CHAPTER VII

SUMMARY AND CONCLUSIONS

Tax Structure refers to the 'mix' and types of taxes imposed by a Government. How taxes are or should be composed in a State are questions that relate to tax structure. In the terminology of Fiscal Science the edifice of tax structure is mainly built on tax base and tax rate. The elements of the tax structure are (a) the number and variety of taxes (b) the structure of each tax and (c) the combination of several taxes.

The importance of the study of tax structure follows logically and essentially from the growing importance of the role of the government in accelerating the rate of economic development. Taxation is an important fiscal instrument in increasing the State revenue and in achieving the social and economic objectives of the community. The functions of the tax system in a developing country/State normally should be (a) curtailing consumption (b) reallocating resources from less to more productive investments (c) providing a flow of funds to the Government and providing incentives to alter economic behaviour
so as to facilitate growth. The efficiency of a tax system in promoting the economic development of a State depends on the tax structure it adopts.

Tax structure of a State is normally designed in such a way that it is capable of reaching most taxable sources. That is, significant proportions of revenue pool should be contributed by desirable types of taxes. Taxes should be equitable both horizontally and vertically. Tax structure should be responsive to the changing economic conditions. The aim should always be a tax structure that is adequate, flexible and harmonious with the emerging pattern of economic activity.

Tax structures manifestly differ markedly from State/country to State because of differences in history, political systems and public attitude towards the Government. In general, a developing State should build on the tax system it already has, making sure that major taxes do not get seriously out of date and are progressive in effect wherever possible. Moreover a tax structure that is particularly relevant and appropriate to any one at a particular stage of development need not and generally is not equally and simultaneously appropriate to the rest of the economies.
Harley H. Hinrichs in his study on the tax structure change during economic development adopted a stimulating 'grand' approach to the subject and sketched out a pattern of tax structure change from primitive to advanced societies. Traditional societies rely primarily on non-tax sources and/or traditional direct taxes like taxes on land. When the economy reaches maturity modern direct taxes become predominant as in the present day United Kingdom and the United States of America. Beyond the primitive stage but below the advanced stage i.e., the transitional stage is the category that fits most of the present day developing economies. Hinrichs generalises in respect of transitional stage, that taxes on foreign trade grow most rapidly at first, then taxes on consumption and transactions while finally although at the end of the transitional phase modern direct taxes increase faster than internal indirect taxes. Moreover the tax structure of advanced economies is more a reflection of political and cultural styles than a simple translation of tax bases to tax structure. So tax structure flexibility is a luxury available to advanced economies.

Another approach to tax structure change has been offered by R.A. Musgrave in his book on Fiscal Systems.
The basic determinant of tax structure at the early stages of development is the availability of feasible tax bases. Given the difficulty of taxing agriculture through income tax, land taxes become an important element in the tax structure in this period. In the later period of an economy's development, tax authorities are offered a much greater variety of tax handles or available bases to tax. The problems of enforcement also shift from extension of the tax net to plugging loopholes constituting legal means of avoiding tax payment.

As income tax is suited to be more a national rather than a state or local tax, the possibility of achieving tax progressivity through indirect taxes on luxury consumption has been receiving more attention. The contrast between progressive direct taxes and regressive indirect taxes has diminished sharply.

Jorgen Lots and Elliott Morse also found that sales taxes and stamp duties have become important new taxes in developing countries because they are closely related to the degree of monetisation of an economy as distinct from the level of per capita income. These taxes are not self assessed and so do not require literacy. R.A. Musgrave also shows that with the dissolution of traditional society older
forms of direct taxation such as land taxes declined in importance and indirect taxes became the mainstay of the revenue structure.

