TACKLING EXTREME INEQUALITY IN INDIA

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Despite a substantial decline in poverty, a persistent increase in inequality in favour of the top 1 per cent of the population over the decades has been a global phenomenon. Like many other countries, it is an area of concern also for India. The problem can be addressed through initiatives of proper taxation and expenditure policies domestically; complemented by concerted effort of countries to check some transnational problems, viz. tax havens, tax dodging and tax avoidance. This would turn help create an economy whose primary purpose is to benefit the 99 per cent of humanity. Taxation policies can reduce inequality and simultaneously augment revenues to the government, which can further be invested on health and education to create equal opportunity for all.

In the past few decades, there has been substantial reduction in extreme poverty across the globe. A marked progress in poverty reduction is visible especially during 1990 to 2010; and in this period, there has been a 50 per cent reduction[1] in the number of people living below the extreme poverty line. Despite the apparent successes; worldwide, one in eight people still go to bed hungry[2]. So, eradicating extreme poverty, which the world leaders have committed to, is still a distant goal.

At the same time, evidence suggests that one of the key obstacles to eradicate poverty is 'inequality', which has been increasing over the years and has reached its 'new extreme'[1] recently. The richest 1 per cent now have more wealth than the rest of the world combined and it is more alarming that 'power and privilege is being used to skew the economic system to increase the gap between the richest and the rest'[1]. The inequality problem is further exacerbated as the richest individuals are hiding their wealth using a global network of tax havens. As per recent estimates, tax havens enable the richest individuals to hide $7.6 trillion[1]. It is estimated by Oxfam that in 2015, just 62 individuals had the same wealth as the 3.6 billion bottom half of humanity whereas in 2010 the corresponding figure was 388 individuals. During 2010 to 2015, wealth of the richest 62 people has risen by 45 per cent, that is an increase of more than half a trillion dollars ($542bn), to $1.76 trillion. However, in the same period, the wealth of the bottom half dropped by 38 per cent which is a decrease by just over a trillion dollars[1]. It implies that far from trickling down, income and wealth are instead being sucked upwards at an alarming rate. Had inequality within countries not grown during that period, an extra 200 million people would have escaped poverty. So, it is clear that the fight against poverty will not be won until the inequality crisis is tackled properly.

In case of India too, there has been a considerable increase in inequality with the spending gap between the rich and poor almost doubling in the last five years[3]. In India, the richest 1 per cent of Indians have 58 per cent of total Indian wealth. Fifty seven billionaires have the same amount of wealth as the bottom 70 per cent of India. If India were to stop rising inequality, and instead hold inequality levels static, by 2019 we could lift 90 million people out of extreme poverty. Reducing inequality by 10 points, the equivalent of a 36 per cent reduction, could almost eliminate extreme poverty altogether, by the uplift of a further 83 million people[4].

Against this backdrop, taxation policy, among other things, could be an effective tool for addressing the deep rooted problem of poverty and inequality simultaneously. The resources generated through taxation could further be used for social services, viz. health and education. In this context, it is noteworthy to mention that one of the primary reasons why developing countries struggle to invest in public services like education and health is the lack of sufficient funds. Drawing upon the evidence, Oxfam India recommends the followings:

1. Introducing an Inheritance Tax and Raising the Wealth Tax;

2. Not reducing existing Corporate Tax rates and eliminating tax exemptions for corporates;

3. Cracking down on tax dodging by corporates and rich individuals, and ending the era of tax havens;

4. Increasing public expenditure on health from 1 per cent to 3 per cent of GDP; and

5. Increasing public expenditure on education from 3 per cent of GDP to 6 per cent.

INTRODUCING AN INHERITANCE TAX AND RAISING THE WEALTH TAX:

In the context of growing social inequity and injustice, inheritance tax and wealth tax could be an option to curb these as well as to generate additional resources. The philosophy behind inheritance taxes is that wealth should be created and earned, rather than inherited. It is the fact that once a fortune is accumulated or acquired it develops a momentum of its own. The super-rich have the money to spend on multiple investment options to secure annual returns far higher than ordinary savers and it leads to growing concentration of wealth.

As per the 2016 Forbes list, 1,810 dollar billionaires own $6.5 trillion which is equivalent to the wealth of the bottom 70 per cent of humanity. Oxfam's report found that whilst some billionaires owe their fortunes exclusively to hard work and talent, half of the world's billionaire wealth is either inherited or the result of crony connections with government. For developing countries, 71 per cent of billionaire wealth is either inherited or the result of crony connections. Global financial services company UBS has projected that over the next 20 years, 500 people will hand over $2.1 trillion to their heirs.

