CHAPTER-7

There is emerging aim of fiscal policy, vigorously assailed by some and staunchely defended by others, the aim of ensuring the full employment of factors of production.

-A.H.Hansen.

SUMMARY ,CONCLUSIONS AND POLICY IMPLICATIONS

The best system of taxation from economic point of view is that which has the best or the least bad economic effects.

-Hough Dalton.

In the foregoing chapters, we have sought to spotlight the various aspects of Orissa's tax system and have also indicated the spheres in which problems have arisen and solutions are necessary. In doing this , we have refrained from an elaborate study of each of the aspects nor have we gone in great details into the considerable statistical materials presented in the tables. The reason is, our object has been to emphasize on the responsiveness and productivity of Orissa's tax system and keep away from exercises, lest it my confuse the scheme of the present work. To this extent the present study can be said to be exhaustive in raising the issues but may not be exhaustive in treating them.

With these limitations, in the present chapter an attempt is made to give a comprehensive account of the major findings of the entire study in the following paragraphs.

7.1 SUMMARY OF THE FINDINGS:

One of the most distressing features of state finance that emerges from this study is the increasing magnitude of revenue deficits in recent years. The continuous outspacing of the growth of revenues both in the eighties and nineties has led to serious deterioration in the State's budgetary positions, from a surplus of 1.32 percent of Net State Domestic Product in the mid- seventies (i.e., in the 1977-78) to a deficit of about 1.22 percent of Net State Domestic Product in 1993-94. In absolute terms, the net revenue deficits in 1993-94 is close to Rs. 181.60 crores.

Since 1982-83 dis-saving has been showing persistent rising trend year after year mainly due to very high growth of revenue expenditures. The increase in expenditures has been particularly alarming in 1984-85, when it has grown at an average rate of 14.63 percent per annum. What is more, with the interest liability itself growing at 23.29 percent per year, expenditure growth has become self propelling. Equally causing grave concern is the high growth of wages and salaries and subsidies.

Thus, the higher growth of revenue expenditure in relation to the growth of revenue receipts has created an explosive cycle of expenditure growth. The use of borrowed funds for meeting revenue expenditure, while increasing interest liability does not create corresponding sources of revenue.In addition, even the borrowed funds used for capital spending are not efficiently utilized. Consequently, interest liabilities feed back into the growth of diversion of borrowed funds. Due to this, the State's gross interest payments during the decade of 1990's grew at the average annual rate of 47.23 percent. Clearly, such a high rate of interest payment expenditure is unsustainable.

If, it is assumed that the observed trend in revenue expenditure will continue into the future in the medium term, then in order to phase out the revenue deficits in the next four years, i,e, by 1998-99, the revenue growth would have to be accelerated by almost 3.36 percentage points to 10.02 percent per annum. This is indeed a unjustified estimation and therefore,immediate remedial measures either to increase the tax effort or to compress the expenditures must be undertaken. The latter proposition may not be a reasonable strategy in case of a most underdeveloped economy like Orissa, where Government assumes the role of a public sector in order to accelerate the tempo of economic development through its various developmental and non-developmental plan expenditure programmes. Thus, the massive participation of the Government in developmental and welfare activities has given rise to the problem of resource-constraint. Resource constraints can be judged interms of predominant agricultural sector, low monetization, low industrialization, structural and industrial rigidities, low taxable capacities of the people and so on.

The overall trends of revenue from taxation in Orissa show a steady increase over all the plan periods covered by our study. But, a close examinationof these especially with relation to state income discloses that the revenues built-in-flexibility has not improved at all. It was of the order of 1.3227 for the period of 1966-67 to

1976-77 and 1.020 for the period 1981-82 to 1991-92. What appears from the results is that the latter years changed composition of taxation in particular has not facilitated much to improve the automatic growth of tax receipts.