Against the background of these studies, the tax structure of Andhra Pradesh has been examined here for about a quarter century. Andhra Pradesh State formed on 1-11-1956 is one of the 22 States of the Indian Union and occupies the fifth rank both from the point of population and geographical area. It has 3.4 per cent of the geographical area of India and 7.6 per cent of the total population of the country. In Andhra Pradesh there are 3 well known regions which differ from one another in their socio-economic conditions - (a) Coastal Andhra, (b) Rayalaseema and (c) Telangana (the first two together are called the Andhra area or erstwhile Andhra State). The per capita income of these 3 regions in 1955-56 was respectively - Rs. 257, Rs. 225 and Rs. 201 whereas for the entire State, the per capita income was Rs. 232. The socio-economic differences of these three regions have their own impact on the financial position of the State and thereby on the economic development of the State.

In the context of the vital relationship between the stage of economic development and the tax structure out-
lined above, an examination is made in detail of the economic development of Andhra Pradesh during the first 25 years of its history after the reorganisation of the State in 1956.

Economic growth is generally thought of as uni-dimensional and is measured by increase in output or increase in output per unit. Economic development goes beyond this to imply structural and functional change. Development in the real sense implies the elimination of hunger and provision of the basic needs like more food and clothing and better quality of housing for all poor sections and thereby increasing the quality of life. Quality of life is meaningless without the minimum requirements like the availability of nutritious food, clean water, more consumer goods, good roads, transport facilities, electricity, education and inexpensive recreation facilities. Therefore, measurement of economic development in the living standards of people is very important.

Andhra Pradesh is rich in natural resources like sun, rain and soil. It is predominantly an agricultural State where 70 per cent of the population is dependent on agriculture and nearly 50 per cent of the State income (SID) is derived from agriculture. The State with perennial rivers and
fertile land has been described as the 'rice-bowl' of South India. Despite all its rich resources Andhra Pradesh at the time of its formation in 1956, had a per capita income of Rs. 229 as against the all India average of Rs. 255 i.e., 90 per cent of the latter.

The density of population in the State is less than the national average. The annual growth rate of population was 1.83 per cent in Andhra Pradesh as against the growth rate of 2.16 per cent for all India during 1951-81. The percentage of literates as a whole in Andhra Pradesh has been less than for all India throughout the period 1951-81. The proportion of urban population to total population also was less in Andhra Pradesh than for India as a whole during 1961-81.

Between 1950-51 and 1979-80 the State income of Andhra Pradesh increased at an annual compound growth rate of 2.58 per cent as against the increase in NNP at 3.64 per cent (at 1960-61 prices). At the commencement of the Third Five Year Plan (1961) Andhra Pradesh's share in the total national income of India was 7.4 per cent and it declined to 6.6 per cent by the end of the Fifth Five Year Plan. Moreover the annual fluctuations in the State income of Andhra Pradesh were larger than in the National income of India.
The growth rate of per capita income in Andhra Pradesh was just 0.959 per cent (at 1960-61 prices) during 1955-80 against the national average of 1.3 per cent. Even in 1975-76 the per capita income of Andhra Pradesh was 53 per cent of the per capita income of Punjab.

Cultivable area per agricultural worker was 1.25 hectares in Andhra Pradesh in 1966-67 as against the national average of 1.40 hectares. The net area sown per agricultural worker was only 0.83 hectares in 1979-80. Among the Indian States, in respect of per capita availability of food grains Andhra Pradesh State ranked 10th in 1977-78. The average liabilities of the rural households in Andhra Pradesh was Rs. 666 whereas it was only Rs. 497 at the national level. However, the assets held by an average rural household in Andhra Pradesh was just 70 per cent of the assets held by the household in India. Judged by an criterion the position of rural households in Andhra Pradesh has been worse than that of the average rural household in India.

Out of a total central sector investment of Rs. 11,451 crores in industries, in India upto 31-3-1977, the investment in Andhra Pradesh was only Rs. 391 crores i.e., 3.5 per cent of the total. Between 1951 and 1971 the State also invested only Rs. 390 crores i.e., 3.3 per cent of the total
plan outlay. The industrial backwardness of the State is reflected in all the indicators of development. In 1980-81 the per capita consumption of power in Andhra Pradesh was 106 KWH as against 205 in Tamil Nadu, 157 in Karnataka and 135 for the country as a whole.

