THE UNION BUDGET 1992-93

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By

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This year's Budget is not a budget for the greedy, paid for by the needy. The Budget provisions properly so called (as distinct from the proposed amendments to the direct tax laws) are well conceived, and deserve the support of the well informed irrespective of party affiliations.

Four main thrusts of the Budget

The four main thrusts of the Budget are – liberalization, integration of India into the global economy, reduction of taxes, and a stable and healthy balance of payments situation.

● Liberalization is the key to the Budget. (The only criticism can be that it measures out liberalization with coffee spoons.) It is a Watershed Budget which marks the beginning of a new chapter in India's economic history. We have left behind the terminal stage of our forty-year affair with shabby State socialism. It was our ideological socialism which had been responsible for India remaining the twentieth poorest nation on earth. Our gross domestic product is smaller than that of greater Los Angeles (population 14 million). We have more than 15 per cent of the world's population, and less than 1.5 per cent of

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Based upon the public talk in Bombay on 3rd March, 1992, and subsequently in Calcutta and Delhi.

the world's income. Our per capita income did not even double since we became a republic – it only increased 92 per cent in real terms.

This year's historic Budget for the first time reflects the consciousness of our government that fast economic growth would be impossible with woolly, outworn socialism which betrays a severe hardening of intellectual arteries and a pathetic lack of knowledge of the revolutionary changes which have recently swept across the world.

During the last 25 years, China's economic growth, despite its communism, has been more than twice as fast as India's. The annual investment in China by foreign companies exceeds the total investment in India in the last 44 years. The new foreign investment in China totalled $10 billion last year! There are already more than 2500 foreign enterprises operating in the 27 hi-tech industrial parks recently started in China.

I have the highest opinion of Indian capacity and potential. But I find it impossible to refute the universal criticism that our two besetting sins are self-complacency and obstinate refusal to face the truth. We could have more realistically chosen the ostrich instead of the peacock as our national bird.

The Survey on India, published by *The Economist* of 4th May 1991, showed the tiger "caged". It should be made compulsory reading in every school and college, as well as for those adults who choose to enter Parliament or the civil service. The jugular vein of the article is that if India has more than its fair share of the world's misery, it is not the fault of former colonial masters or wicked western capitalists or the cruel hand of fate: it is largely India's own doing.

We are slipping behind the rest of the world – except in population growth. This truth can hardly be better illustrated than by the fact that the present per capita income in South Korea is 13 times, and in Hong Kong 30 times, that of India, though the three countries started at about the same level.

The United Nations Development Report, published last June, ranks the nations of the world by reference to the Human Development Index (HDI). In determining a nation's position in the list, the HDI takes into account the expenditure incurred by the state on human priority sectors – health, water, sanitation, daily calorific intake, literacy, and education at primary and secondary levels. Having regard to the HDI, India is placed, for the second year running, pretty much at the bottom of the list – 123rd out of 160 countries.

Dr. Manmohan Singh has rightly emphasized that unless certain values are adhered to by the nation, it cannot come out of the recession. The Finance Minister has no Midas touch; he has no snake oil which can be used as having a magical healing power in matters economic.

• The proposed integration of India into the global economy has not come a day too soon. The emerging world economy has erased national boundaries. Capital and companies no longer stop at the border. If India is to grow and prosper, it has no alternative but to be integrated into the world economy.

- Reduction of taxes is one of the avowed aims of the Budget. In a global economy, cutting taxes has become a matter of national interest: high tax countries inevitably lose out. The days when the government could adopt any tax policy, as if the nation existed within a vacuum, are over.

- If India is to have a stable and healthy balance of payments, it can only be through increased exports. Our share has dropped from 2.2 per cent of world exports in 1950 to 0.44 per cent. Among the exporting countries, India ranked sixteenth in 1950: today its rank has dropped to fortythird! Even Holland, one of the tiny countries of the world with a population of 15 million, has six times the exports of India! Hong Kong has almost three times the international trade of India, although its population is less than one per cent of India's – 0.7 per cent to be precise, while its land area is 0.03 per cent of India's.

Unjustified criticism

The least justified criticism of the Budget is that it has been framed under the dictates of the World Bank and the International Monetary Fund. The censure is levelled by those whose critical perception does not exceed forty watts. They should credit India with enough intelligence to make the right decision for itself after forty years of mistaken policy. Some of the ablest men in the two international institutions are Indians: to say that the Indian Government cannot think for itself is gratuitous self-condemnation.

In any event we must judge the policy underlying the Budget on its merits, and it is wholly irrelevant to be concerned about who suggested the path of wisdom. One of the great failings of democracy is the mistaken belief that it is the duty of the opposition to oppose.