The role of the state's own tax revenue as an element of state income over the period (1961-62 to 1993-94) has not been commensurate with the expected or likely drive for additional taxation as a source of revenue for the state. This is so,because of the fact that the percentage share of the state's own tax revenue in state income has increased at a much slower pace than the pace ascribed to total tax revenue.

If, we assume tax-income ratio as a simplest measure of tax burden or sacrifice , then the result of our analysis shows that, states tax burden has almost doubled and hence going for further taxation would be objectionable. But, in a relative sense (i.e., from the angle of total tax revenue) the concept of tax burden would be more meaningful and in this comparison Orissa emerges rather poorly.

Judged from the angle of state's own tax revenue,a progressive system of direct taxes on agricultural land, agricultural income and estate duty, in the hope that these would complement and support each other in such a manner as to make available to the state as much of revenue from these sources as can be collected through them, given the constraints of the low amount of per-capita income and wealth and the highly skewed nature of their distribution in a predominantly agrarian structure of the Orissan economy, had already been put on the statute book in all the plan periods. This is supported by the evidence that the contribution of the total agricultural taxes to the state's own tax revenue has remained almost static during the last two decades of 1970-71 to 1993-94. Thus, the system of agricultural taxation appears to have designed for a static and subsistence agriculture. That seems to be the plausible reason, why the system has remained almost inelastic with respect to changes in prices and production over the years. An analysis of the revenues from this source and the relevant proxy bases, viz; agricultural income and the level of agricultural production indicates a considerable scope for raising revenue from these categories of taxes. In other words, its rate of growth is estimated to be much lower than that of the relevant bases such as agricultural income and agricultural production. As the revenue requirements of the State are duly high, this source ought to be adequately tapped.

However, against the background of the reluctance of the state Government not only to increase the rates of these taxes, but even to continue to keep these taxes on the statute book at the existing rates and the land reform measures of imposing ceilings on the ownership of agricultural land, it is doubtful whether the amount of revenues which could be mobilized through these agricultural taxes would be commensurated with the cost of administering these taxes. But, the truth remains that, with the secular upward trend in prices and consequent heightened income structure, the inelastic agricultural taxes are losing importance as a source of public revenue in the State.

The tax system since the beginning of the sixth plan in particular is heavily oriented towards the urban and industrial sectors of the economy and has neglected the rural and the agricultural sectors. This follows from the declining importance of agricultural taxes and the increasing importance of taxes on commodities and services. The primary consideration in the wider coverage and increased rate of these taxes (taxes on commodities and services) has been the need to obtain the ever-mounting resources for developmental purposes. At the same time, these taxes have been expected to impose certain amount of restraints on increase in consumption thereby releasing additional resources for developmental needs. But, the continual outpacing of the states own tax revenue by the shared taxes raises serious doubt about the relative tax-effort of the state on the one hand and indicates the relative inelastic nature of state's taxes (or the productivity of state's own taxes) to those of shared taxes on the other hand.

An examination of the state's direct taxes on agricultural land, and income have not shown themselves to be "effective" instrument of resource mobilization. The income elasticity and buoyancy of these taxes have been comparatively low and in addition owing to the `loopholes' in the law and perhaps laxity in its enforcement, the magnitude of tax avoidance and evasion has been enormous, with the result that these taxes have shrunk both in their dimension and dinomination. On the other hand, the elasticity and buoyancy coefficients in case of indirect taxes are worked out to be relatively greater in comparison to the direct taxes.

There is thus substantial evidence to purport that the taxation trend of Orissa's economy in recent years has become more and more oriented towards indirect or consumption taxes. This trend by itself has been sought as an explanation for low elasticity of the states direct taxation. To be more specific the opinion is that the inelastic nature of the Orissa's tax system on the direct tax front is an inherent characteristic resulting from heavy reliance placed on indirect taxes. The results of the present study do not however provide adequate emperical justification to this account. They contrary to the expectations disclose that indirect taxes in general contain better automatic growth potentialities.

