

NOTE

Why Not Consumption Tax

Bharat Jhunjhunwala writes :

THE GOVERNMENT HAS TO collect more taxes in order to close the budget deficit. Imposing higher Income Tax hits at investment, while imposing excise duty and sales tax hits at equity and social stability. A possible solution to this predicament is to impose a Progressive Consumption Tax. Population of the country can be divided in three groups on the basis of high-, middle and low-incomes. Goods sold in the market can be classified according to bulk of the purchasers. Items like air-conditioned car, LCD TV, swimming pool and foreign travel can be considered to be mostly consumed by high-income groups. These items can be taxed at high rates-say 50% or even more. Items like motorcycle, computer, refrigerator, washing machine and beauty parlours can be considered to be mostly purchased by middle-income group. These can be taxed at middle rates-say 25%. Items like match box, bicycle, bus travel and bread can be considered to be mostly purchased by low-income group. These may be tax-free. Such a steeply progressive consumption tax would attain both objectives of investment and social justice. The rich will be encouraged to invest more because they will pay fewer taxes if they abstain from consumption and invest their incomes. On the other hand, they will have to pay heavy taxes on luxury consumption. This will act as a disincentive to ostentatious consumption. The upper classes will be prodded in the right direction both by the carrot and stick. The poor, on the other hand, will have to pay virtually no taxes. Items mostly consumed by them will be tax free. This will promote social justice.

Consumption of items like electricity and water should also be taxed or priced in a progressive manner. Consumption of electricity upto 30 units per month may be free. This will be poor friendly. Consumption between 30 to 1000 units may be priced at, say Rs 5 per unit. Consumption above 1000 units may be priced at Rs 15 per unit to provide a disincentive. Similar progressive pricing should be done in respect of water. High price of these essential commodities for the rich will reduce their claims and enable greater supply to the poor.

The ambit of consumption tax should be enlarged to indirect consumption as well. People living in self-owned houses are consuming housing. This consumption must be taxed by imputing a notional rental value to the self-occupied house. A part-say 33%-of perks obtained from companies and expenditures incurred in official government travel should also be considered consumption and taxed. The Government, unfortunately moving in exactly the opposite direction of imposing a uniform Goods and Services Tax (GST) on all items irrespective of the nature of the consumer. This move is wholly retrogressive. It may be efficient from the standpoint of tax collection and economic growth but the loss in terms of social unrest will be huge.

Existing rates of excise and sales tax, or the proposed GST, must be classified according to the category of the consumer. Simultaneously, existing income tax should be made more

progressive. Businessmen in USA, France and other western countries are asking their governments to increase the taxes upon them. Indian businessmen should be subjected to similar high taxes. These two measures will provide both social justice and economic growth.

□□