The length of total roads maintained by the State was 37 Kms. per 100 Sq. Kms. in 1975-76, whereas the national average was 42 Kms. The railway route mileage in the State was 17 Kms. per 100 Sq. Kms. against the all India average of 18 Kms. In respect of motor vehicles per lakh of population the State ranked 16th out of 21 states. Even in respect of social services the position of Andhra Pradesh has not been satisfactory.

Judged by any criterion, the position of Andhra Pradesh is such that in the list of more advanced States, Andhra Pradesh is likely to be at the bottom while in the list of backward States it is likely to be at the top. Even after a quarter century of its planned development the State has not been in a position to catch up even with the low and sub-optimal national average in many crucial fields of development as shown in table 3.39. The economy is gripped by problems of unemployment, low and unequal incomes, illiteracy, malnutrition and the like. The performance of agriculture
in the State is still determined by the natural factors and the vagaries of monsoon. Failure to complete the irrigation
and power projects on hand led to escalation of costs and
denial of the timely benefits.

One of the principal reasons for the State to lag behind the all India averages in the vital sectors of the
economy has been the inadequacy of investment by both the public and private sectors at a rate sufficient to wipe out
the hitherto existing differences in the levels of living. Unless the rate of investment in the State is raised and
maintained at a level higher than that of the national average, the State cannot catch up with the all India per capita
income in the near future. As the public sector has a vital responsibility in this regard the tax and expenditure poli-
cies of the Government should be such as to facilitate the rate of development warranted.

Under the Constitution of India of 1950, both the Union Government and the State Governments are responsible
for accelerating the pace of economic development. The financial relations of the Union and the States are laid down
in the Indian Constitution in great detail. In a way it is necessary as the problem of finance is the fundamental pro-
blem of federalism.
The Constitution of India enumerated the Union and State powers and the concurrent powers exercisable by both. The pattern of distribution of revenue resources between the Union and the States has been based on the following categories.

1. exclusively federal taxes - i.e., taxes levied and collected by the State and appropriated by it.
2. exclusively State taxes.
3. duties levied by the Union and collected and appropriated by the States.
4. taxes levied and collected by the Union but assigned to the States and
5. taxes levied and collected by the Union and distributed between the Union and the States.

A Finance Commission appointed by the President of India periodically also examines the financial position of the Union and the States and recommends appropriate devolution of resources from the Union to the States. The transfer of resources from the Centre to the States has been progressively increasing over a period of years.

The Central assistance in the form of shared taxes and grants-in-aid to the States constituted 27.5 per cent of
the total revenue of all the States in India during 1957-59, 42.2 per cent during 1971-73 and 39.2 per cent by the end of 1978-80. The corresponding percentages for Andhra Pradesh were 29, 41 and 36 respectively.

There has been a decrease in the relative share of Andhra Pradesh both in income tax and Union excise duties under the recommendations of the successive Finance Commissions. For example while the share of Andhra Pradesh in the divisible pool of Union excise duties and income tax was 9.38 per cent and 8.12 per cent respectively under the recommendations of the second Finance Commission, the share was only 7.7 per cent and 8.02 per cent respectively under the recommendations of the Seventh Finance Commission. Grants-in-aid from the Centre to Andhra Pradesh as a percentage of total revenue stood at 18.4 per cent during 1971-73 and 12.1 per cent during 1980-82. The State Governments argue that erosion of States' revenues and concentration of power in the hands of the Centre have been taking place in different spheres and sectors of the economy. As such, the Government of Andhra Pradesh urged the Eighth Finance Commission to transfer at least 60 per cent of the gross revenues of the Centre to the States. The States also demand a share of revenue from Corporation tax and surcharge on income tax. The States have
rightly pleaded that the transfer of bulk of the resources should be on a statutory basis rather than on a discretionary basis.

