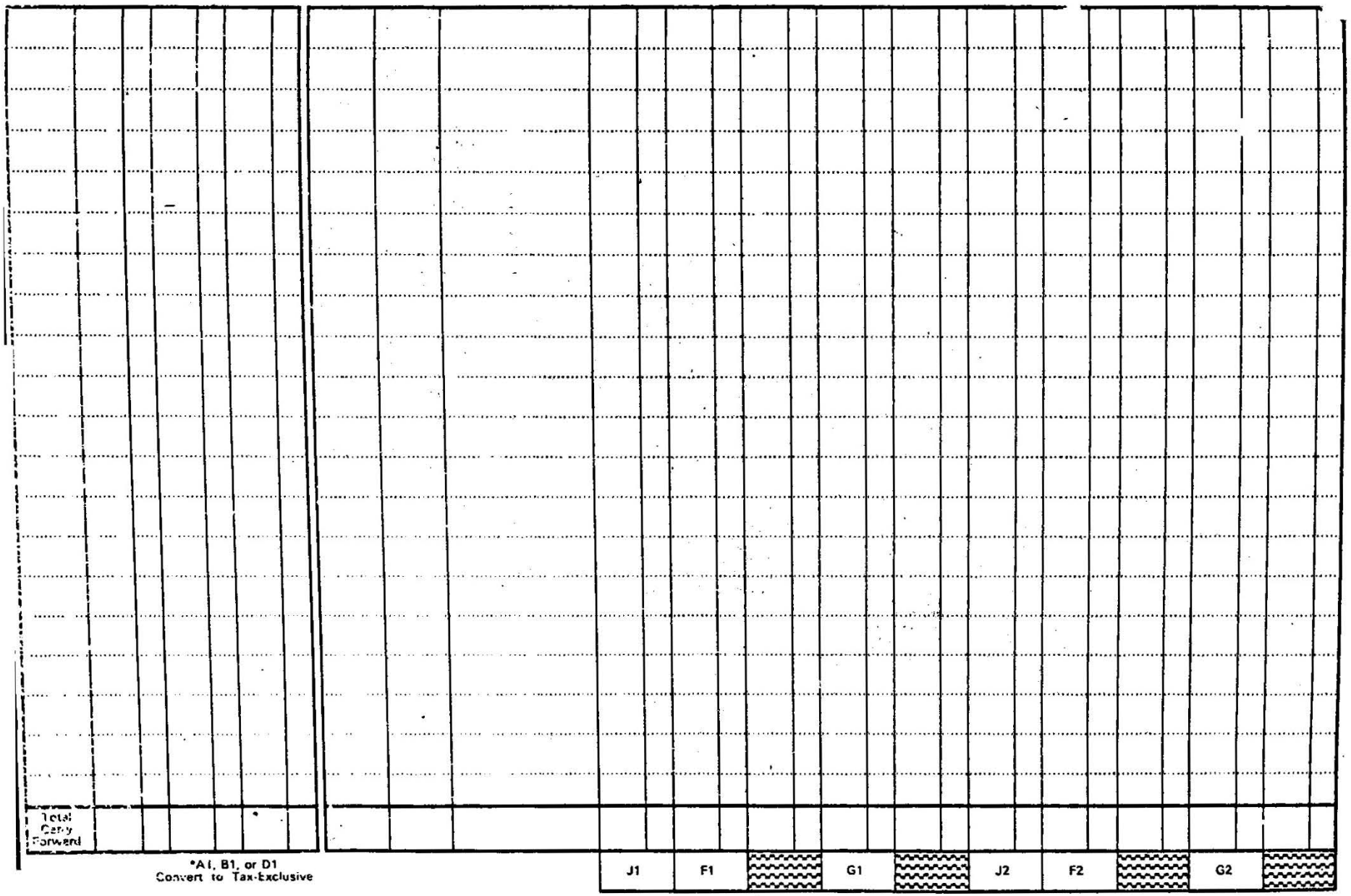
VAT 5

VALUE-ADDED TAX

Record of purchased and daily receipts

DATE OF RECEIPT	CASH RECEIPTS INCLUSIVE OF VAT			PARTICULARS OF INVOICE			PURCHASES FOR RESALE					PURCHASES NOT FOR RESALE (Do not include Cars or Petrol)				
	(a) Net Receipts	(b) Cash Payouts & Drawings	(a+b) Gross Receipts	DATE	Trader's Filing Ref. No.	NAME OF SUPPLIER	@ ZERO RATE	@ LOWER RATE		@ STANDARD RATE		@ ZERO RATE	@ LOW RATE		@ STANDARD RATE	
							PRICE	PRICE EXCL VAT	VAT	PRICE EXCL VAT	VAT	PRICE	PRICE EXCL VAT	VAT	PRICE EXCL VAT	VAT
	£	£	£				£	£	£	£	£	£	£	£	£	£

762


Total
Carry
Forward
*A1, B1, or D1
Convert to Tax-Exclusive
J1
F1
G1
J2
F2
G2

Return of Value Added Tax
for the period

Registration No. Period No.

The registered person named here must complete and return the form to VAT Central Unit, H.M. Customs and Excise, Alexander House, 21, Victoria Avenue, Southend-on-Sea X, SS99 IAB. not later than

A pre-paid addressed envelope is enclosed. Any tax payable must be paid by the same date.

Before completing any item on this form please read the appropriate note; the paragraph numbers in the attached notes correspond to the numbers of the items on the form.

Note: A return which is incomplete or qualified in any way (e.g. marked "Provisional") does not satisfy the legal requirements. Failure to make a return or to pay the full amount of tax payable by the due date is an offence.

PART A. Account of tax payable or repayable
This part must be completed by all registered persons. Please complete all boxes. Writing 'NONE' where there is no amount to be entered.

Tax due for this period :	Output tax	1	
	Tax on imported goods and ex-warehouse	2	
Under declarations and/or under payments of tax in respect of previous periods	Notified by Customs and Excise	3	
	Other	4	
Total tax due :	Sum of boxes 1 to 4	5	
Deductible input tax for this period:		6	
Overdeclarations and/or overpayments of tax in respect of previous	Notified by Customs and Excise		
	Other	8	

Total tax deductible :			Sum of boxes 6 to 8 - 9
Net tax payable or repayable If the amount in box 5 is greater than that in box 9 tax is payable to Customs and Excise.	than	Payable to Customs and Excise	...
If the amount in box 9 is greater than that in box 5 tax is repayable by Customs and Excise.	than	Repayable by Customs and Excise	...

(Please tick appropriate box).

Method of payment of Customs and Excise.	National Gire	....	Bank Gire	....	Remittance enclosed ....
(Please tick appropriate box).		....		....	

PART B. Value of outputs and inputs (excluding any tax)
This part must be completed by all registered persons.
Please complete all the boxes, writing 'NONE' where there is no amount to be entered. Pence should be disregarded.

Output :	Outputs chargeable at the standard rate of tax	11
	Exports	12
	Other zero-rated taxable output	13
	Total taxable outputs (sum of boxes 11, 12 and 13)	14
	Exempt outputs	15
	Total outputs (sum of boxes 14 and 15)	16
Inputs :	Total taxable inputs including zero-rated inputs	17

PART C. Retailers' special schemes

This part must be completed by retailers who use any of the special schemes for the calculation of output tax described in Notice No. 707.

Enter in the box(es) : 1 if you have used scheme 1, 2, 3 or 4 if you have used any of these schemes 18

PART D. Calculation of deductible input tax

Except as explained in the notes, this part must be completed by all partly exempt persons; it need NOT be completed by any other registered persons.

Enter 1, 2, or 3 in this box to show which method you have used _____ 19

Amount of any input tax wholly attributable to taxable supplies 20

Amount of input tax partly attributable to taxable supplies 21

Percentage used to attribute input tax $\frac{\text{box 14 X 100}}{\text{box 15}}$ 22

That part of the amount in box 21 which is deductible for the period $\frac{\text{box 21X box 22}}{100}$ = 23

Total deductible input tax for the period (sum of boxes 20 and 23); this total should also be entered at box 6 overleaf 24

PART E. Declaration by the signatory
This part must be completed by or on behalf of all registered persons

I _____
(full name of signatory in BLOCK CAPITALS)

declare that (i) the information given in this return is true and complete in respect of all business or businesses carried on by the registered person except in so far as he is separately registered if so required and that, except as notified, one of the changes listed in Notice No. 700 i.e. occurred during the period covered by the return.

