

Indian Economic Review

Journal of the Delhi School of Economics

January–June 2014

Volume XLIX, Number 1

ISSN 0019-4670

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Book Reviews

Parthasarathi Shome, *Taxation Principles and Applications: A Compendium*, Lexis Nexis, Gurgaon, India, 2014, pp. xvi + 824, Rs 1495/- , ISBN 9789351431244

The volume under review is a compendium of papers on taxation by Parthasarathi Shome, an internationally well known expert in the area. Dr Shome has had a distinguished career at the IMF and in academia. He has held important advisory positions in the governments of India and the UK, and has been Director of the National Institute of Public Finance and Policy in New Delhi. He won the highest civilian honour of the Government of Brazil in the year 2000 for his contributions to Brazilian tax reform. He chaired the Expert Committee on General Anti-Avoidance Rules (GARR) and Taxation of Indirect Transfers, Government of India, whose recommendations attracted widespread attention.

The compendium includes papers on virtually all major issues in the area of taxation, viz., theory, policy, administration and actual practice. The first section of the book contains some reflective pieces by way of an overview of the scope of this volume. In the very first piece the author takes a look at some of the early practices in taxation, going back to Kautilya's 'Arthashastra'. Kautilya had written: 'A wise Chancellor is one who collects revenue so as to increase income and reduce expenditure. He shall take remedial measures if income diminishes and expenditure increases'. Kautilya had emphasized the importance of the internal management of the tax system, rather than diplomacy or the impact of foreign influences. The words of Kautilya continue to be relevant for modern fiscal systems. The section includes a paper that discusses the theoretical foundations of taxation. There is a comprehensive discussion of whether income or expenditure should be taxed, a treatment of consumption and production taxes, environmental taxes and taxation of international trade. There is also a detailed consideration of property tax and value added tax (VAT) in a decentralized economy.

There is no denying that tax policy plays a vital role in economic development and this is the theme of the third paper of this section. Another paper looks at the important concepts of buoyancy and elasticity of the tax structure. If taxes are elastic then the revenue realization increases paripassu with growth of national income, and is of great help to the fiscal planners. However if taxes are inelastic then special discretionary measures have to be taken to enhance revenue. Discretionary measures usually take the form of rate increases rather than base expansion, often contributing little to the revenue elasticity of the tax system. The author attaches substantial importance to the need for base expansion. In Asian countries, nearly two thirds to three quarters of tax revenue are realized from customs duties, sales taxes and excise duties, which have some inherent built-in inflexibilities. This section also contains a fairly comprehensive account of tax policy reform in Latin American countries.

'Who ultimately bears the burden of the tax?' is possibly the most critical question pertaining to any tax system. The second section of the volume deals with this important issue of incidence and the distribution effects of taxation. Two of the five papers in this section have some detailed mathematical modelling. One of these deals with the incidence of the corporation tax in India. The author reaches the conclusion that the tax is essentially borne by capital, with a small portion being shifted on to labour. The second looks at the concept of tax incidence in the presence of more than two factors in a standard general equilibrium model. The remaining papers deal with the issue of the shifting of the corporation taxes in ASEAN countries, and an examination of the fiscal burden of consumption taxes in the Bangkok Metropolitan area.

All taxes other than poll taxes result in some efficiency losses, and much of tax theory is fundamentally concerned with minimization of the so called dead weight loss. The third section of this book deals with several ramifications of this issue. The opening paper deals with taxation of high income earners. It is suggested that no foolproof argument can be provided against taxing the well off at higher rates. The author however cautions that one ought not to inordinately hike up the rate structure. In order to improve compliance the author makes a case for a minimum tax based on gross assets. Analysing the case of Botswana the author shows that rate adjustments are not a substitute for inflation adjustment of the personal income tax base. In a paper addressing corporate tax reform in the US the author makes a case for moving away from corporate profits to capital use as the tax base. In the concluding paper of this section there is a fairly detailed consideration of presumptive taxation of corporate and business incomes.

The fourth section deals with VAT, goods and services tax (GST) and customs duty. There are papers dealing with the VAT in Mexico, Colombia, Brazil and the UK, as well as the modified value added tax (MODVAT) in the context of India. VAT avoids the cascading effect of sales tax by taxing only value added at each stage of production and has therefore been gaining favour over traditional sales taxes. In the Indian context the key focus now is on a successful move towards a generalized GST, where both the Centre as well as the states would play a significant role. The author is of the view that the Canadian GST may have some salient characteristics that may be useful for India.

What are the new innovations in the tax arena in recent years? The fifth section deals with financial transactions tax (FTT), global carbon tax, cash flow tax, minimum alternate tax (MAT) on companies and businesses and the fringe benefits tax. In a globalized world there is clearly a role for FTT as a protection from unwanted capital inflow. This would help minimize fluctuations in financial markets while providing a revenue source of global proportions that could be earmarked for poverty alleviation. In the context of world-wide environmental degradation, the need for a global carbon tax can hardly be overemphasized. A number of possible initiatives including a Pigouvian global tax on airlines and shipping and a system of international tradable permits are examined in some detail.

The volume concludes with a discussion of country and regional experiences as well as the critical issue of tax administration. The author refers to the tax policy changes in India in the 1990s as having been far reaching enough to be thought of as a revolution. Widespread changes were brought about in the realms of both direct and indirect taxes. The author regards the 1997-98 budget as a watershed budget, in that the supply side element was underlined by scaling back the personal income tax rates from a rate structure of 15, 30 and 40 per cent to 10, 20 and 30 per cent. In separate chapters there are treatments of tax policy in the Central Asian and Transcaucasian newly independent states (NIS), Latin America, as well as the US.

Possibly the most vexing aspect of tax policy in developing countries like India has to do with the issue of tax administration along with the related issue of evasion. There is wide agreement that a comprehensive data base and the use of information technology (IT) is an urgent imperative. The author examines the efficacy of a number of possible options such as presumptive taxation and tax deduction at source to deal with this demanding issue. The organization and management of any large tax administration set up has to intrinsically deal with issues of moral hazard, corruption and administrative command and control. In addition to all of the above, there is need for simplicity, transparency and efficient dealing with customers.

In this brief review we have been able to highlight only some of the broad contours of the issues of tax principles and application that have been elaborated at length by the author. The author writes with great clarity and brings to bear his mastery over the theoretical issues as well as his extensive experience as a high profile international tax policy maker. The volume could be profitably used as basic reading material in post graduate courses in public finance anywhere in the world. One need hardly add that tax administrators and policy makers would do well to carefully go through this comprehensive, well researched and up to date tract.

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