The Government of Andhra Pradesh, for its part, imposes indirect taxes like sales tax, state excise duties, motor vehicle tax, entertainment tax, electricity duties and direct taxes like the land revenue and stamps and registration fee. Agricultural income tax is not imposed in Andhra Pradesh. It may be noted that the tax structure of Andhra Pradesh has not been devised by any expert economist - Statesman with any specific overall objective. It is the result of historical accidents and not the design of any master architect.

Taxes on commodities and services constituted 89.3 per cent of state's own tax revenues, while taxes on property and capital transactions constituted 10.7 per cent in 1981-82. Even in the all States model the corresponding percentages were 89.8 and 8.8 respectively. But in the all States model, taxes on income and expenditure constituted 1.4 per cent of the state's own tax revenue. In other words in 1981-82 direct taxes constituted 10.7 per cent of tax revenue in Andhra Pradesh and 10.2 per cent in the all States model. So indirect taxes contributed 89.3 per cent of tax revenue in Andhra Pradesh and 89.8 per cent in the all States model.
However in 1957-58 the direct indirect tax ratio was 37:63 for Andhra Pradesh and 31:69 for the all States model. This was largely due to the growing importance of sales tax and excise duties and the decline in the importance of land revenue. Details regarding the method of assessment, fiscal importance, rate structure, inter-state comparisons and the possible lines of reform in respect of direct and indirect taxes imposed in Andhra Pradesh have been presented in Chapters five and six. A study of these taxes shows that if the dependence of the State Governments on indirect taxes was heavy in 1957-58, it was heavier in 1981-82. Decline in the importance of direct taxes and reliance on the indirect taxes therefore are not the peculiar features of Andhra Pradesh tax structure. Even in the United States of America, at the State level, the major development over the first half of the 20th century was the dwindling of the property tax share and rise in the importance of sales and gross receipts taxes particularly retail sales and gasoline taxes.

The responsiveness of tax structure of Andhra Pradesh to the economic development that took place from 1956 is examined at two levels - macro level and micro level.

The per capita state's own tax revenue in Andhra Pradesh which was Rs. 12.70 in 1960-61 increased to Rs. 40.20
In 1980-81, the corresponding figures in the all States model were Rs. 12.44 and Rs. 97.46. Despite the fact that the per capita income of Andhra Pradesh was less than that of India, the per capita State's own tax revenue was Rs. 246 as against Rs. 155 for the all States' model in 1982-83 (BE).

Between 1957 and 1981, the State's own tax revenue in Andhra Pradesh increased at an annual compound growth rate of 14.78 per cent while it was only 13.56 per cent for the all States model. The own tax revenue of Andhra Pradesh which constituted 8.9 per cent of the aggregate own tax revenue of all States in the country rose to 10.7 per cent in 1983-84 (BE). Andhra Pradesh State's own revenue including tax revenue and non-tax revenue constituted 76 per cent of the total revenue in 1957-58 and 64 per cent in 1981-82. The corresponding percentages in the all States model were 74 per cent and 62 per cent (i.e., less than that of Andhra Pradesh). The rising tax-SDP ratios in Andhra Pradesh also indicate the increasing tax effort of the State. The per capita own tax revenue as a percentage of per capita income was 7.6 per cent in Andhra Pradesh and 6.2 per cent in the all States model in 1980-81.

That the tax effort in Andhra Pradesh was more or less satisfactory and that Andhra Pradesh on the whole was an
average performer has also been indicated by the studies on inter-state tax effort undertaken by Prof. D.M. Ranjundappa, Prof. K.N. Reddy, Prof. G. Thimmaiah and Prof. Raja J. Chellaiah (NIPFP) on different dates for different periods from 1957 to 1982. For the period 1973-76 the per capita taxable capacity of Andhra Pradesh was calculated as Rs. 47.75 by Prof. Chellaiah. The average taxable capacity for all the 15 States in India was Rs. 49.37 and for Punjab it was Rs. 74. The deficiency in the per capita taxable capacity in Andhra Pradesh during that period was only Rs. 1.62 (49.37 - 47.75).