(ii) The amounts shown as deductible input tax in this return relate to tax which may be deducted by virtue of Section 3 of the Finance Act, .72 and regulations made under that Section, and I claim deduction of input tax accordingly.

(iii) where I have used one of the retailers' special schemes I have complied with Notice No. 707.

Signed _____
director,

Date _____

*Delete as necessary

BEFORE RETURNING THIS FORM PLEASE DETACH THE NOTES*

*Reproduced from Specimens issued by the Customs and Excise Authorities. The accompanying notes are not available at the time of going to press.

Illustration 1 DANISH VAT FORM

Value Added Tax
TAX ACCOUNTING

Date	Purchases			Sales			Comments
	1 Purchase price including VAT	Tax Credit		4 Joint price	5 Tax payable	6 VAT deductible on exports	
		2 Domestic purchases	3 on own imports				

Illustration 2

Value Added Tax
DECLARATION

Taxable Period

Kroner (rounded)	Specification
	Tax payable
	Tax deductible
	Tax liable

Signature

LETTER

Official Paid

194

To
Tax Service
Postbox 297

Co-penhagen V

Space reserved

APPENDIX - 22

MANVAT SYSTEM FOR COMMERCIAL VEHICLES - A MODEL*

There exists, at present, a multiplicity of indirect taxes applicable to the manufacture and sale of products, viz. excise, customs (with countervailing duties), and sales tax. Though the totality of these taxes could be replaced by MANVAT, we have considered in this exercise two alternatives :

Alternative I : MANVAT to replace excise duty

Alternative II : MANVAT to replace excise and customs duties (exclusive of the protective element of 20%).

2. Restricting thequantification exercise to the vehicle manufacturing stage and the immediate preceding stage, inflationary effects because of tax on mark-up can be computed as follows :

(1) Increase in price at the preceding stage :

Tax-exclusive inputs : X_i 1 in Rs.

Effective (total) input tax rate : t_i 1%

Input tax = X_i 1 t_i 1 in Rs.

Mark-up : M_1 %

'Nominal' (direct output tax rate) : t_o 1%

Increase in price due to mark-up in input tax.

$$\Delta P_1 = (X_i\ 1\ t_i\ 1)\ M_1\ (1 + t_o\ 1) \text{ in Rs.}$$

---

* Adopted from a special study made by Shri Asit Chandmal with reference to a TELCO truck/bus chasis.

(2) Increase in price at the vehicle manufacturing stage :

Tax-exclusive inputs : $X_i 2$ in Rs.

Effective(total input tax rate : $t_i 2\%$

Input tax = $X_i 2 \quad t_i 2$ in Rs.

Mark-up : $M_2\%$

'Nominal' (direct) output tax rate : $t_{02}\%$

Cumulative increase in price due to mark-up on input tax at the two stages,

$$\Delta P_2 = \Delta P_1 + (\Delta P_1 + X_i 2 \quad t_i 2) \quad M_2 (1+t_o 2) \text{ in Rs.}$$

(3) In general, the increase from stage i to stage (i+1) is

$$P_i+1 - \Delta P_i = (\Delta P_i + X_i + 1 t_i 1) (M_{i+1}) \quad (1+t_i 2)$$

Summing all these increases, i.e. $\sum_{i=o}^{n} (\Delta P_i+1 - \Delta P_i)$

gives the total increase in price due to mark-up on tax.

For TELCO vehicles, our calculations show :

(1) Inputs to TELCO (i.e. preceding stage) :

The inflationary impact on price (i.e. ΔP_1) because of mark-up on tax by the component manufacturers would range from Rs. 275 to Rs.800 per truck (since mark-ups are between 5% and 15%).

(2) At TELCO :

For an average mark-up of 5%, the inflationary impact on price ($\Delta P_2 - \Delta P_1$) works out to Rs.960 - Rs. 1,000 (for mark-ups of 5% to 15% respectively at the preceding stage).

The total inflationary effect on the vehicle price (ΔP_2) because of mark-ups at the last two stages of manufacture would range from a minimum of Rs. 1,200 to as much as Rs, 1,800.

Working Capital Requirements

4. Indirect taxes are levied at all stages of manufacture, (i.e. on all bought-out raw materials, semi-finished and finished components). There is at present no comprehensive provision for credit/ exemption of all taxes on manufacturing material inputs and hence inventory values are inflated to this extent. In other words, additional working capitals required because of the tax element in material input costs. We estimate that this additional requirement is of the order of Rs. 28.6 crores for TELCO and its suppliers.

5. Details of the above calculations have been given in Schedule 3, Table 1. These give the tax content in working capital requirements (for inventory holding) at the component and vehicle manufacturing stages. The figures indicated therein correspond to a production level of one vehicle per month. At the estimated production rates of 26,000 TELCO vehicles and production in the ratio of 1 : 2 for supply of original equipment (i.e. to vehicle manufacturers) and the replacement market, tax content in working capital locked up works out as follows :

TELCO commercial vehicles :

	(Rs. in crores)
(i) At TELCO	15.37
(ii) Ancillaries	13.24
	28,61

6. At an interest rate of 15% the inventory-carrying costs because of the tax content alone work out to Rs. 4.29 crores for TELCO vehicles. The consequent inflationary impact on the vehicle price is of the order of Rs. 1,625 per truck.

7. In our calculations in Schedule 3, we have made a credit provision for "tax realisation on sales". This represents an average of half a month's sales tax revenues collected by the manufacturer from the customers. This adjustment is necessary since sales tax is to be paid by a manufacturer to the Government on a monthly basis. In the case of exports, sales tax is not levied, and hence such credit would not be available.

8. The average stock levels shown in Tables 1 and 2 represent estimates on the basis of analysis of inventory of a number of manufacturers in the automobile industry (Schedule 3, Table 3).

9. Thus the total inflationary impact per truck is Rs. 2, 825 to Rs. 3, 425 (1, 625 puls 1, 200 to 1, 800)

Exports ; Duty Drawback

10. Under the present duty drawback system, sales tax on all direct material inputs are not refunded. Further, no duty on indirect materials is refunded. At best, subject to the production of an auditor's statement, and subject to individual ceilings and estimates (where accurate data is not available), the duty drawback benefit is available for excise, customs and countervailing duties paid on direct material inputs.

11. For a TELCO truck, the drawback benefit allowed is of the order of Rs.10,900. This means that about a third of the total taxes on the inputs still remain in the export prices. This is one of the factors which results in the products being uncompetitive in international markets.

Vertical Integration:

12. As the present system of multi-stage results in a 'tax on tax' (cascading), the element of total tax increases disproportionately with the number of stages in the production/distribution cycle. In order to minimise total tax incidence firms would thus tend to integrate vertically.

13. Specifically the consumer price is higher if value added is greater at the earlier stages. Algebraically, for a two-stage model, let

Total value added in the two stages 1 and 2 = V

Value of input at stage 1 = 0 (zero)

Value added at stage 1 = A = (V - B)

Value added at stage 2 = (V - A)

Nominal tax rate at output of stage 1 = t_1

Nominal tax rate at output of stage 2 = t_2

Then,

Input price at stage 2 = $A(1 + t_1)$

Consumer price, P (after tax at output of stage 2)

$$= \overline{\underline{A(1 + t_1)} + \underline{B}} (1 + t_2)$$

$$= \overline{\underline{A(1 + t_1)} + (V - A)} (1 + t_2)$$

$$= (V + At_1)(1 + t_2)$$

or

$$P = \overline{\underline{V + (V - B)t_1}} (1 + t_2)$$

$$= \overline{\underline{V(1 + t_1)} - Bt_1} (1 + t_2)$$

$$\frac{\delta P}{\delta A} = t1 (1 + t_2)$$

$$\frac{\delta P}{\delta B} = -t1 (1 + t_2)$$

Since $t_1, t_2 \gtrless 0$, $\frac{\partial P}{\partial A} \gtrless \frac{P}{B}$

and $\frac{\partial P}{\partial A} - \gtrless 0$ and $\frac{\partial P}{\partial B} \lessgtr 0$

In other words, for a constant total value added, the final price increases with an increase in the value added at the initial stages. This conclusion is independent of the nominal tax rates at the different stages.

14. Thus the proposition is mathematically proved and this is a major dafect of the present system, viz. it encourages vertical integration.