As an instrument of resource mobilization, the indirect levy of sales tax has been much more productive than all other taxes and further that the levy would have been helpful also as a means of curtailing consumption. The electricity duty has shown a high degree of income elasticity and buoyancy with a result that it has come to occupy a prominent place so to say among the numerous tax measures. State's excise duty which once was the most productive means of revenue has lost its importance and most probably is currently being used more for putting a curb on the consumption of liquor, Bhang, opium, ganja and other narcotics than that of resource mobilization.

From the above findings, it is clear that as an instrument of resource mobilization, fiscal policy in general and the taxation policy of the state Government in particular has not been a remarkable success. From the available evidence, it is seen that taxation policy of the state both through its direct and indirect levies has not able to bring about any significant increase in the overall resource mobilization programme to meet its ever increasing public expenditure programs. As a result of which, the attainment of financial self-reliance has become a distinct reality for the state in recent times.

To substantiate our findings, it is imperative to provide some of the specific conclusions that have emerged in long course of econometric exercise.

7.2. SPECIFIC CONCLUSIONS:

The specific conclusions that emerges from the study are as follows.

(1) An analysis of the revenue budget of the state clearly indicates that the annual compound rate of growth of total revenue receipts is slightly greater than that of revenue expenditures by 0.22 percent and thereby serve to show the relative inflexibility of revenue expenditures in the state.

(2) Similarly, on the capital account, the growth rate in both capital receipts and capital expenditures are found to be approximately 11 percent. There does not seem to be any difference between the two growth rates. Thus, the growth in capital revenue is absorbed by the growth in capital expenditures and the former does not add anythiings substantial to the net surpluses in the capital budget.

(3) Taking time as an explanatory factor, the regression analysis of variance of the Revenue Budget shows that about 73 percent of the total variation in revenue receipts is explained by the time factor. In case of revenue expenditures, about 72 percent of the variation is explained by time.

(4) An analysis of the nature and extent of dependence of revenue expenditure on revenue receipts of the revenue budget reveals that 99.85 percent of the variation in expenditures from revenue is explained by variation in revenue, which clearly indicates the relatively greater importance of revenue receipts as an explanatory factor than time.

(5) On the capital account, the regression analysis of variance shows that about 81 percent of the total variations in capital receipts are explained by time factor alone. In the like manner, about 82 percent of the total variations in capital expenditures are explained by time.

The following broad conclusions emerged from the analysis of Range of fluctuations in receipts and expenditures on revenue and capital accounts of the budgets of the state Government.

(6) The analysis reveals that the fluctuations on capital account are greater than those of revenue account.

(7) Within the capital account of the budgets, the fluctuations are higher in capital expenditures (11.07) than in capital receipts (3.22)

(8) On the revenue account of the budgets, the fluctuations in revenue receipts (7.65) are observed to be higher than those in revenue expenditures (2.94).

(9) The highest ratio of range in annual fluctuations is exhibited by expenditures on capital account of the budgets (11.07).

(10) An analysis of the overall budgetary position of state reveals that the surplus or deficit in the revenue account has more or less largely been counterbalanced by a deficit or surplus in the capital account in most of the years. This, it is believed has set a pattern for the state Government for over thirty -three years covered by the present study.

The analysis of the income elasticity of the revenue receipts and revenue expenditures reveals the following findings.

(11) There are negative elasticity on revenue and expenditure accounts for the years 1965-66, 1976-77 and 1984-85. This is largely due to decline in state incomes during these years as compared to the immediately preceding year.

(12) Negative elasticities are also observed in case of state expenditures during the years 1969-70 and 1983-84. The negative values of income elasticities of state expenditures for these two years seem to be due to factors other than state income as such because in these years, state incomes show a rising trend as compared to the corresponding previous years.

(13) The elasticities of revenue receipts and expenditures are found to be of very high orders in the years 1971-72, 1975-76, 1978-79, to 1982-83, 1986-87 and 1992-93.