The buoyancy coefficient of State's own tax in Andhra Pradesh was 1.37 during 1957-66 and it increased to 1.42 during 1966-78 indicating a high responsiveness of the tax yield to the changes in State income. General Sales tax, State excise duties, Motor vehicle taxation and land revenue imposed by the State Government had a buoyancy coefficient of more than unity in both the periods - 1957-68 and 1966-78. Only stamps and registration fees had a buoyancy coefficient of less than unity. If the longer period of 1957-58 - 1980-81 is taken for calculation of buoyancy coefficients, it is found that all taxes had a buoyancy coefficient of more than unity with the exception of land revenue. The study shows that
land revenue has been insensitive to changes in State income. These conclusions are broadly supported by studies undertaken by others for varying periods.

Income elasticity of tax system is of considerable significance in formulating a tax policy for planned development. The elasticity coefficient in respect of Andhra Pradesh State’s own tax revenue was 1.1037 during 1957-66 and this increased to 1.30 during 1966-78. For the longer period of 1957-81 the elasticity coefficient of State’s own tax revenue of Andhra Pradesh was 1.1326. Further analysis, shows that indirect taxes had an elasticity coefficient of more than unity while the direct tax had a elasticity coefficient of less than unity. Through out the period direct taxes namely land revenue and stamps and registration fees had been inelastic. The inelasticity of stamps and registration fee however was less than that of land revenue. For 1957-82 the elasticity coefficient of indirect taxes was 1.1370. It is of interest to note that the difference between the buoyancy and elasticity estimates for most of the taxes is fairly large indicating the additional tax effort put in by the Government. All the studies relating to elasticity show that State’s own tax revenue in Andhra Pradesh was responsive to the changes in State income.
For the period 1957-81 entertainment tax had the highest elasticity coefficient in Andhra Pradesh whereas sales tax had the highest elasticity coefficient in the all States model. Sales tax had the second highest elasticity coefficient in Andhra Pradesh whereas in the all States model entertainment had the second highest elasticity coefficient. State excise duties occupied the third place followed by Motor vehicles tax and stamps and registration fee both in Andhra Pradesh and the all States model. The elasticity coefficient of land revenue was the lowest in both the models though its magnitude was higher in Andhra Pradesh than in the all States model. A comparison of Andhra Pradesh with the other 3 southern States shows that both in terms of elasticity and buoyancy the position of Andhra Pradesh is fairly good.

A comparison of the tax structure of Andhra Pradesh and the all States model both in 1957 and 1981 shows that Andhra Pradesh tax structure is not basically different from the general pattern. General sales tax, state excise duties, land revenue, stamps and registration fees and motor vehicle tax have continued to be the major sources of revenue. The percentage contribution of these 5 taxes to Andhra Pradesh State's own tax revenue was 92 and 97 in 1957-58 and 1981-82 respectively whereas the corresponding percentages in the
all States nodal stood at 82 and 84 respectively. The composition of Andhra Pradesh tax structure shows that Andhra Pradesh is dependent relatively more on taxes on primary sector and commercial taxes play relatively a less significant role as the turnover of business and trade was less in Andhra Pradesh compared to States like Maharashtra, Tamil Nadu etc. Low rates of urbanisation and monetisation are the other factors responsible for lower revenue from commercial taxes in Andhra Pradesh. In the case of State excise duties, Andhra Pradesh seems to have had the highest revenue in almost all the years from 1960-61 to 1980-81.