Government Revenues :

15. As we have already seen, the incidence of taxation on the automobile industry is very high. At a production level of 26,000 vehicles per annum, the manufacture and sale of TELCO vehicles alone contribute approximately Rs. 90 crores to the exchequer.

Computation of MANVAT Rates and Structure Rationalisation

Computation ofMANVAT Rates :

16. The computation exercise starts off at the stage where quantification of present tax incidence ends. For Commercial vehicles, we have arrived at four different series of MANVAT rates (Schedule 1, Tables 6, 7 and 8). The methodology is as follows :

(1) Four different types of "visible" taxes are incident on a finished product and the range of manufacturing inputs at the different production stages. These are: excise duty, customs duty (including countervailing duty), sales tax and octroi duty. In this exercise, we cover the final vehicle and the immediately preceding stages, all "visible" taxes at previous stages being "invisible" and clubbed together under the term "Built-in Taxes" ("Built-in Taxes" plus "Base Taxes" of Table 2).

(2) We have computed MANVAT series (A & B) of MANVAT rates covering these taxes. The series are defined as follows : Series A rates represent the replacement of excise duty alone by MANVAT ; Series B represents the replacement of excise and customs duties exclusive of the protective element.

(3) It has been found that the total tax structure (in terms of A & B Series) is not sensitive to the actual protective element in customs duty in the range of 10%

to 30%. Accordingly, for the purpose of all future calculations a 20% protective element in customs duty has been assumed.

(4) Component manufacture input stage (suffix 1 : A 1, B 1,). The different tax bases and the tax elements on component manufacturers' inputs are defined as shown below. VAT rates for computation of VAT credits on component manufacturers' inputs are arrived at by dividing each tax component by the applicable tax base (Schedule 1, Table 6).

Tax Base (T.B.)		Tax Component to be recovered as MANVAT
A1 :	Tax-exclusive input costs to component manufacturer plus built-in taxes.	Excise duty on inputs.
B1:	A1 plus 20% customs duties on inputs.	(Excise duty + 80% customs duty) on inputs.

(5) Vehicle manufacture input stage (Suffix 2 : A 2, B 2) : The different tax bases, and the tax components to be recovered as MANVAT at the point of sales from component manufacturers to vehicle manufacturers, are defined as shown under. Appropriate MANVAT rates for obtaining credit on the vehicle manufactuer's inputs are arrived at by dividing each tax component by the applicable tax base. (Schedule 1 Table 7).

Tax Base (T.B.)		Tax Component to be Recovered as MANVAT
A2 :	Total (tax-inclusive) input costs to component manufacturer (-) excise duty on inputs (+) value added by component manufacturer.	'Excise duty on inputs to 'component and vehicle 'manufacturers = Total 'excise duty. ' '
B2:	A2 (-) 80% customs duty on component manufacturer's inputs.	'Total excise duty (+) '80% customs duty on 'component manufac- 'turer's inputs. "

The input "invisible" taxes in respect of raw materials, miscellaneous auto and electrical components, and indirect and other materials have been estimated and corresponding A2 and B2 MANVAT rates have also been obtained. (Schedule 1, Table 8).

The above estimation of "invisible" taxes has been done assuming the percentage break-up of excise, customs and sales tax as per the distribution of known items (Schedules 1 Table 1) and the final VAT rates are not sensitive to changes in these percentages.

By additing on "value added" at the vehicle manufacturing stage, and the excise duty and sales tax on the finished vehicle, A and B type MANVAT rates for the finished vehicle have been obtained (Schedules 1. Table 9).

17. After detailed computations, we have arrived at appropriate MANVAT rates in the series A & B and as applicable to the finished vehicle, to vehicle manufacturer's input and to the component manufacturers' inputs. Each tax rate is different from the other. This has resulted precisely because of the attempt to maintain revenues and prices generated by erratic, multi-rate, multi-stage ('cascading') taxation. The next major exercise in MANVAT design, therefore, would be structural i.e., rate rationalisation.

Structural Rationalisation:

18. Having obtained item-wise MANVAT rates applicable at the different stages along the manufacturing cycle, rate rationalisation is attempted employing cluster analysis techniques. For each of the series A1, B1, and A2, B2, points can be marked on an one-dimensional axis, each point representing the MANVAT rate for one item (i.e. a component or a group of components). Where clusters appear, a common MANVAT rate can be applied to the total grouping. Further improvisations may be necessary to obtain logical groupings in terms of component types or to maintain groupings at different stages along the production cycle. In addition, integer value rates in multiples of five can be fixed for computational and administrative simplicity.

19. In the above rationalisation process, care has to be taken to see that input and output MANVAT rates (T_1 and T_2 respectively) are not so structured that a manufacturer gets a cumulative net credit. Algebraically, if tax-exclusive inputs are Xi and value added is VA, $Xi\ T_1 < (Xi + VA)\ T_2$, or $T_1/T_2 - 1) < (VA/Xi)$ are necessary conditions to be met.

20. Such an exercise was carried out for commercial vehicles, the final recommendations on applicable MANVAT rates are tabulated in Tables A, B and C appended to this study.

Impact of Introduction of MANVAT

Cascading:

21. It is evident that the present system results in cascading and resultant unintended and erratic inflationary effects. While the MANVAT system preserves the total effective tax, it eliminates cascading, by the system of credits on inputs. In particular, effective tax rates would no longer be erratic and the effect of tax rate changes would be precisely forecast (subject to the availability of accurate consumption statistics).

Mark-up on Tax:

22. It was shown that, depending on the actual mark-up rates in the industry, the inflationary impact on the consumer price of a commercial vehicle, because of mark-up on present taxes, is of the order of Rs. 1,200 to Rs. 1,800.

23. In order to gauge the likely change in consumer price because of the elimination of mark-up on tax by a change-over to MANVAT, the following mathematical preliminaries are useful :

(1) Notations

Value of tax-exclusive inputs : Xi in Rs.

Effective (total) input tax rate : t_1 %

'Nominal' (direct) output tax rate : t_0 %.

Mark-up : M %

Value Added : VA in Rs.

Consumer Price : P in Rs.

Total Tax : T in Rs.

(2) Algebric Relationships :

(i) Present Consumer Price

$$P1 = \left[Xi\,(1 + ti) + VA \right] (1 + M)\,(1 + t_0)$$

(ii) Total Tax

$$T = Xi\,ti + \left[Xi\,(1+ti) + VA \right] (1 + M)\, t_0$$

(iii) MANVAT Rate

$$\text{MANVAT Rate} = \frac{T}{(Xi + VA)\,(1+M)}$$

(iv) Consumer Price under MANVAT

$$P_2 = (Xi + VA)\,(1 + M)\left[1 + T/(Xi + VA)\,(1+M)\right]$$

(v) Change in Price Because of Switch-over to MANVAT

$$P_1 - P_2 = Xi\,(1+M)\left\{ (1 + ti + VA/Xi)\,(1 + t_0) - (1 + VA/Xi)\left[1 + \frac{(T/Xi)}{(1+VA/Xi)\,(1+M)}\right] \right\}$$

Where $T/Xi = (ti + (1 + ti + VA/Xi)\,(1 + M)\, t_0$

24. After substitution of appropriate values in the above equation, the reduction in the price of commercial vehicle, taking the final vehicle manufacturer's stage alone works out to approximately Rs. 600.

25. Similarly, there should be a fall in prices of components for both O.E. and replacement markets. This, in turn, would lead to a further reduction in price at the vehicle manufacturing stage.

26. We have not attempted to exactly quantity the anticipated deflationary impact on price because it is very sensitive to the values of the parameters in the equation. Having illustrated the case for a TELCO commercial vehicle, we emphasise that this further deflationary effect could be substantial.

Working Capital Requirements :

27. In Table 1 of Schedule 3, we have shown the additional working capital requirements because of tax component in inventories under the present system. Also computed therein are working capital requirements because of the tax component in inventories under a system of credits under MANVAT.

28. Two considerations are important in this context :

(a) Because of the system of credits, the tax component in inventories would, in general, be only the total of built-in taxes and the protective element in customs duty. This quantum is negligible viz. hardly 3% of the present total taxes.

(b) Assuming regular (viz. daily) purchases and sales, the manufacturer would have to look-up working capital for total taxes on his inputs for a period representing half the MANVAT period. Similarly, as he has to pay net taxes to the Government only at the end of this period, he would have with him, for use as working capital, MANVAT collections on his sales for half the period. We have accounted for this in our calculations. For exports, however, no MANVAT is levied. The MANVAT collections would hence be correspondingly lower.