(14) The values of elasticity of total expenditure are reported to be relatively greater than those of the elasticity of revenue expenditures.

(15) An analysis of the trends of public expenditures suggests that both the developmental and non-developmental expenditures in absolute terms have been stepped up to remarkably high levels during all the plan periods covered by the study.

(16) The analysis further reveals that the expenditure on human capital increased in a cognisable way during the Annual plan of 1979-80. But all through the period, the stress is laid more on human capital than on physical capital except in the initial years of the Third Five- year plan.

The conclusions that emerge from the analysis of the feasible trends in states tax effort are as follows.

(17) During the span of the past thirty-three years plan period states own tax revenue has increased in absolute terms roughly eighty-eight fold,from Rs.10.35 crores in 1961-62 to Rs.916.10 crores in 1993-94.

(18) Judged by the familiar growth rate, states own tax revenue has registered a growth rate of 13.86 percent per annum over the years.

(19) The total tax revenue shows a rising trend throughout the period from 1961-62 to 1993-94, increasing

from Rs.16.87 crores in 1961-62 to Rs.1953.70 crores in 1993-94, that is an increase of about one hundred and sixteen fold during these years.

(20) Annual compound growth rate of the total tax revenue is found to be of the order of 14.69 percent.

(21) On the other hand, annual compound growth rate of the state income is observed to be 10.89 percent.

(22) A simple comparison between these growth rates of the tax revenue and state income reveals that the increasing state income has been outpaced by the increasing states own tax revenue and much more so, by the total tax revenue over the period.

(23) Further, it is be to noted that the role of the state's own tax revenue as an element of state income over the period (1961-62 to 1993-94) has not been commensurated with the expected or likely drive for additional taxation as a source of revenue for the state.

(24) The analysis also indicates that the state has been relying more and more on shared taxes for the purpose

of resource mobilization. This is evident from the fact that the rate of growth of the state's own tax revenue (13.96) is much lower than the rate of growth of the state's share in central taxes (15.62).

(25) An analysis of Average and Marginal tax rate shows that for all practical purposes, there exists a shift in the pattern of tax revenue since the fiscal year 1961-62.

(26) Average tax rate seems to have registered a moderate increase for the state's own tax revenue and a spectacular increase for the shared taxes. This is evident from the fact that ,where the average tax rate of the State's own tax which was 4.27 percent in the year 1961-62 increased to only 5.87 percent in the year 1991-93, the average tax rate of shared taxes on the other hand, increased from 1.65 percent in the year 1961-62 to 7.50 percent in the year 1992-93.

(27) The segmentation of the total tax revenue into those accruing to the state's own taxes and shared taxes respectively clearly suggests that, of the 13.36 percent of the state income taken away by the state

and union Government in the year 1992-93,7.51 percent is by the Union Government alone and the rest 5.85 percent by the state Government.

(28) An analysis of the compositional pattern of state's tax revenue exhibits that, it is indirect taxes that have been responsible for the major share in the increase in tax revenues of the Government over the years.

(29) While the total tax revenue have gone up by nearly one hundred sixteen told during 1961-62 to 1993-94, the direct tax revenues have gone up only by fifty three times, and indirect tax revenues by more than one hundred seventy three times.

(30) On the State's front, the enormous growth in revenues from indirect taxes has certainly to be attributed to states sales tax. The percentage contribution of sales tax to state's own tax revenue which was only 38.94 percent in the year 1961-62. has enormously increased to 60.62 percent in the year 1993-94.

(31) A noteworthy feature at State's taxation as revealed by the analysis is that the phenomenal increase in the share of central tax in total tax revenue has out-paced the relative contribution of states own tax revenue to the total tax revenue of the state.

(32) The percentage contribution of shared tax to the tax revenue of the state has tremendously increased from 38.65 percent in the year 1961-62 to 53.11 percent in the year 1993-94.

An analysis of the ratio of individual taxes to state income reveals the following broad conclusions.