Secondly, the fear has been expressed in some quarters that India will be swamped by multinationals. The truth is that India runs no risk whatever of being dominated by foreign corporations. We must get rid of the illusion that we are still fighting the East India Company.

Thirdly, the view has been expressed that the Budget has not done enough to check inflation or to counter recession. To control inflation is possible, but to eliminate it is beyond hope at this juncture. The last time we had "negative inflation" (to use bad English) was when Mr. Morarji Desai was the Prime Minister (1977-79). The spirit of the nation – the spirit of national dedication and confidence which then emerged after the tyranny of the Emergency – had as much to do with the fall in prices as any budget.

Inflation is a worldwide phenomenon. A dollar today is worth only 13 cents in 1945 money; a pound is worth six pence. Even the Deutschemark is only one-third of its value in 1948 when it replaced the worthless Reichsmark.

Again, the world economy is going through a period of recession. The current economic depression in the United States is billed as "the mother of all recessions" – the longest since 1945. General Motors, the giant among corporations, incurred a loss of $4.5 billion in 1991 – unparalleled in the Company's 84-year history. The critics claim that in Britain the recession is deeper than in any other country. About 20,000 companies went into liquidation in 1991, which works out to one in every 50 British companies.

Points in favour of the Budget

There are several points on which the Budget deserves to be commended.

(1) It is the first Budget which aims at breaking the shackles of the bureaucratic command system.

(2) It reflects consciousness of the risk to the nation of an unbridled increase in the total liabilities of the Government. We are stealing from the future. For years to come, the dead hand of the excessive national debt will continue to rest heavily upon the productive energies of our people. No less than Rs. 32,000 crores will be spent next year merely on servicing the loans. That would constitute almost one-fourth – 23 per cent to be precise – of the total governmental expenditure: more than what will be spent on Plan or Defence.

(3) It has restored the balance of payments to a less critical level than before. We have a reserve of $4.4 billion. The risk of defaulting or having

to ask for rescheduling of debts, no longer looms over the horizon.

(4) Partial convertibility of the rupee is a sensible step. That this step is in the national interest is proved by the example of Pakistan. At the beginning of last year the currency of India was stronger than that of Pakistan – 100 Pakistani rupees equalled 86 Indian rupees. The situation was reversed after the Pakistani rupee was made fully convertible. Today 100 Pakistani rupees are equal to 111 Indian rupees.

(5) The confidence of foreign investors has been restored. The scramble by Non-resident Indians to withdraw their deposits from banks has ceased.

(6) The abolition of the office of the Controller of Capital Issues is an essential step in the process of liberalization.

(7) The decision to abolish deduction of tax from interest on term deposits with banks is in the public interest. When Bonn introduced ten per cent withholding tax from interest on bank deposits, there was a flight of capital. Deposits worth DM 100 million vanished from West German banks and re-appeared next door in tiny Luxembourg. The law was promptly scrapped.

(8) Permitting the import of gold is a prudent decision. But the levy of 15 per cent import duty in foreign exchange is likely to render the scheme less successful than it deserves to be. The name and address of the importer would remain on the records of the customs authorities and attract inquiries by the Tax Department. Again, Pakistan levies an import duty of three per cent, so the

possibility of gold being imported legally into Pakistan and then illegally smuggled into India cannot be ruled out.

(9) The reduction of the statutory liquidity ratio from 38.5 per cent to 30 per cent would release larger bank funds for loans to business and reduce the heavy bank interest rate by one percentage point.

(10) The lowering of the vertiginous customs tariffs to a less unreasonable level is welcome. It is the inevitable step which has to be taken if India is to be integrated into the global economy.

(11) The lowering of the maximum marginal rate of income-tax on individuals would, in the long run, have no detrimental effect on government revenues, because it would result in better compliance. Professor Lawrence Lindsey of the Harvard University has given cogent evidence to prove that income-tax revenues are most buoyant when the maximum rate is 40 per cent. This phenomenon, called "the Lindsey effect", has been accepted in the United States where the maximum rate is 33 per cent and in Britain where it is 40 per cent. The reduction of the maximum marginal rate on non-corporate assessees to 44.8 per cent (including surcharge) will bring India closer to the fast developing countries which have slashed their rates.

Personal taxation

The threshold of chargeability to income-tax is sought to be increased from Rs. 22,000 to Rs. 28,000. It should be increased to at least Rs. 42,000, even if tax incentives are not to be abolished. The minimum taxable limit of Rs. 15,000 was fixed in 1981, and that corresponds to more than Rs. 40,000 today; while the limit of Rs. 18,000 fixed in 1985 is equivalent to more than Rs. 33,000 today. (Based on Consumer Price Index for Industrial Workers).