29. The net impact of these considerations is that working capital locked up in tax component in inventories reduces substantially, in fact it even becomes negative, i.e. industry would use zero cost government money to finance its working capital needs. We have attempted a sensitivity analysis giving two possible periods for MANVAT collections by Government. As can be seen from the tables, for a 3 month period almost all sectors of the economy would enjoy net Government credits. Understandably, this would be quite unacceptable. Hence we recommend a one month period of net MANVAT payments to Government. Even with this reduced period, at the commercial vehicle manufacture stage, the net working capital requirements on account of tax are negative. To offset this, we recommend that the Government collect a deposit from such manufacturers. The deposit amount should be so fixed that a situation would not arise whereby manufacturers get zero cost Government funds for working capital. We comment on this in detail in the subsequent section on MANVAT administration.

30. Assuming a 1-month MANVAT payment period and the estimates given in Tables 1, Schedule 3, typical working capital requirements of the industry should work out to :

	Rs. in Crores
TELCO Commercial Vehicle	
(i) Vehicle manufacture stage	(1.01)
(ii) Ancillaries (O.E. plus 200% of O.E. for replacement market)	0.96
	(0.05)

31. For the above computations, an annual production level of 26,000 commercial vehicles has been assumed. At 15% interest rate, the total (net) deflationary impact on vehicle prices under MANVAT is as follows :

Commercial Vehicle (TECLO) (A fall of Rs. 3 as compared to a rise of Rs. 1,625 at present)	Rs. 1,628

It is obvious that the introduction of MANVAT would produce a vitally needed deflationary impact on prices.

Exports :

32. We have seen at an earlier stage that an exporter is allowed excise duty drawbacks on his direct material inputs. In addition, no sales-tax and any local taxes would be levied on the finished product which is earmarked for exports. For example, the duty drawback so available for TELCO amounts to approximately Rs. 11,000. This is roughly two-thirds of the total indirect taxes. Under MANVAT virtually full credit would be made available by zero-rating of the export consignment. This facility would enhance export opportunities in the competitive international market.

Vertical Integration :

33. We had seen that the present system of indirect taxation inherently favoured vertical integration. MANVAT is neutral with respect to, the stage at which value is added is greatest; the total number of stages; and the tax rates applicable at these stages. The total tax element depends only on the VAT rate at the final stage and is independent of taxation rates at all intermediate stages (catching-up effect).

TABLE A

MANVAT RATES : MAJOR COMPONENTS

DESCRIPTION	"VAT" RATES FOR CREDIT TO COM. MANUFACTURER		"VAT" RATES FOR SALES TO VEHICLE MANUFACTURER		PRESENT NOMINAL RATES
	A_1	B_1	A_2	B_2	EXCISE
1. Tyres and Tubes	5%	5%	10%@	10%@	55%
2. Battery	N.A.	N.A.	5%@	20%@	17.5%
3. Fasteners	10%	15%	15%	20%	10%
ENGINE PARTS :					
4. Piston Assembly	10%	20%	5%	10%	— **
5. Gaskets	5%	20%	5%	15%	— **
6. Engine Valves	1%	15%	1%	10%	—
7. Carburettors	1%	20%	1%	10%	—
8. Fuel Injection Pump	1%	5%	1%	5%	—
9. Fuel Pump	1%	25%	—	30%	—
10. Nozzle Holder	1%	5%	1%	5%	— **
11. Fuel Filter	1%	10%	1%	10%	—
12. Oil Filter	1%	5%	1%	5%	—
13. Radiator	1%	30%	1%	20%	—
14. Bearings	1%	25%	15%	40%	13.6%
15. Bimetal Parts	1%	30%	1%	20%	0.6%
16. Master Cylinder	1%	5%	1%	5%	—
ELECTRICAL PARTS :					
17. Starter Motor	10%	15%	25%	25%	20%
18. Dynamo	10%	10%	5%	5%	—

TABLE A

MANVAT PARTS : MAJOR COMPONENTS

DESCRIPTION	"VAT" RATES FOR CREDIT TO COM. MANUFACTURER		"VAT" RATES FOR SALES TO VEHICLE MANUFACTURER		PRESENT NOMINAL RATES
	A_1	B_1	A_2	B_2	EXCISE
19. Distributors	1%	5%	1%	5%	—
20. Ignition Coil	15%	15%	15%	15%	—
DRIVE, TRANSMISSION PARTS:					
21. Propeller Shaft	1%	5%	1%	5%	—
22. Clutch Assembly	5%	5%	5%	5%	1.4%
23. Tie Rods & Drag Links	1%	5%	1%	5%	—
24. Steering wheel	10%	15%	5%	10%	—
25. Wheels	1%	25%	5%	30%	2%
26. Gear Box	N.A.	N.A.		5%	—
SUSPENSION, BRAKING PARTS:					
27. Shock Absorbers	10%	15%	10%	15%	— **
28. Hydraulic Brake	2%	5%	1%	5%	—
29. Brake Assembly	1%	5%	1%	5%	—
30. Coil Springs	5%	5%	5%	5%	—
EQUIPMENT :					
31. Head Lamps	1%	10%	1%	5%	—
32. Wiper Motor	10%	10%	25%	25%	22.5%
33. Other Instruments	1%	10%	1%	5%	—
34. Glass	20%	20%	15%	20%	—
MISCELLANEOUS COMPONENTS:	N.A.	N.A.	5%	5%	1%

Notes : 1. @ The present rates for trucks are substantially higher since no exemption of excise is available on fitments as original equipment.

2. (**) These items would bear excise duty when sold as a spare part.

TABLE B

MANVAT RATES : IMPORTS BY VEHICLE MANUFACTURER

DESCRIPTION	"VAT" CREDIT RATE	PRESENT NOMINAL RATE
Steel	40%	55% *
Non-ferrous Metal	70%	102%
'CKD' Components	95%	136%
Bearings	95%	154%
Steel top rings	95%	155%
Oil Rings	95%	166%
Others	70%	108%

TABLE C

MANVAT RATES : SALE OF TRUCKS

	"MANVAT" RATE	
	A_3	B_3
TELCO Vehicle	25%	30%

Note: (*) In addition, octroi duty is levied at 4% in Bombay. The nominal rate inclusive of octroi duty is 31.9%.

Schedule 1 : Table 1

TELCO TRUCK : TOTAL INCIDENCE OF INDIRECT TAXES

	TYPE OF TAX (1)	AMOUNT (Rs.) (2)	PERCENT - I (3)	PERCENT - II** (4)
1.	"Built-in-Tax" plus "Base Tax".	394	0.95%	
2.	20% Customs Duty*	1,037	2.51%	
		1,431	3.46 %	
3.	Excise Duty	16,920	40.95%	47.44%
4.	80% Customs Duty	4,148	10.04%	11.63%
5.	Sales Tax (Maharashtra)	14,599	35.33%	40.93%
		35,667	86.32%	100.00%
6.	Octroi :			
	(a) Component & Vehicle Mfr.	24	0.06%	
	(b) TELCO Vehicle (Bombay)	4,197	10.16%	
		4,221	10.22%	
	TOTAL	41,319	100.00%	

Note: 1. (*) This represents the assumed protective element in Customs Duty.

2. (**) These percentages relate to the types of taxes proposed to be covered by MANVAT.