The percentage share of central transfers in the total revenue of Andhra Pradesh in 1980-81 was 35.37 as against 37.57 in the all States model. For Bihar the percentage was as high as 62.5, for Orissa 60.9 and for West Bengal 52. Grants-in-aid from the Union Government which constituted 8 per cent in the total revenue of Andhra Pradesh in 1957-58 and 10.00 per cent in 1981-82 had been less in comparison with the all State model where the corresponding percentages were 10.07 and 14.60 respectively.

Though the per capita own tax revenue was more in Andhra Pradesh than in the all States model, the per capita
revenue receipts were comparatively less in Andhra Pradesh than in the all States model indicating the smaller share of resources transferred from the centre and the need for development of non-tax revenue.

However, statistics relating to tax arrears indicate the need for a more effective tax collection machinery and the urgency for taking effective steps to plug the loopholes in the tax legislation. Administrative machinery has to be strengthened for checking the evasion of taxes and delay in payment. Accumulation of arrears of tax revenue affects the financial position of the State and forces the Government to resort to over drafts from the Reserve Bank of India.

Tables relating to budget estimates, revised estimates, and accounts in respect of various components of budgets indicate the existence of wide variations between these estimates which also affect the financial position of the Government. While it is difficult to have close budgeting and eliminate the variations particularly in an economy depending heavily on agriculture (where agriculture and budgets are said to be gamble in monsoon) there is need to change the financial year from first April to first October or November.
Studies relating to the incidence of indirect taxation in India in general indicate a progressive distribution of the tax burden in terms of per cent of expenditure. The progressive pattern of distribution of indirect tax burden is seen to prevail among rural and urban households taken separately except that burden on the urban households is distinctly higher than on the rural households in the corresponding expenditure classes. The study reveals that indirect taxes have not been regressive in nature and indicate a progressive distribution of the burden among different expenditure groups.

In the absence of a progressive productive direct tax on land an element of progression can be imparted to the tax structure of Andhra Pradesh at present only through indirect taxation by taxing luxuries and comforts at heavier rates. In respect of agricultural taxation, the question should not be, whether to tax or not to tax, but how best to tax and how soon to tax. Adequate taxation of agricultural sector is long over due and the sooner it is done it is better in the interests of equity. The present land revenue system ensures equity between lands of equal fertility and productivity and not between the land holders.
The broad objectives of the tax policy of Andhra Pradesh Government have been largely reflected in the objectives of the Five Year Plans of the State. These objectives have been (a) a sizable increase in the State income (b) progressive reduction in the incidence of poverty and a large expansion of employment opportunities and (c) a reduction in inequalities in income and wealth and a more even distribution of economic power.

As has been already noted, the per capita income of Andhra Pradesh increased at 0.96 per cent during 1950-80. During the period 1957-81 land revenue constituted only 0.84 per cent of the State domestic product. An important sector of the economy like the agricultural sector has remained undertaxed. However, the investment in the State has not been of such an order and kind as to wipe out the erstwhile backwardness and take the State above the national average in several sectors of development. The number of registrants in the employment exchanges in the State stood at 20.22 lakhs in November 1983. During 1984-85, on any single day about 18 lakhs persons are estimated to remain under-employed. Even in 1978 the number of persons below the poverty line constituted 42.3 per cent. All these facts therefore indicate that the most important objectives of the tax policy have not been
fully and satisfactorily achieved and the most cherished goals seem to be as distant today as when the State started on the road to planned development. The per capita income of the State was below the national average in 1957 and even now the position remains substantially the same in spite of perceptible increase in per capita income. All the 5 taxes which contributed 92 per cent of State's own tax revenue in 1957 continue to be imposed even now and they contributed 97 per cent of State's own tax revenue in 1981-82. This indicates the non-availability of new tax handles or bases and the limited options available to the State Government to change the 'mix' of taxes. However traditional direct taxes particularly land revenue lost their importance and general sales tax occupies the pivotal position. This is the record of the evolution of tax structure and economic development of Andhra Pradesh from 1956 to 1981.