The proposal to abolish tax incentives, like the ones contained in Sections 80-CCA, 80-CCB, and 80-L, is wholly indefensible. If such repeal were effected, the lower middle class (specially retired people) would be savagely hit. Up to a total income of Rs. 3,30,000, an assessee would have to bear a higher burden of income-tax, despite the reduction in the maximum rate from 50 per cent to 40 per cent. For millions of citizens, the increase in the threshold and the reduction in the maximum rate would only be a teasing illusion.

Select Committee to examine changes

This year the Finance Bill is an amalgam of two distinct parts – one which can be appropriately called the Finance Bill which contains the budgetary provisions, and the other which virtually amounts to a Direct Taxes (Amendment) Bill. This other part purports to make changes, substantive and procedural, in direct tax laws of a far-reaching nature.

Stability and simplicity have been mostly ignored. On the whole the Income-tax Act will be more elaborate and complex than ever before. No less than 155 amendments in direct tax laws are sought to be made by this Budget, on top of the 163 amendments which were made only six months ago by the Finance (No. 2) Act, 1991. The pressure on the Finance Minister and on the Minister of State for Finance is so heavy that you need a separate Minister for Simplicity and Stability whose exclusive task should be to ensure that the bureaucrats do not trivialize the fiscal law.

Most of the proposed amendments should be severed and referred to a Select Committee of Parliament, as the Direct Taxes (Amendment) Bill, 1992. In particular, reference may be made to the proposals regarding tax on partnerships, inclusion of minor child's income in the parent's income, capital gains tax, and wealth-tax on companies in which the public are substantially interested. All the above four proposals in the Finance Bill should be deleted as being oppressive and inconsistent with the avowed policy of the Government.

For decades the law was stable, fair and simple regarding assessment of partnerships. Genuine firms were registered and the firm's income was assessed in the hands of the partners who were taxed at the appropriate rate on their respective shares. If the firm was not genuine, it was not registered and the unregistered firm was taxed as an assessable entity on its entire income. From 1956 double taxation was resorted to by the Government and the registered firm had to pay the registered firm's tax, over and above the tax levied on the individual partners' shares of the firm's income. Public protest against this injustice went unheeded.

The Direct Tax Laws (Amendment) Act, 1987, despite its far-reaching provisions, was rushed through the Lok Sabha in less than half an hour. It was scheduled to come into force on April 1, 1989. One of its provisions was to compound the injustice on partnerships by providing that while the registered firm's tax would be removed, each partner would not be assessable on his share of the firm's income but the entire income would be assessed at the maximum marginal rate in the hands of the firm as an assessable entity. Thus the distinction between genuine firms and bogus firms was sought to be obliterated.

Countrywide protests were made and when the attention of the then Prime Minister, Rajiv Gandhi, was pointedly drawn to this measure, he was surprised and called it "an aberration". The Government repealed this unjustly harsh law by the Direct Tax Laws (Amendment) Act, 1989 which received the President's assent on March 15, 1989 with the result that the obnoxious provision never came into force.

It is amazing that now an identical provision is again proposed in the present Finance Bill. Presumably, no one drew the attention of the Finance Minister to the past record.

Income-tax began in India more than a century ago but there has never been a time when the minor child's total income was included in the parent's. (Only by way of exception, the minor child's share of profits in a firm, and income from assets transferred by the parent, were included). Now the proposal is to club the entire income of the minor child in all cases with the parent's, inevitably resulting in an increase of the tax burden.

As regards capital gains, the proposal is to restructure the entire scheme. Income-tax and capital gains tax would hereafter be two different taxes. Further, the existing scheme is to scale down the sale proceeds with a view to giving appropriate relief in the effective tax rates. But the new scheme is to scale up the cost by bringing in the concept of "indexed cost of acquisition". In the unavoidable pressure at budget time, no one could have examined the full implications of the far-reaching consequences of the new scheme.

While the reduction of wealth-tax from two per cent to one per cent is a step in the right direction, the most objectionable feature of the Finance Bill is the re-emergence of wealth-tax on companies in which the public are substantially interested. Section 13 of the Finance Act, 1960 repealed wealth-tax on all companies public as well as private. Section 40 of the Finance Act, 1983 restored wealth-tax on private companies, restricted to certain unproductive assets.

This year the Finance Bill proposes to repeal both the aforesaid two Sections and make all companies liable to wealth-tax in respect of certain assets one of which is "urban land". The reimposition of wealth-tax on public companies is itself a most reprehensible step. The delirious stock markets, which operate in a thought-free zone, do not seem to have even noticed the repercussions of the Bill on millions of shareholders.

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