

## **Tax Concessions to Companies**

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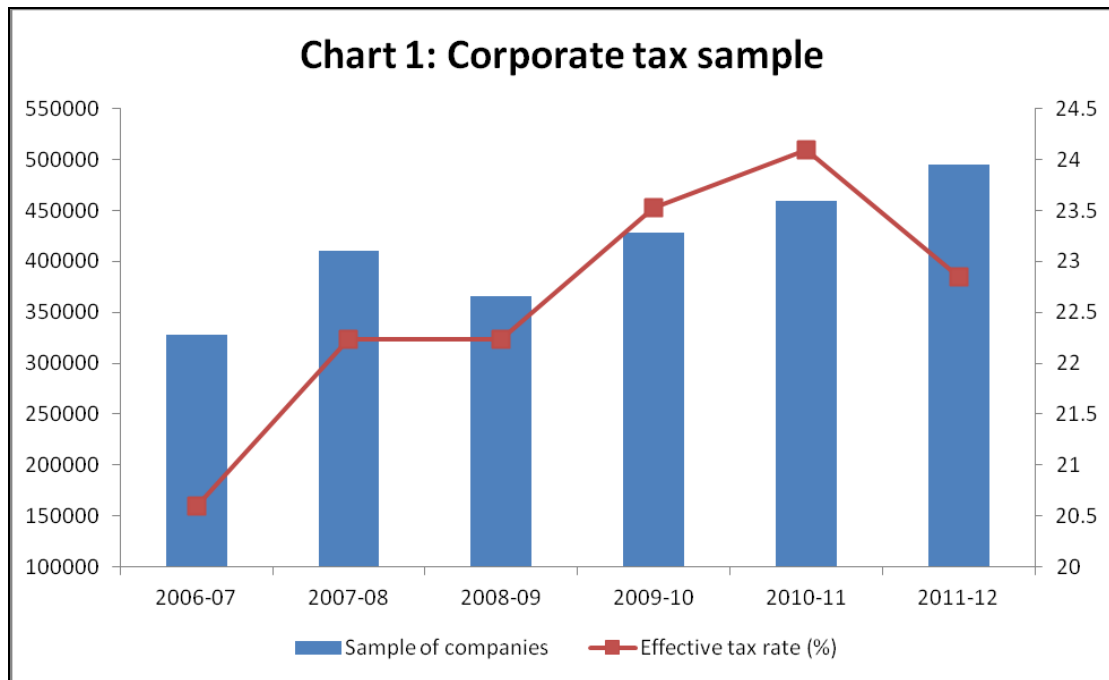
Revenues foregone through various concessions and tax preferences have become a significant part of fiscal policy. Although the Kelkar Committee Report on Direct Taxes (2003) had recommended reducing or eliminating such concessions while reducing tax rates, this has not happened. Indeed, while the tax rates have been reduced progressively since then, various concessions were also continued and then even expanded especially in the wake of the global crisis in [Budget 2009-10](#). As a result, such concessions have grown significantly in value. For 2012-13, they have been estimated at a total of Rs 5,73,627 crore – as much as ten per cent higher than the total fiscal deficit of the central government.

These "tax preferences" include a range of measures - such as special tax rates, exemptions, rebates, deductions, deferrals and credits - that are provided in accordance with certain policy priorities of the government, and obviously affect both the level and distribution of tax revenues.

As the Finance Ministry has noted, these tax preferences may be "viewed as an indirect subsidy to preferred taxpayers". These are essentially equivalent therefore to subsidies or expenditures, though the subsidy character is sought to be concealed by terming them tax expenditures. They are provided in various ways: as concessions on direct tax payments to companies and individuals, as well as reductions or rebates in customs and excise duties. The use of "subsidies" to characterise progressively redistributive welfare payments and "expenditures" to describe regressively redistributive tax concessions is indicative of the political economy embedded in official economic jargon. Here we will consider specifically the impact of corporate tax concessions in the recent past.

The latest Statement on "Revenue Foregone under the Central Tax System" (part of the Budget Papers of 2013-14) provides data on such tax expenditures in 2011-12. The concessions on corporation taxes amounted to Rs 61,765 crore, which was 61 per cent of the total benefits given to direct tax payers and around 12 per cent of the total amount of estimated tax expenditures. (It should be borne in mind that most of the indirect tax concessions are also effectively preferences given to companies, especially if they do not result in declines in retail prices faced by consumers.)

Since 2006-07, the Ministry of Finance has been providing estimates of revenues foregone through various concessions on tax payments and related fiscal measures. The data relating to corporate taxes are provided from the database of electronic returns filed by companies. In the last few years these have accounted for 90 per cent of the total corporate returns expected in that year. Chart 1 provides an idea of the number of companies used to derive these data and the average effective tax rate across these companies.