Schedule 1 : Table 2

TELCO TRUCK : INPUT COSTS TO COMPONENT MANUFACTURERS

(Figures in Rupees)

	DESCRIPTION	INPUT COSTS EXCLUDING TAXES	"BASE TAX"	"BUILT-IN TAX"	SUB-TOTAL (I) (5)=(2)+(3)+(4)	DIRECT PAYMENTS BY COMPONENT MFR. EXCISE DUTY	CUSTOMS DUTY	SALES TAX	OCTROI DUTY	TOTAL DIRECT PAYMENTS	INPUT COSTS INCLUDING TAXES
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1.	Tyres and Tubes	3,519	136	-	3,655	201	91	148	7	447	4,102
2.	Wheels	2,110	8	11	2,129	40	676	15	-	731	2,860
3.	Battery	N.A.	N.A.	N.A.	N.A.	24	87	9	-	120	N.A.
4.	Bearings	683	1	-	684	7	224	7	7	245	929
5.	Ferrous metal Parts	205	--	-	205	2	83	—	-	85	290
6.	Fasteners	242	5	-	247	19	16	6	-	41	288
7.	Piston Assembly	225	2	-	227	29	20	8	-	57	284
8.	Fuel Injection Pump	725	8	39	772	12	49	28	7	96	868
9.	Nozzle Holder	256	3	-	259	2	9	4	1	16	275
10.	Fuel Filter	46	1	8	55	1	7	4	1	13	68
11.	Oil Filter	131	1	6	138	5	-	4	-	9	147
12.	Engine Valves	189	1	6	196	6	43	4	-	53	249
13.	Hydraulic Brake	99	1	2	102	5	3	5	-	13	115
14.	Master Cylinder	90	—	3	93	1	8	3	-	12	105
15.	Clutch Assembly	189	—	14	203	8	6	5	-	19	222
16.	Tie Rods and Drag Links	183	1	6	190	3	16	5	-	24	214
17.	Radiator	384	-	-	384	9	148	8	-	165	549
18.	Starter Motor	418	2	11	431	51	19	22	-	92	523
19.	Dynamo	146	1	3	150	18	-	9	-	27	177
20.	Wiper Motor	80	1	5	86	7	1	3	-	11	97

Contd.....

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
21. Head Lamps	143	2	-	145	5	9	5	-	19	164
22. Instruments	110	-	-	110	1	14	2	--	17	127
23. Shock Absorbers	88	1	4	93	9	4	3	-	16	109
24. Gaskets	38	-	-	38	3	6	7	-	16	54
25. Starting Wheel	38	-	-	38	5	-	2	-	7	45
26. Glass	184	12	-	196	39	-	8	1	18	244
	10,522	186	118	10,826	512	1,539	324	24	2,399	13,105

Schedule 1 : Table 3

TELCO TRUCK : INPUT COSTS TO VEHICLE MFR. : MAJOR COMPONENTS

(Figures in Rupees)

	DESCRIPTION	COMP. MFR. INPUT COSTS (INCLDG. TAXES)	COMP. PRICE TO VHL. MFR. (EXCLDG. DIR. PAYMENTS)	VALUE ADDED BY COMP. MFR.	DIRECT PAYMENTS BY VEHICLE MFR.*				TOTAL (9) = (3) + (8)
					EXCISE DUTY	SALES TAX	OCTROI DUTY	TOTAL DIRECT PAYMENTS	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	Tyres and Tubes	4,102	4,806	704	2,823	305	-	3,128	7,934
	Wheels	2,860	2,853	N.A.	56	116	-	172	3,025
	Battery	N.A.	602	N.A.	105	29	-	134	736
	Bearings	929	1,059	130	144	45	-	189	1,248
	Bimetal Parts	290	495	205	3	20	-	23	518
	Fasteners	288	342	54	34	15	-	49	391
	Piston Assembly	284	590	306	-	24	-	24	614
	Fuel Injection Pump	868	1,105	237	-	44	-	44	1,149
	Nozzle Holder	275	390	115	-	16	-	16	406
	Fuel Filter	68	71	3	-	3	-	3	74
	Oil Filter	147	292	145	-	12	-	12	304
	Engine Valves	249	371	122	-	15	-	15	386
	Hydraulic Brake	115	251	136	-	10	-	10	261
	Master Cylinder	105	179	74	-	7	-	7	186
	Clutch Assembly	222	366	144	5	15	-	20	386
	Tie Rods and Drag Links	214	299	85	-	12	-	12	311
	Radiator	549	750	201	-	30	-	30	780
	Starter Motor	523	873	350	175	42	-	217	1,090
	Dynamo	177	301	124	-	12	-	12	313
	Wiper Motor	97	235	138	53	12	-	65	300
	Head Lamps	164	248	84	-	10	-	10	258
	Instruments	127	252	125	-	10	-	10	262
	Shock Absorbers	109	127	18	-	5	-	5	132
	Gaskets	54	60	6	-	2	-	2	62
	Steering Wheel	45	86	41	-	3	-	3	89
	Glass	244	295	51	-	12	-	12	307
		13,105	17,298	3,591	3,398	826	-	4,224	21,472

Schedule 1 : Table 4

TELCO TRUCK : INPUT COSTS TO VEHICLE MFR. : OTHERS

(Figures in Rupees)

	DESCRIPTION	INPUT COSTS EXCLUDG. TAXES	"BUILT-IN" AND "BASE" TAXES	SUB-TOTAL (1) (4) = (2) + (3)	DIRECT PAYMENTS BY VEHICLE MFR. EXCISE DUTY	SALES TAX	OCTROI DUTY	TOTAL DIRECT PAYMENTS	TOTAL (9)=(4)+(8)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1.	Steel Castings	468	52	520	-	21	-	21	541
2.	Steel Forgings	3,492	395	3,887	-	155	-	155	4,042
	Sub-Total (1)-(2)	3,960	447	4,407	-	176	-	176	4,583
3.	Brake Linings	90	18	108	-	4	-	4	112
4.	Valve Seat Rings	97	19	116	-	5	-	5	121
5.	Air Filter	89	5	94	-	4	-	4	98
6.	Truck Brake Valve	362	35	397	-	16	-	16	413
7.	Regulator	48	8	56	-	2	-	2	58
8.	Cylinder Head Collar	86	28	114	-	4	-	4	118
9.	Protective Sleeve	94	35	129	-	5	-	5	134
10.	Air Compressor	131	15	146	-	5	-	5	151
11.	Air Pressure Regulator	131	10	141	-	6	-	6	147
12.	Tyre Inflator	107	10	117	-	5	-	5	122
13.	Compression Rings	29	11	40	-	2	-	2	42
14.	Oil Rings	156	58	214	12	8	-	20	234
	Sub-Total (3)-(14)	1,420	252	1,672	12	66	-	78	1,750

(1)		(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
15.	Miscellaneous Lamps	36	2	38	-	2	-	2	40
16.	Switches	122	10	132	-	5	-	5	137
17.	Cables	55	19	74	7	3	-	10	84
18.	Other Electrical Appliances	64	6	70	2	3	-	5	75
	Sub-Total (15)-(18)	277	37	314	9	13	-	22	336
19.	Proprietary Parts	1,380	50	1,430	-	57	-	57	1,487
20.	Miscellaneous Metal Parts	80	7	87	-	4	-	4	91
21.	Steel	2,918	131	3,049	331	134	-	465	3,514
22.	Non-ferrous	70	-	70	6	3	-	9	79
23.	Rubber Parts	150	13	163	5	-	-	12	175
24.	Paints	446	47	493	78	23	-	101	594
	Sub-Total(21)-(24)	3,584	191	3,775	420	167	-	587	4,362
25.	Indirect Materials	6,418	630	7,048	714	263	-	977 176*	8,201
26.	Other Materials	2,285	71	2,356	878	129	-	1,007	3,363

Note : (*) Customs Duty

Schedule 1 : Table 5

TELCO TRUCK : INPUT COSTS & "VAT RATES" FOR VEHICLE MFR. : IMPORTS

(Figures in Rupees)

DESCRIPTION	C.I.F. VALUE OF IMPORTS	TOTAL CUSTOMS DUTY	TOTAL (4) = (2) + (3)	ASSUMED PROTECTIVE ELEMENT * PERCENTAGE	ASSUMED PROTECTIVE ELEMENT * AMOUNT	"VAT BASE" (7) = (2) + (6)	DUTY TO BE LEVIED AS VAT	"VAT RATE" (9) = (8) / (7) X 100
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8) = (3) - (6)	(9)
1. Steel	4,647	2,450	7,097	10%	245	4,892	2,205	45.07%
				20%	490	5,137	1,960	38.15%
				30%	735	5,382	1,715	31.87%
2. Non-ferrous Metals	45	46	91	10%	5	50	41	82.00%
				20%	9	54	37	68.52%
				30%	14	59	32	54.24%
3. CKD (Completely Knocked Down Components)	133	181	314	10%	18	151	163	107.97%
				20%	36	169	145	85.80%
				30%	54	187	127	67.91%
4. Bearings	95	146	241	10%	15	110	131	119.09%
				20%	29	124	117	94.35%
				30%	44	139	102	73.38%
5. Steel Top Rings	146	227	373	10%	23	169	204	120.71%
				20%	45	191	182	95.29%
				30%	68	214	159	74.30%
6. Oil Rings	32	53	85	10%	5	37	48	129.73%
				20%	11	43	42	97.67%
				30%	16	48	37	77.08%
* Weighted Average of (1) to (6)	406	607	1,013	10%	61	467	546	116.92%
				20%	121	527	486	92.22%
				30%	182	588	425	72.28%
7. Miscellaneous	126	136	262	10%	14	140	122	87.14%
				20%	27	153	109	71.24%
				30%	41	167	95	56.89%
	5,224	3,239	8,463	10%	324	5,548	2,915	52.54%
				20%	647	5,871	2,592	44.15%
				30%	971	6,195	2,268	36.61%

Sensitivity analysis for different "protective" rates, viz. 10%, 20%, 30%.