India is also experiencing a similar type of growing

1 An Economy for the 1%, Oxfam Briefing Paper, Oxfam GB, 18th January 2016

2 An Economy for the 99%, Oxfam Briefing Paper, Oxfam GB,16, January, 2017

3 Kundu, P. (2014), Major Dimension of Inequalities in India: Taxation, CBGA 2014

4 Nisha Agrawal & Namit, Agarwal, Inequality and the Indian Private Sector, IIC Quarterly, Autumn 2016, Vol. 43, No. 2

concentration of inherited wealth. In India, where direct tax revenue is low, for augmenting it, inheritance tax and wealth tax are yet to be explored properly. It should be noted here that in several G20 and BRICS countries, wealth tax is an important source of direct tax revenue[1]. The proportion of wealth tax in total gross tax revenue is one of the lowest in India - 0.09% only, that is, 0.009% of the GDP for 2011-12. Wealth tax has declined to 0.07 per cent of gross tax revenue in 2015-16, which is equivalent to 0.08 per cent of GDP. A conservative estimate has shown that the revenue potential of inheritance tax and wealth tax in India is around 0.8 per cent of the GDP (for 2011-12)[1].

In between 2000 and 2013, India's private wealth has reportedly increased drastically from USD 1.2 trillion to 3.6 trillion, that is, an increase by 300 per cent[1]. State of World Wealth Report[2] reveals that only about 20 per cent of this wealth is owned by the bottom 70 percent of India's households. The number of billionaires in India increased from only 2 in the mid-1990s to 46 in 2012 (Forbes, 2012) and their wealth constituted 10 per cent of India's GDP in 2012. The number of billionaires has increased further to 111[3] in 2016. Wealth held by billionaires in India came from three major sources - inheritance, self-made and 'inherited and growing'[4]. While a sizeable number of billionaires (21) are 'self-made', as revealed by a recent study done by Gandhi and Walton (2012)[5], about 40% of total billionaire wealth is in the 'inherited and growing' category. Further, the study also found that all of these billionaires are associated with corporate activities and notable wealth creation occurred in sectors with substantial potential for rent extraction and rent sharing between private and government players. It is also noteworthy that income inequality is underestimated due to hidden wealth, owned mostly by the richest segment of the population. In his 2013-14 budget speech, the Union Finance Minister Mr. P. Chidambaram, had quoted that out of the 3.7 crore income tax assesses in India, only 42,800 people's declared income was more than Rs. 1 crore a year. It is definitely a gross underestimation. Further, the official estimates of income, due to unavailability of information, also fail to capture the assets held by some people in offshore 'tax havens' (e.g. Mauritius, Cyprus, Cayman Islands etc.

Against this backdrop, it is imperative that Government of India introduce inheritance tax and raise the tax rate[6] on wealth.

NOT REDUCING EXISTING CORPORATE TAX RATES AND ELIMINATING TAX EXEMPTIONS FOR CORPORATES:

Oxfam's research[7] identified three core elements of corporate tax competition, such as, lowering corporate tax rates, offering wasteful tax incentives and a lack of international cooperation against tax avoidance due to these elements governments across the globe incur huge loss in revenue collection.

Countries often lower their corporate income tax rates in response to other countries doing the same, and often for unfounded reasons. There is a deeply entrenched assumption among governments that lowering corporate taxation is necessary to attract investment or to realise growth. Often this assumption is unfounded. When Australia planned to cut its corporate tax rates from 30 to 25 per cent, analysis by the Australian Commonwealth Treasury showed that it would only result in a very small increase in employment (0.1 per

1 Kundu, P. (2014), Major Dimension Inequalities in India: Taxation, CBGA 2014

2 State of World Wealth Report, Credit Suisse, a Switzerland based global bank, 2013

3 No. of Billionaires in India, in 2016 is 111. (Source: http://www.dnaindia.com/money/report-china-defeats-us-to-have-most-number-of-billionaires-in-2016-india-no3-2181962)

4 The terms coined in the Forbes list. This is the group of billionaires who inherited their wealth and subsequently experienced substantial growth in wealth.

5 A. Gandhi and M. Walton, 2012, "Where do India's Billionaires get their Wealth?", Economic and Political Weekly, Vol. – XLVII, No. 40, October 6, pp.1-14.