The number of companies has been increasing over the years, suggesting improved coverage of the sample. The effective tax rate also rose, particularly for the year 2009-10 and 2010-11, but declined again for 2011-12, the latest year for which actual data (rather than projections) are available. Even in 2011-12, the effective tax rate of 22.85 per cent was well below the statutory corporation tax rate of 32.45 per cent.

Table 1 shows how these rates varied by size of company, in terms of amount of profits. All sizes of companies (by amount of profit) paid much less than the statutory taxes. As expected, the largest companies with annual profits of more than Rs 500 crore accounted for the bulk of the profits and the greater amount of the tax payable. However, the effective burden of tax paid was among the lowest for them – only 21.67 per cent, substantially lower than the 26.26 per cent paid by smaller companies with less than Rs 1 crore of profits.

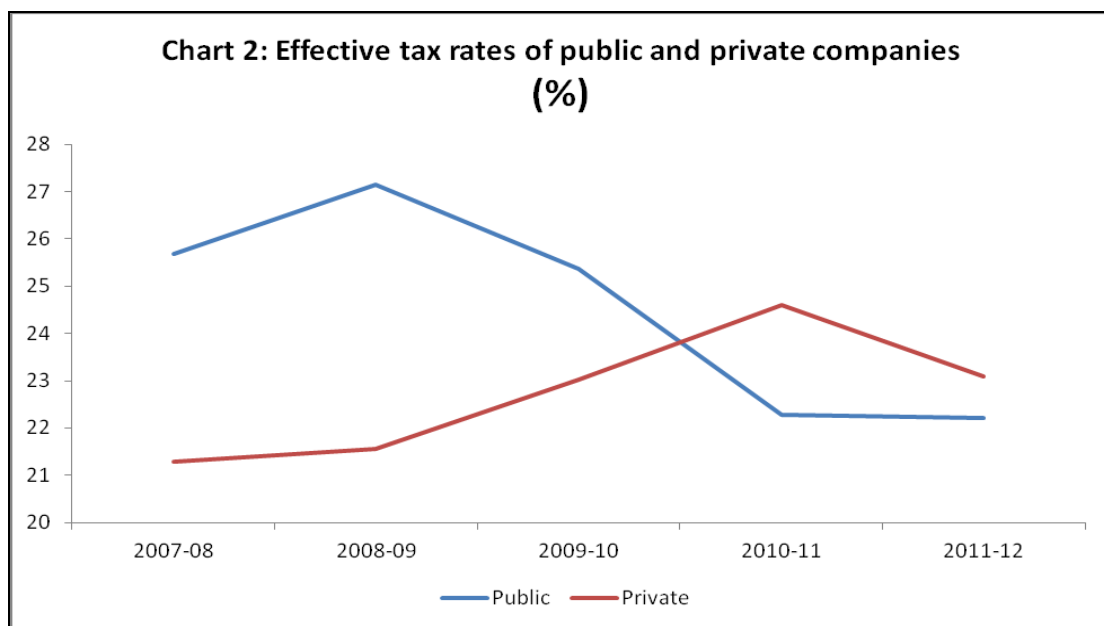
In previous years, the incidence of tax has been least on middle to large sized companies with Rs 50-100 crore of profits, but in 2011-12 the giant companies with more than Rs 100 crore of profits clearly paid the lowest rates of effective tax. They also showed the lowest rates of taxable income to profits before tax, indicating that they were the best placed to take advantage of the various fiscal concessions offered. This is of relevance when we note that the only major tax effort in the Budget for 2013-14 is the imposition of a 10 per cent surcharge on individuals and corporations with taxable incomes exceeding Rs. 1 crore. Besides the small numbers falling in this range, the concessions and exemptions exploited by corporates in this category would severely limit the additional resources garnered from the move.