Schedule 1 : Table 6

TELCO TRUCK : "VAT RATES" FOR INPUTS TO COMPONENT MFRS.

(Figures in Rupees)

	DESCRIPTION	INPUT COSTS EXCLDG. TAXES	"BUILT-IN" AND "BASE" TAXES	TAX RATE (I) (4) = (3) / (2) X 100	TAX BASE A1 (5) = (2) + (3)	EXCISE DUTY ON INPUTS	(6) AS % OF T.B. A1	TAX BASE B1/C1 (T.B. A1 + 20% CUSTOMS)	EXCISE + 80% CUSTOMS	(9) AS % OF T.B. B1 / C1	EXCISE + 80% CUSTOMS + SALES TAX	(11) OF B1 /
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12
1.	Tyres and Tubes	3,519	136	3.86%	3,655	201	5.50%	3,673	274	7.46%	422	11.
2.	Wheels	2,110	19	0.90%	2,129	40	1.88%	2,264	581	25.66%	596	26.
3.	Battery	N.A.	N.A.	N.A.	N.A.	24	N.A.	N.A.	94	N.A.	103	N.
4.	Bearings	683	1	0.15%	684	7	1.02%	729	186	25.51%	193	26.
5.	Bimetal Parts	205	-	-	205	2	0.98%	222	68	30.63%	68	30.
6.	Fasteners	242	5	2.07%	247	19	7.69%	250	32	12.80%	38	15.
7.	Piston Assembly	226	1	0.44%	227	29	12.78%	231	45	19.48%	53	22.
8.	Fuel Injection Pump	725	47	6.48%	772	12	1.55%	782	51	6.52%	79	10.
9.	Nozzle Holder	256	3	1.17%	259	2	0.77%	261	9	3.45%	13	4.
10.	Fuel Filter	46	9	19.57%	55	1	1.82%	56	7	12.50%	11	19.
11.	Oil Filter	131	7	5.34%	138	5	3.62%	138	5	3.62%	9	6.
12.	Engine Valves	189	7	3.70%	196	6	3.06%	205	40	19.51%	44	21.
13.	Hydraulic Brake	99	3	3.03%	102	5	4.90%	103	7	6.80%	12	11.
14.	Master Cylinder	90	3	3.33%	93	1	1.08%	95	7	7.37%	10	10.
15.	Clutch Assembly	189	14	7.41%	203	8	3.94%	204	13	6.37%	18	8.
16.	Tie Rods and Drag Links	183	7	3.83%	190	3	1.58%	193	16	8.29%	21	10.
17.	Radiator	384	-	-	384	9	2.34%	414	127	30.68%	135	32.
18.	Starter Motor	418	13	3.11%	431	51	11.83%	435	66	15.17%	88	20.
19.	Dynamo	146	4	2.74%	150	18	12.00%	150	18	12.00%	27	18.
20.	Wiper Motor	80	6	7.50%	86	7	8.14%	86	8	9.30%	11	12.
21.	Head Lamps	143	2	1.40%	145	5	3.45%	147	12	8.16%	17	11.
22.	Instruments	110	-	-	110	1	0.91%	113	12	10.62%	14	12.
23.	Shock Absorbers	88	5	5.68%	93	9	9.68%	94	12	12.77%	15	15.
24.	Gaskets	38	-	-	38	3	7.89%	39	8	20.51%	15	38.
25.	Steering Wheel	38	-	-	38	5	13.16%	38	5	13.16%	7	18.
26.	Glass	184	12	0.11%	196	39	19.90%	196	39	19.90%	47	23.
		10,523	304	2.89%	10,826	512	4.51%	11,118	1,742	14.82%	2,066	17.

Notes :

Coverage of : Excise | Excise + 80% Customs | Excise + 80% Customs + S.T.

"VAT Rate" applicable to : (1) Inputs to Component Manufacturers — A1 | B1 | C1

(2) Inputs to Vehicle Manufacturer — A2 | B2 | C2

Schedule 1 : Table 7

TELCO TRUCK : "VAT RATES" FOR INPUTS TO VEHICLE MFR. : MAJOR COMPONENTS

(Figures in Rupees)

DESCRIPTION	TAX BASE A2	EXCISE DUTY	(3) AS % OF T.B. A2	TAX BASE B2	EXCISE + 80% CUSTOMS	(6) AS % OF T.B. B2	TAX BASE C2	EXCISE + 80% CUSTOMS + S.T.	(9) AS % OF T.B.C2
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1. Tyres and Tubes	4,605	3,024	65.67%	4,532	3,097	68.34%	4,384	3,550	80.98%
2. Wheels	2,813	96	3.41%	2,272	637	28.04%	2,257	768	34.03%
3. Battery	N.A.	129	N.A.	N.A.	199	N.A.	N.A.	237	N.A.
4. Bearings	1,052	151	14.35%	873	330	37.80%	866	382	44.11%
5. Bimetal Parts	493	5	1.01%	427	71	16.63%	427	91	21.31%
6. Fasteners	323	53	16.41%	310	66	21.29%	304	87	28.62%
7. Piston Assembly	561	29	5.17%	545	45	8.26%	537	77	14.34%
8. Fuel Injection Pump	1,093	12	1.10%	1,056	51	4.84%	1,026	123	11.99%
9. Nozzle Holder	388	2	0.52%	381	9	2.36%	377	29	7.69%
10. Fuel Filter	70	1	1.43%	64	7	10.94%	60	14	23.33%
11. Oil Filter	287	5	1.74%	287	5	1.74%	283	21	7.42%
12. Engine Valves	365	6	1.64%	331	40	12.08%	227	59	25.99%
13. Hydraulic Brake	246	5	2.03%	244	7	2.87%	239	22	9.21%
14. Master Cylinder	178	1	0.56%	172	7	4.07%	169	17	10.06%
15. Clutch Assembly	358	13	3.63%	353	18	5.10%	348	38	10.92%
16. Tie Rods and Drag Links	296	3	1.01%	293	16	5.65%	278	33	11.87%
17. Radiator	741	9	1.21%	623	127	20.39%	615	165	26.83%
18. Starter Motor	822	226	27.49%	807	241	29.86%	785	305	38.85%
19. Dynamo	283	18	6.36%	283	18	6.36%	274	39	14.23%
20. Wiper Motor	228	60	26.32%	227	61	26.87%	224	76	33.93%
21. Head Lamps	243	5	2.06%	236	12	5.08%	231	27	11.69%
22. Instruments	251	1	0.40%	240	12	5.00%	238	24	10.08%
23. Shock Absorbers	118	9	7.63%	115	12	10.43%	112	20	17.86%
24. Gaskets	57	3	5.26%	52	8	15.38%	45	17	37.78%
25. Steering Wheel	81	5	6.17%	81	5	6.17%	79	10	12.66%
26. Glass	256	39	15.23%	256	39	15.23%	248	59	23.79%
	16,208	3,910	23.33%	15,048	5,140	32.83%	14,733	6,290	41.08%

Notations :

"VAT Rate" applicable to :	Coverage of :	Excise	Excise + 80% Customs	Excise + 80% Customs + S.T.
(1) Inputs to Component Manufacturers		A1	B1	C1
(2) Inputs to Vehicle Manufacturer		A2	B2	C2

Schedule 1 : Table 8

TELCO TRUCK : SUMMARY OF APPROPRIATE "VAT RATES"

(figures in Rupees)