(33) The share of total tax revenue to Net State Domestic Product has increased from 4.27 percent in the year 1961-62 to 13.07 percent in 1993-94.

(34) Land revenue has been a declining source of revenue. From 0.61 percent of state income in 1961-62, it declined to 0.16 percent in the year 1993-94.

(35) Receipts from state excise duty which was 0.42 percent in 1961-62 has slightly increased to 0.51 percent in 1993-94.

(36) It is again sales tax, where the increase is very large. From 1.02 percent of state income in 1961-62 ,it increased to 3.72 percent in 1993-94.

(37) Stamps duty and Motor Vehicle tax show an increasing trend during the period under study. Whereas, in 1961-62 they constituted only 0.24 and 0.26 percent of the state income respectively, this proportion has almost doubled to 0.37 and 0.55 percent in the year 1993-94.

(38) In respect of other taxes and duties, no consistent trend emerges through as a proportion of state income, they appear to be falling over the period under study.

The analysis of the trends and patterns of Federal transfers to the state suggests the following inferences.

(39) The state's share of divisible taxes and duties has gone up both in absolute and relative sense, from Rs. 53.82 crores in the course of Third Five year plan to Rs.3571 crores in the Eighth Five year Plan periods.

(40) The percentage share of divisible taxes to the total resources transferred, which was 16.92 percent in the Third Five year Plan has gone up to 39.25 percent in the Eighth Five year plan periods. This trend no doubt, has created a plausible deleterious effects on the growth and sustenance of the taxation efforts of the state in recent times.

The analysis of Buoyancy and elasticity of State's aggregate taxes gives the following broad conclusions.

(41) The buoyancy coefficient for the total own tax revenues works out as 1.2651, which means over the period under review, every one percent increase in state income on an average is associated with 1.2651 percent increase in tax collection.

(42) The buoyancy coefficient of the state's own tax revenue which was 1.3949 during the year 1971-72 to 1981-82 declined substantially to 0.9615 during the period 1986-87 to 1993-94.

(43) Comparing state's own total tax revenue and shared taxes, it is found that buoyance coefficient is slightly

more (1.4223) for shared taxes than that of state's own total tax revenue (1.2651) for the period 1961-62 to 1993-94 .

(44) While the buoycany coefficient of direct taxes works out to be 1.0177, the buoyancy coefficient of indirect taxes is found to be 1.3204 for the entire period covered by the study.

(45) The buoyancy coefficent of the total taxes on agricultural land and income shows a declining trend from 1.4402 during the period 1971-72 to 0.8807 during the period 1986-87 to 1993-94.

(46) The overall buoyancy coefficient for the taxes on property and capital transaction and those of taxes on commodities and service are found to be 1.1031 and 1.1796 respectively for the entire period covered by the study.

(47) The elasticity coeffecient of the state's total own tax revenue works out as of the order of 1.1557 for the period 1961-62 to 1993-94 .

(48) The elasticities of the selected tax groups are found to be rather divergent. Following one classification, they are found to be ranging from 0.5510 for taxes on agricultural land and income to 1.0098 for taxes on property and capital transactions.

(49) According to another classification, the elasticity coefficients are found to be ranging from 0.9394 for state's total direct tax revenues to 1.24966 for state's total indirect taxes.

(50) In general, direct taxes when compared to indirect taxes are found to be less elastic.

An analysis of elasaticity and buoyancy of individual state taxes reveals the following conclusions.

(51) Of all the taxes collected by the Orissa Government, the electricity duty is found to be most responsive to changes in state income in comparison to all other state taxes. The buoyancy and eleasticity coefficients are worked out to be 1.7082 and 1.60822 respectively.

(52) Four other taxes exhibit buoyancy and elasticity coefficients greater than unity. These are the stamps and Registering duty, state excise duty, vehicle tax and sales tax.

(53) On the otherhand, the elaasitcities of taxes on agricultural sector are found to be very small and insignificant i.e.; -0.02142 for agricultural income tax and 0.5490 for land revenue.