**Table 1: Profile of sample companies in 2011-12**

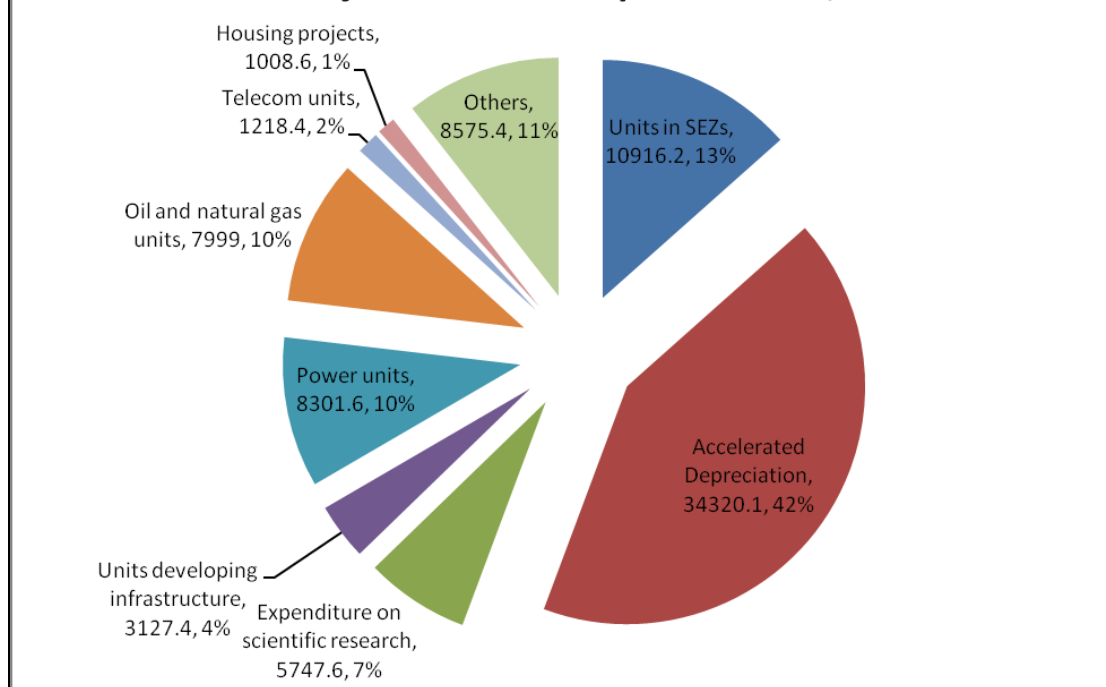
	Number of companies	Share in profits before taxes (%)	Share in total tax payable (%)	Total taxable income to profits before tax (%)	Effective tax rate (%)
Less than zero	184653	0	0.41		
Zero	30910	0	2.3		
Less than Rs 1 crore	249567	2.96	6.11	85.79	26.26
Rs 1-10 crore	23339	7.1	7.82	79.2	25.16
Rs 10-50 crore	4330	9.31	9.46	73.11	23.21
Rs 50-100 crore	755	5.28	5.21	71.24	22.54
Rs 100-500 crore	739	15.86	15	68.23	21.63
More than Rs 500 crore	252	59.49	56.4	68.99	21.67
All sample companies	494545	100	100	70.6	22.85

An interesting feature of recent years has been the reversal of the effective tax rates paid by public sector and private sector companies (Chart 2). Until 2010-11, the effective tax rates paid by public sector companies were significantly higher than those paid by the private corporate sector. However, in the latest two years for which data are available, public sector companies have shown a lower effective rate of taxes paid, although the gap has narrowed in 2011-12. This may be due to the tax concessions provided to oil and natural gas companies as well as to power and infrastructure companies, a significant number of which are in the public sector.

Chart 3 indicates the major items of tax expenditure that account for this ballooning fiscal cost of concessions. The biggest item by far is the tax incentive provided to Accelerated Depreciation, which in 2011-12 accounted for more than Rs 34,000 crore, or 42 per cent of the total direct tax preferences provided to corporates.



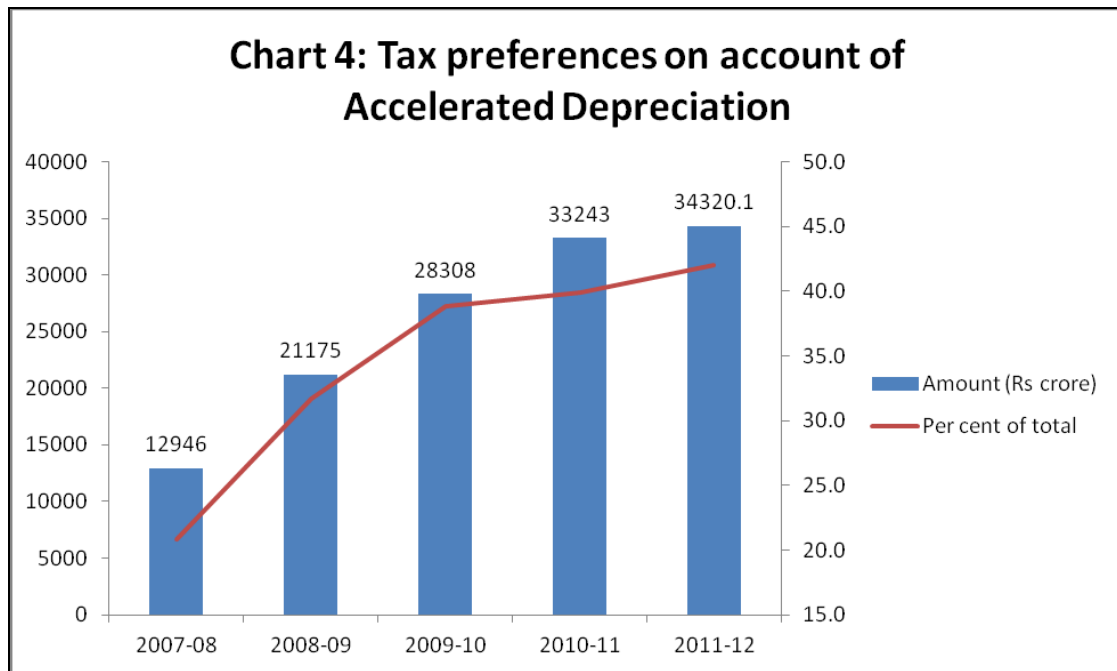
**Chart 3: Major items of tax preferences, 2011-12**