DESCRIPTION	"TAX EXCLUSIVE" INPUTS TO MFR*	VALUE ADDED BY MFR*	SUB-TOTAL (I) (4)=(2)+(3)	TAX BASE A2	TOTAL EXCISE	(6) AS% OF T.B.A2	TAX BASE B2	TOTAL EXCISE + 80% CUSTOMS DUTY	(9) AS % of OF T.B.B2
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1. Inputs for vehicle Manufacture:									
(a) Raw Materials									
i) Indigenous	N.A.	N.A.	3,594	3,689	506	13.72%	3,668	527	14.37%
ii) Imported	N.A.	N.A.	5,344	5,344	-	-	5,344	2,106	39.41%
(b) Components:									
i) Tyres & Tubes	3,680	704	4,384	4,605	3,024	65.67%	4,532	3,097	68.34%
ii) Wheels	2,264	(7)	2,257	2,813	96	3.41%	2,272	637	28.04%
iii) Battery	N.A.	N.A.	499	578	129	22.32%	508	199	39.17%
iv) Other major components	5,198	2,894	8,092	8,790	661	7.52%	8,244	1,207	14.64%
v) Misc. Auto components	N.A.	N.A.	6,881	7,257	351	4.84%	7,174	434	6.05%
vi) Miscellaneous	N.A	N.A	279	297	26	8.75%	293	30	10.24%
vii) Imported components	N.A	N.A	527	527	-	-	527	486	92.22%
(c) Indirect Mtls.	N.A.	N.A.	6,487	6,941	997	14.36%	6,590	1,207	18.32%
(d) Other Mtls.	N.A.	N.A.	2,289	2,324	910	39.16%	2,316	918	39.64%
Sub-Total (1)			40,633	43,165	6,700	15.52%	41,468	10,848	26.16%

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
2.	Manufacture and Sale of Vehicles (Increments in Taxes and Tax Bases)									
8	(a) Manufacture of Vehicle	40,633	25,980	25,980	25,980	10,220		25,980	10,220	
	(b) Sale of Vehicle (incldg. Freight, Insurance, etc.)	66,613	3,368	3,368	3,368			3,368		
	TOTAL:			69,981	72,513	16,920	23.33%	70,816	21,068	29.75%

Schedule 3 : Table 1

TELCO AND ANCILLARIES : TAX CONTENT IN WORKING CAPITAL

(AT THE RATE OF ONE VEHICLE PER MONTH)

(Figures in Rupees)

DESCRIPTION (1)	MONTHS @ OF STOCK (2)	PRESENT SYSTEM TAX COMPONENT (3)	PRESENT SYSTEM TAX CONT. IN W.C. (4)	PROPOSED MANVAT SYSTEM TAX COMP. 'A'* (5)	PROPOSED MANVAT SYSTEM TAX COMP. 'B'* (6)	PROPOSED MANVAT SYSTEM TAX CONT. IN W.C. (PROPOSAL I)** (7) = 0.5x(5) + (2)x(6)	PROPOSED MANVAT SYSTEM TAX CONT. IN W.C. (PROPOSAL II)** (8) = 1.5x(5) + (2)x(6)
A. ANCILLARY INDUSTRIES :							
1. Direct Material Inputs	3.5	3,441	12,043	2,765	676	3,749	6,514
2. Indirect Materials & Stores	6.0	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
3. Work-in-Progress (Dir. Mtl. Cont.)	1.5	3,441	5,162	-	676	1,014	1,014
4. Finished Goods	0.5	6,851	3,426	-	676	338	338
5. Tax Realisation on Sales***	0.5	1,127	(565)	7,304	-	(3,652)	(10,956)
			20,066			1,449	(3,040)
B. VEHICLE MANUFACTURER :							
1. Direct Material Inputs	2.5	13,135	32,838	11,795	1,340	9,248	21,043
2. Indirect Materials & Stores	6.0	1,783	10,698	1,714	69	1,272	2,985
3. Work-in-Progress (Dir. Mtl. Cont.)	1.5	13,135	19,703	-	1,340	2,010	2,010
4. Finished Goods	0.5	25,138	12,569	-	1,409	705	705
5. Tax Realisation on Sales***	0.5	11,922	(5,961)	35,651		(17,826)	(54,977)
			69,847			(4,591)	(28,234)

Note: 1. (@) Please refer to Schedule 3, Table 3.

2. (*) Tax Component 'A' represents the taxes proposed to be covered by MANVAT.
Tax Component 'B' represents the balance taxes (i.e. "built-in tax", "base tax", 20% Customs Duty, and Octroi Duty) not recovered by MANVAT.

3. (**) "VAT" Proposal (I) and (II) are on the assumption of 'Payment Periods' of 1 month and 3 months respectively.

4. (***) For a detailed discussion of this, please refer to pages 17 and 32 of the report.

Schedule 3 : Table 3

AUTOMOBILE INDUSTRY : AVERAGE INVENTORY HOLDINGS

	DESCRIPTION	MONTHS OF INVENTORY CARRIED			
		DIRECT MTLS.	INDIRECT MTLS.	W.I.P. (DIR. MTL. CONT.)	FINISHED GOODS
1.	Commercial Vehicles	2.5	6	1.5	0.5
2.	Tyres & Tubes	2 to 2.5	10 to 16	0.5	0.5 to 1
3.	Batteries	1.5	8	1	1
4.	Pistons, Shock Absorbers etc.	1.5 to 3.5	13 to 18	2	0.5
5.	Inlet and Exhaust valves	10	10	3	0.5
6.	Fuel Pump & parts.	2 to 4	7 to 14	1.5 to 8	0.5 to 1
7.	Electrical Parts	2.5 to 6	6	0.5	0.5 to 1.5
8.	Clutch Brake Assembly	3.5	10	12	0.5
9.	Brake Linings	3.5	8.5	1	1
10.	Steering Gears & Tie Rod Ends	4.5	3.5	2	0.5
11.	Gears	0.5	20	3.5	-
12.	Wheels	4	11	1	0.5
13.	Tyre Tube Valves	1.5	2	0.5	0.5
14.	Bearings	7.5	7.5	2	1.5
15.	Fasteners etc.	3 to 7.5	2 to 8	4 to 5	1.5
16.	Forgings	3 to 4	9.5 to 11.5	2 to 3	0.5
17.	Castings	5	6	4	0.5
18.	Cables	3	30 to 38	0.5 to 1	0.5

Source : Annual Reports of Companies.

Schedule 4 : Table 1

AUTOMOBILE INDUSTRY : SAMPLE PERCENTAGES FOR VALUE ADDED & MARK-UP

DESCRIPTION		GROSS VALUE OF PRODN.	INPUTS (EXCLUDING UTILITIES) DIRECT MTLS	INDIRECT MTLS	VALUE ADDED	MARK-UP ON COST
(1)		(2)	(3)	(4)	(5)	(6)
1.	Commercial vehicles	100	55	10	35	5%
2.	Passenger Cars	100	65	5	30	neg.
3.	Tyres & Tubes	100	64	2	34	2 to 5%
4.	Batteries	100	64	2	34	2%
5.	Pistons, Shock Absorbers etc.	100	32	3	65	6 to 7%
6.	Inlet & Exhaust Valves	100	35	5	60	25%
7.	Fuel Pumps & Parts	100	26	11	63	20%
8.	Electrical Parts	100	60	5	35	7 to 15%
9.	Clutch, Brake Assembly	100	62	5	33	3%
10.	Brake Linings	100	38	5	57	18%
11.	Steering Gears & Tie Rod Ends	100	55	4	41	1%
12.	Gears	100	40	6	54	neg.
13.	Wheels	100	59	6	35	8%
14.	Tyre Tube Valves	100	41	16	43	23%
15.	Bearings	100	45	5	50	3 to 30%
16.	Rubber Tubes	100	35	5	60	neg.
17.	Fasteners	100	25	12	63	13%
18.	Forgings	100	47	7	46	6%
19.	Castings	100	33	16	51	neg.
20.	Cables	100	60	1	39	9 to 13%

Source : Annual Reports of Companies.