6 At present in India, Wealth-tax is levied at only 1% on the net wealth in excess of Rs. 30 lakhs.

7 Tax Battles, Oxfam GB, 12th December 2016.

TABLE 1: CORPORATE TAX RATES IN SELECTED COUNTRIES IN 2016

COUNTRY	Russia	China	South Africa	Brazil	Japan	India	France	Germany	USA
TAX RATE (%)	20.0	25.0	28.0	34.0	33.06	34.61	33.33	29.65	40.0

Source: http://www.livemint.com/Money/ybhCrBCOyXfRapVgNHPNVL/The-budget-should-cut-corporate-tax-rates-drastically.html

Note: It should be noted that if all exemptions are taken into account, effective corporate tax rates in India will be around 23 per cent or so, as mentioned in the Budget speech 2016.

cent in 20 years), wage growth (up less than 0.1 per cent per annum) and GDP growth (0.05 percent per annum)[1]. Other research[2] has shown that other factors (e.g. a well-educated workforce, living environment, etc.) are far more important when deciding where to invest. As Nobel Prize-winning economist Joseph Stiglitz said in 2014: 'The idea that lowering the corporate tax rate will lead to more investment is fundamentally wrong'[3]. On the other hand, corporate tax revenues can play an important role in enabling governments to finance the other factors that are more important for attracting investments.

It is often argued that tax incentives can play a positive role in attracting investment or helping a country shape its economy, and most of the countries across regions provide tax incentives. But, before providing tax incentives to corporates, proper parliamentary or public disclosure or scrutiny is the prerequisite; too often it is not done. Resultantly, tax incentives are often ineffective and have become associated with abuse and corruption.

However, large companies receive many tax incentives especially in developing economies like India. Developing countries are estimated to give away over USD 138 billion[4] just in statutory corporate income tax exemptions every year. Corporate tax exemption is one among many incentives that are offered. India has lost over Rs. 620 billion (Rs. 62,000 Crore)[5] in tax incentives to corporates in 2014-15. There are over 50,000 profitable Indian companies which do not pay any tax[6]. Despite this, it is a common practice for companies to resort to tax evasion through various mechanisms, especially the use of tax havens. Tax evasion takes away from the poorest people opportunities to get access to essential services.

The 'Revenue foregone statement under the Central Tax System' shows that aggregate revenue impact of tax incentives is Rs 5,49,984.1 crore for 2013-14 and is projected to be Rs 5,89,285.2 crore for 2014-15. The revenue foregone is estimated to be 43.2 per cent of total tax revenue for the year 2014-15[7]. There is an urgent need for detailed sectoral break-up of revenue foregone for different industries, with a comparative assessment regarding objectives of exemptions fulfilled vis-à-vis magnitude of exemptions. The Finance Minister, Arun Jaitley, announced[8] the phased reduction of corporate tax rate and phased elimination of exemptions from next financial year onwards. Although it is true that many developing countries have corporate tax rates below 30 per cent, researchers have highlighted this to be a worrying trend to reduce corporate tax rates. IMF's Keen and Simone (2004)[9] have noted, in their research on tax competition, that downward pressure on corporation tax revenues is more striking in developing economies than developed. So, there is a need for urgent deliberation on tax exemption and to rationalise it.

Given this situation, it is recommended that corporate tax rates in India should not be reduced and the practice of tax exemption to corporates should be eliminated.

CRACKING DOWN ON TAX DODGING BY CORPORATES AND RICH INDIVIDUALS, AND ENDING THE ERA OF TAX HAVENS:

Like large companies in other countries, Indian companies have liberally used tax havens in Mauritius, Cyprus, the Cayman Islands, etc., for tax planning and transfer pricing. Names of Indian nationals and companies in the Panama Papers is an indication that Indian companies are not far behind some of their global peers in tax dodging. It is therefore of critical importance that Indian companies pay fair taxes and stop tax avoidance and evasion in any form.

Various complex accounting mechanism and international loopholes are used by companies and individuals to reduce their tax burden, which is a common practice in most of the countries. The tax havens is one such legal means, which allows income

1 The Australia Institute. (2016). Company tax cuts do not add up to growth http://www.tai.org.au/content/company-tax-cuts-do-not-add-growth

2 An OECD policy brief from 2008 already stated that 'while tax is recognized as being an important factor in decisions on where to invest, it is not the main determinant'. See OECD. (2008). Tax Effects on foreign direct *investment* *https://www.oecd.org/investment/investment-policy/40152903.pdf* and Tax Justice Network. (2016). New research: *Competing' aggressively on tax reduces growth.* http://www.taxjustice.net/2016/01/06/new-research-competing-aggressively-tax-reduces-growth/