Companies in core infrastructure sectors – power and oil and gas – received around Rs 16,000 crore of benefits. Similarly providers of telecom services received Rs 1218 crore of direct tax concessions. While these are defended as necessary to promote much needed infrastructural investment, it is also true that this is one among the many ways in which the government is subsidising private firms being attracted to the infrastructural industries. Further, there are other categories of spending that have received significant tax preference that may not be so easy to justify on grounds of national development.

Units operating in SEZs received nearly Rs 11,000 crore in benefits, justifying the apprehensions that had been expressed about such tax concessions embedded in the SEZ Act by Mr Chidambaram during his earlier tenure as Finance Minister. This was in addition to nearly Rs 1000 crore of benefit received by companies engaged in development of SEZs. Further, it is evident that the actual loss in terms of foregone revenues under this head was significantly higher than was originally anticipated (by Rs 2763 crore), and it may be the case that in the current year as well, the revenue loss will be much greater than is anticipated in the Budget.

Industrial units engaged in the development of infrastructure facilities received more than Rs 3000 crore benefit in addition to the benefits of accelerated depreciation provision that effectively subsidised all new investment. Housing projects of all kinds – including luxury housing etc. – continue to receive significant tax concessions of more than Rs 1000 crore. The tax preference given to expenditure by companies on scientific research sounds unexceptionable. However, it is known that to exploit the R&D expenses tax benefit associated firms tend to include expenses on product differentiation and other minor modifications under R&D. That is, this figure actually includes measures of tax avoidance.



The most significant giveaways in the form of direct tax concessions to corporate India have come in the form of the Accelerated Depreciation allowance. As Chart 4 shows, this has also grown significantly over time. It is likely to continue to increase, because the projected amount of foregone taxes under this head for 2012-13 is nearly Rs 38,000 crore. It is intriguing that the amounts claimed under this head (and therefore lost as potential tax revenues that could finance much need public spending) have been going up so sharply at a time when corporate investment has been decelerating and even declining.

All this assumes special significance because in the proposed Budget there is a plan for a further concession: an investment allowance for new high value investments. “A company investing Rs 100 crore or more in plant and machinery during the period 1.4.2013 to 31.3.2015 will be entitled to deduct an investment allowance of 15 percent of the investment. This will be in addition to the current rates of depreciation.” (emphasis added)

As it happens, it is precisely the big guns of corporate India that have slowed down their investment in the recent past. Small and medium enterprises have been starved of credit and deprived of many other essential amenities and facilities that could ensure their viable functioning. In addition, as has been noted, they typically face much higher rates of effective taxation. Nevertheless, they are the ones that have kept the corporate sector ticking through this time of global and domestic uncertainty.

So it is surprising, to say the least, that the Finance Minister has chosen to provide a further tax concession only to giant companies to coax them to increase their spending. He claims that “there will be enormous spill-over benefits to small and medium enterprises”, but that has not been so evident in the recent past. It is far more likely that direct benefits to MSMEs would have had more impact on investment and therefore production and productivity, while costing much less for the exchequer.

These concessions have other implications as well. During the 2000s, when corporate profits were soaring, tax concessions in different forms provided to the corporate

sector amounted to well above one per cent of GDP. And corporate tax rebates are only one form in which the corporate sector is favoured, as the controversies over spectrum sale, coal blocks and even gas pricing suggest.

All this has reduced the fiscal space available for some much required public spending. Even the sum estimated by the Parliamentary Standing Committee on Food Security as needed to support its recommendation for universal provision in 2011-12 was less than one-fourth of the taxes foregone through various concessions in that year. Anyone with a sense of social priorities should, in the circumstances, recognise that the argument that the money is not available is without much basis. What is lacking is the will to mobilise the surplus and allocate it to where it is needed most.

\* [This article was originally published in the Business Line, March 4, 2013.](#)