(54) The elesticity coefficient in case of entertainment tax and taxes on goods and passengers are worked out to be 0.6634 and 0.8058 respectively. The buoyancy coefficients of these taxes incidentally happens to be low.

(55) The wide differences between the elasticity and buoyancy estimates of entertainment tax and vehicle tax suggests that increase in revenue productivity has come through new tax measures. The difference is greater in the case of entertainment tax.

(56) An analysis of elasticity and buoyancy estimates of states excise duty indicates that no significant discretionary changes have taken place in the case of the state on this account.

(57) The elasticity and buoyancy estimates discloses that the sales tax receipts of the state is embodied with adequate degree of elasticity. The overall buoyancy and elasticity are placed around 1.4964 and 1.2456 respectively.

7.3 POLICY IMPLICATIONS

It is always possible to devise a suitable system of taxation where the existing weakness can be removed.

Taking into account the above factors, it is possible to suggest the following considerations for evolving a suitable system of taxation.

Given the high proportion of consumption expenditure in total state Domestic Product, the relative share of Government revenues has to be increased mainly by impinging upon consumption activities. Here, the emphasis will have to be not much on reducing existing consumption expenditure all along the line as on reducing additional consumption corresponding to additional income. Clearly, therefore, what we argue is that the incidence of taxation should be more on those sectors which , in the development process, enjoy a faster growth of incomes; and the particular instruments of taxation have to be tailored on such a way that they operate in these sectors most effectively.

Given the basic objectives, the following elements may be mentioned as desirable for being incorporated in a satisfactory policy of taxation: on the agricultural taxation front, (i) It may be advisable to have a rate structure such that it would not impose an unwiedly burden on the agriculturists, but at the same time would bring within the tax net as large a number of agriculturists as are able to pay the tax without undue distress,(ii) The standard settlements should be periodically revised every five to seven years so as to make the system elastic with respect to changing economic conditions, and (iii) Since, there exists a system of differential taxation of agricultural and non-agricultural incomes, which disturbs the natural flow of resources between sectors, we may suggest a unified income tax structure for both agricultural and non-agricultural incomes. We believe that this will help in regulating the intersectoral flow of resources.

On the indirect taxation front, we may stress on the Rationalisation of simplification of the tax structure in order to compel it to be more buoyant and elastic than its original level. In this regards, certain measures which needs immediate attention are : (i) Ways have to be found to reduce the number of sales tax rate and levy uniform tax rates in respect of some important commodities. The number of tax rates should be brought down to atleast two or three in the course of next two years and this will nodoubt reduce both administrative and compliance costs significantly. (ii) Measures should be taken to relieve the burden of the tax on inputs through a system of tax credits. And, with better information system, perhaps attempt could be made to extend the tax base to the stages beyond manufacturing on the principle of "value added". (iii) The sales tax incentives given for industrialization in the state need to be rationalised. (iv) The other two taxes which need to be rationalised are the entertainment tax and stamps and Registration Duty. The levy of the stamp duties at very high rates of 15 to 20 percent has resulted in substantial under valuation of immovable property. This has led to investments in real estates, an important source of underground economy. The same amount of tax could perhaps be collected by reducing the tax rate, and lastly, (v) the entertainment tax should be brought under stricter tax compliance in order to make it more buoyant and elastic.

If one were to attempt to compress our arguments in this dissertation into one single argument, it would be that the direct and indirect tax systems of the state have to be integrated and treated in such a way that each can play the role expected of it. In this sense, the problem of state finance is not one to be solved by sheer financial expertise or by accounting gymnastics or by discovering new sources of revenue. Ultimately, the problem of state finance has to be treated alongside the problems of politics and public administration and with a general sense of proportion. It is such an outlook on the part of the political and administrator that can make it possible for them to come to grips with the problem which demands and will continue to demand attention in the State Scene.