3 The New York Times (2014), The muddled road to overhauling corporate taxes. http://www.nytimes.com/2014/08/07/business/the-muddled-road-to-overhauling-corporate-taxes.html?_r=0

4 http://www.actionaid.org/sites/files/actionaid/give_us_a_break_-_how_big_ companies_are_getting_tax-free_deals_21_aug.pdf

5 http://www.hindustantimes.com/business/modi-calls-for-targeted-subsidies-questions-corporate-tax-breaks/story-IP1WX17PvJeyOfyLf0ZXxJ.html

6 http://thewire.in/25216/why-52911-profitable-indian-companies-pay-0-tax/

7 Rohith Jyothish, Taxation and Fiscal Policy Space in India, YOJANA March 2015

8 Budget Speech of Arun Jaitley, Budget 2015-2016, February 28, 2015.

9 Keen and Simone (2004), Tax Notes International, Special Supplement.

and wealth to flow offshore, untaxed and in secret. It leads the rich to stay rich and prevents essential redistribution that would reduce inequality and benefit society overall. So, the progressive principles, upon which most tax systems are based, is undermined by tax havens and it is an injustice. Tax dodging will continue to drain public budgets and undermine the ability of governments to tackle inequality until the rules are changed.

Between six and seven trillion dollars' worth of black wealth lies hidden in tax havens across the world, according to a fresh estimate by a trio of senior economists from the Bank of Italy in 2016. Indians' share in this is estimated at $152-181 billion, by one calculation. This is only wealth invested in shares and debt securities or held in bank deposits. It is impossible to get a handle on other wealth invested in physical assets like real estate, gold or art. On the basis of Reserve Bank of India data, Hindustan Times Analysis shows that in 44 years (1972 to 2015), India lost at least Rs 17 trillion to tax havens and out of this 95 per cent was in the last decade.

Tax evasion and tax avoidance[1] are the two major ways of escaping taxes. The popular ways of tax dodging[2] are: Money laundering, *Hawala,* Tax Havens, Transfer pricing and Trade mispricing. To change this requires global coordination. All governments need to commit to a second generation of tax reforms to effectively put an end to harmful corporate tax practices in a way that benefits all countries. Specific measures[3], as suggested by Oxfam, are:

- Establish a clear list of which are the worst tax havens, based on objective criteria, and free from political interference. The criteria must include transparency measures, very low tax rates and the existence of harmful tax practices granting substantial reductions. This could be done on an annual basis by a global tax body or in its absence another independent body. Strong measures (including sanctions and incentives depending on the context) should be then be used to limit base erosion and profit-shifting.

- Adopt strong defensive measures (including sanctions) against listed corporate tax havens to limit Base Erosion and Profit Shifting (BEPS). As a top priority, all countries should at least implement strong controlled foreign company (CFC) rules, which prevent multinationals based in those countries from artificially shifting profits into tax havens, which can be done without waiting for global agreement.

- Support those tax havens that are economically dependent on their tax haven status to build fairer, more sustainable and diversified economies.

It is recommended that the Government's efforts must be enhanced and measures taken to stop tax dodging by corporates and rich individuals by ending the era of tax havens.

INCREASING PUBLIC EXPENDITURE ON HEALTH FROM 1% GDP TO 3% GDP:

Public expenditure on Health was about 0.93 per cent of GDP in 2007–08 which increased to about 1.04 per cent during 2011–12.[4] As per the latest data available, the Total Health Expenditure (THE) in India in the FY 2013-14 is estimated to be 4.02% of the country's Gross Domestic Product (GDP), of which only 1.15% of GDP is public expenditure (National Health Accounts, 2016).[5] The rest is private out-of-pocket expenditure, three-fourths of which is on out-patient treatment and medicines.

The proportion of public spending on health by India is significantly lower than that by countries like Sri Lanka, China and Thailand.[6] This is not so because India is poorer than these countries, but mainly because of the very low priority that, historically, governments in India have accorded to the health sector, thereby allocating very less amount to public health[7].

Although the need to increase public expenditure on health has been acknowledged in several policy documents by Government of India, it has not been realised yet. The single most important policy

1 Tax evasion: Illegal practice of non-payment of tax liabilities and tax avoidance: Deliberate acts of reducing one's taxes by legal means.