Annexure VII.2

Statewise Population Table
(1971 Census)

Sl. No.	States	Total population (in lakhs)	Rural Population Nos. (in lakhs)	Rural Population Percentage (Col.4 to 3)	Urban population Nos. (in lakhs)	Urban population Percentage (Col.6 to 3)	Density of Population (persons per sq.Km.) Total	Rural	Urban	S.Castes Nos. (in lakhs)	S.Castes Percentage (Col.11 to 3)	S. Tribes Nos. (in lakhs)	S. Tribes Percentage (Col.13 to 3)	Literacy (per '000) Total	Males	Females
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1.	Andhra Pradesh	435.03	351.00	80.68	84.03	19.32	157	128	2360	57.75	13.27	16.58	3.81	246	332	158
2.	Assam	146.25	133.36	91.19	12.89	8.81	150*	137	2911	9.13	6.24	16.07	10.99	287	372	193
3.	Bihar	563.53	507.19	90.00	56.34	10.00	324	296	2032	79.51	14.11	49.33	8.75	199	306	87
4.	Gujarat	266.97	192.01	71.92	74.96	28.08	136	100	1625	18.25	6.84	37.34	13.99	358	461	248
5.	Haryana	100.37	82.64	82.34	17.73	17.66	227	189	3928	18.96	18.89	Nil	Nil	269	373	149
6.	Himachal Pradesh	34.60	32.18	93.01	2.42	6.99	62	58	1556	7.70	22.25	1.42	4.10	320	432	202
7.	Jammu & Kashmir	46.17	37.59	81.42	8.58	18.58	NA	NA	NA	3.81	8.25	Nil	Nil	186	268	93
8.	Karnataka	292.99	221.77	75.69	71.22	24.31	153	118	2272	38.50	13.14	2.31	0.79	315	416	210
9.	Kerala	213.47	178.81	83.76	34.66	16.24	549	477	2585	17.72	8.30	2.69	1.26	604	666	543
10.	Madhya Pradesh	416.54	348.69	83.71	67.85	16.29	94	79	2378	54.54	13.09	83.87	20.13	221	327	109
11.	Maharashtra	504.12	347.01	68.83	157.11	31.17	164	115	2555	30.26	6.00	29.54	5.86	392	510	264
12.	Manipur	10.73	9.31	86.77	1.42	13.23	48	42	3083	0.16	1.49	3.34	31.13	329	460	195
13.	Meghalaya	10.12	8.65	85.47	1.47	14.53	45	39	3860	0.04	0.40	8.14	80.43	295	341	246
14.	Nagaland	5.16	4.65	90.12	0.51	9.88	31	28	1230	Nil	Nil	4.58	88.76	274	350	187
15.	Orissa	219.45	200.99	91.59	18.46	8.41	141	130	1113	33.11	15.09	50.72	23.11	262	383	139
16.	Punjab	135.51	103.35	76.27	32.16	23.73	269	208	4650	33.48	24.71	Nil	Nil	337	404	259
17.	Rajasthan	257.66	212.22	82.36	45.44	17.64	75	63	1198	40.76	15.82	31.26	12.13	191	287	84
18.	Sikkim	2.10	1.90	90.48	0.20	9.52	29	26	1967	0.10	4.76	Nil	Nil	NA	NA	NA
19.	Tamil Nadu	411.99	287.34	69.74	124.65	30.26	317	231	2115	73.16	17.76	3.12	0.76	395	518	269
20.	Tripura	15.56	13.94	89.59	1.62	10.41	149	134	3871	1.93	12.40	4.51	28.98	310	402	212
21.	Uttar Pradesh	883.41	759.52	85.98	123.89	14.02	300	260	4356	185.49	21.00	1.99	0.23	217	315	106
22.	West Bengal	443.12	333.45	75.25	109.67	24.75	504	380	5628	88.16	19.90	25.33	5.72	332	428	224
	Total All States	5414.85	4367.57	80.66	1047.28	19.34	171	139	2441	792.52	14.64	272.14	6.87			
	Total All India	5481.60	4390.46	80.09	1091.14	19.91	177	148	2505	800.06	14.60	380.15	6.94	295	395	107

* Includes Mizoram.

Source : (i) Statistical Abstract India : 1974 (Page 3)
(ii) Census of India 1971, General Population tables series I (India) Part II(A)(i) page 54.

Annexure VII.3

Comparable Estimates of per capita State Domestic Product at State Current Prices

(In Rs.)

S T A T E S	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	Av. 1973-74 to 1975-76
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Andhra Pradesh	586	629	664	868	1020	897	928
2. Assam	570	559	632	676	849	848	791
3. Bihar	418	437	500	559	706	669	645
4. Gujarat	845	859	759	1116	1051	1236	1134
5. Haryana	932	1008	1091	1276	1408	1514	1399
6. Himachal Pradesh	676	731	813	953	1086	1165	1068
7. Jammu & Kashmir	557	566	602	720	887	825	811
8. Karnataka	675	699	740	992	1106	1038	1045
9. Kerala	636	633	709	876	969	1000	948
10. Madhya Pradesh	489	539	585	714	825	790	776
11. Maharashtra	811	860	876	1157	1435	1455	1349
12. Manipur	408	449	533	792	914	904	870
13. Meghalaya	644	568	648	729	921	899	850
14. Nagaland	508	527	586	683	829	949	
15. Orissa	541	527	631	765	780	834	793
16. Punjab	1067	1106	1208	1484	1585	1688	1586
17. Rajasthan	629	573	600	826	860	873	853
18. Sikkim	-	-	-	-	-	-	*820
19. Tamil Nadu	616	692	714	865	964	997	942
20. Tripura	563	575	535	729	888	872	830
21. Uttar Pradesh	493	504	623	677	740	727	715
22. West Bengal	729	775	776	920	1080	1100	1033
Total States:	619	645	693	853	968	969	930
For all States and Union Territories :	625	652	701	861	978	981	940

Source : Columns (1) to (5) - Central Statistical Organisation.

* Figures in respect of Nagaland adopted for Sikkim.

Annexure VII.4

Non-suburban Passenger Earnings of Railways allocated on the basis of originating stations located in each State.

(Rs. crores)

State	1974-75	1975-76	1976-77	1977-78	1974-75 to 1977-78
(1)	(2)	(3)	(4)	(5)	(6)
1. Andhra Pradesh	25.02	30.58	34.11	37.67	127.38
2. Assam	8.41	10.60	12.34	13.43	44.78
3. Bihar	32.33	43.23	47.16	50.38	173.10
4. Gujarat	18.38	22.70	25.68	29.57	96.33
5. Haryana	7.31	8.55	9.58	10.40	35.84
6. Himachal Pradesh	0.34	0.45	0.79	0.83	2.41
7. Jammu & Kashmir	2.73	2.46	3.63	4.58	13.40
8. Karnataka	11.53	14.34	16.11	16.54	58.52
9. Kerala	9.41	10.37	12.24	15.57	47.59
10. Madhya Pradesh	20.36	26.36	30.16	29.05	106.43
11. Maharashtra	56.17	71.38	75.94	85.90	289.39
12. Manipur	-	-	-	-	-
13. Meghalaya	-	-	-	-	-
14. Nagaland	0.98	1.24	1.25	1.30	4.77
15. Orissa	5.68	7.47	9.11	9.24	31.50
16. Punjab	13.82	16.66	18.31	20.63	69.42
17. Rajasthan	20.04	25.27	25.52	29.15	99.98
18. Sikkim	-	-	-	-	-
19. Tamil Nadu	25.35	30.67	34.21	34.72	124.95
20. Tripura	0.14	0.18	0.21	0.25	0.78
21. Uttar Pradesh	64.88	81.83	93.21	98.83	338.75
22. West Bengal	31.55	39.75	41.73	44.73	157.76
Total:	354.93	444.09	491.29	532.77	1823.08

Source : Railway Board, Ministry of Railways.

Annexure VII.5

Revenue from Income-tax, Corporation Tax collections and Union Surcharge, 1952-53 to 1975-76.

(Rs. crores)

Year	Income-tax collections (inclusive of Union surcharge)	Union Surcharges.	Corporation Tax collections.
(1)	(2)	(3)	(4)
1952-53	143.2	6.1	43.8
1953-54	124.2	4.9	41.6
1954-55	123.2	5.0	37.3
1955-56	132.0	5.0	37.1
1956-57	151.2	5.6	51.2
1957-58	161.6	6.9	56.1
1958-59	172.8	8.4	54.3
1959-60	149.2	8.3	106.6
1960-61	168.7	5.7	110.7
1961-62	161.0	5.1	160.8
1962-63	187.4	5.6	220.1
1963-64	245.6	14.9	287.3
1964-65	266.9	12.6	313.6
1965-66	271.9	7.1	304.8
1966-67	306.3	8.2	330.8
1967-68	325.9	9.3	310.5
1968-69	378.5	11.1	299.8
1969-70	448.4	18.2	353.4
1970-71	473.2	19.3	370.5
1971-72	534.4	27.3	472.1
1972-73	625.5	34.7	557.9
1973-74	741.4	42.9	582.6
1974-75	878.3	47.6	709.5
1975-76	1214.4	62.7	861.7

Source: Combined Finance and Revenue Accounts and Finance Accounts.