2 Money laundering - an attempt to conceal the identity of illegally obtained proceeds; Hawala -an informal process of funneling money from one location to another through a network of Hawala brokers; Tax Havens - jurisdictions with zero or low tax rates that also offer a high degree of secrecy in financial matters; Transfer pricing – this refers to the transaction price of goods and services between related companies. Although not illegal in nature, severe manipulation in transfer pricing takes place in order to shift profits from high tax countries to low tax countries; and Trade mispricing - it occurs when import / export of particular goods or services are invoiced at a higher / lower rate of market price.

3 Tax Battles, Oxfam GB, 12th December 2016.

4 National Health Policy 2015 Draft. Ministry of Health and Family Welfare, Government of India.

5 National Health Accounts Estimates for India (2013-14). New Delhi: Ministry of Health and Family Welfare, Government of India.

6 World Health Organisation (2015). *World Health Statistics 2015.*

7 93rd Report of the Parliamentary Standing Committee on Health and Family Welfare, 2016

pronouncement of the National Health Policy 2002 articulated subsequently in the 10th, 11th and 12th Five Year Plans, the National Rural Health Mission framework, High Level Expert Group Report 2011 and the Parliamentary Standing Committee on Health and Family Welfare, 2016, was the **decision to increase public health expenditure to 2 to 3 per cent of the GDP**.[1] A major portion of these increased resources should be invested in primary health care services.

It should be noted that the result of this resource crunch is evident in the failure to expand health workforce, infrastructure and provide quality services. The Rural Health Statistics 2015 indicates that as on 31 March 2015, shortfall[2] (based on required number of posts vis-à-vis in position) of health assistants (female)/ Lady Health Visitor (LHV) at Primary Health Centres (PHCs) was 49 per cent and for health assistant (male) and doctors the shortfall was 61 and 12 per cent respectively. Out of the all functioning PHCs, 8 per cent were running without a doctor. Proportions of functioning PHCs without laboratory technicians and pharmacists are 38 and 22 per cent respectively. Specialist allopathic doctors are in very short supply in the public sector. At the Community Health Centres (CHCs) level, there was shortfall of 81 per cent, if 'specialist doctors in position' are compared to 'requirement[3] of doctors'. Out of these specialists, shortfall of surgeons and physicians was 83 per cent followed by pediatricians with 82 per cent and for obstetricians and gynecologists this shortfall was 76 per cent. Around 21 per cent of posts for nursing staffs at primary and community health centres are vacant.

In order to meet the national health goals and the sustainable development goals, the proportion spent by the government on health services must be increased with special focus on primary health care and augmenting health human resources.

INCREASING PUBLIC EXPENDITURE ON EDUCATION FROM 3% GDP TO 6 % GDP:

The Kothari Commission on education recommended 6 per cent of the GDP as a benchmark for improving education in the country and that was way back in 1966-68. The expenditure on education was never higher than 3 per cent of GDP from 2008-09 to 2014-15 and the last budget is not any different.

It is the fact that in many states, more than 37 per cent of teacher vacancies are not filled and around 1 million teachers are absent from the system. The education backwardness of the country could only be improved through proper public expenditure in education through increasing the quantity and quality of the same. One cannot expect to improve quality without public investment in education. For properly implementing the Right of children to free and compulsory Education Act, 2009, huge amount of resources should be channelised for education. So, in line with the recommendation of several committees and many right-based organisations, it is recommended that the government must increase the expenditure on education from 3 per cent of GDP to 6 per cent of GDP in a time bound manner for addressing the problem of human resource crunch, infrastructure etc. to make 'education for all' a reality.

An accountable, responsive government can reduce inequality effectively and create equal opportunity for all by reforming its policies. At the present juncture of extreme inequality, for welfare of the whole society, the government must redesign its tax policies to redistribute wealth by taxing the super-rich, who have accumulated wealth by inheritance or avoiding/ dodging taxes or using crony connections; and by spending the augmented resources on health, education to create equal opportunity for all.

1 93rd Report of the Parliamentary Standing Committee on Health and Family Welfare, 2016

2 Percentage of shortfalls are estimated from the data available in the Rural Health Statistics 2015.

3 "Requirement" is as per the Indian Public Health Standards (IPHS) norms.

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Oxfam is marking its 65th year in India this year. In 1951, Oxfam Great Britain, came to India during the Bihar famine to launch its full scale humanitarian response in a developing country. Over the past 64 years, Oxfam has supported civil society organisations across the length and breadth of the country. Oxfam India's vision is to help create an equal, just and sustainable society by empowering the underprivileged. It works primarily through grassroots organisations to bring deep-rooted sustainable changes in people's lives.

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