Weekly Notes

Deficit Financing—New Look

THE deficit financing estimated in the 1960-61 budget was Rs 153 crores. How did it come down to Rs 15 crores? True, in comparing the Revised Estimates with the Budget Estimate. an adjustment has to he made for a new item, viz Rs 210 crores received as investment of P L 480 funds which are now deposited with the Reserve Rank. This includes Rs 108 crores transferred from the State Bank; and the investment of P L 180 funds to that extent merely represents a transfer of ownership of Government bonds from one agency to another. But what of the remaining Rs 132 crores? There is a ticklish point hen- and in comparing deficit financing in the Revised Estimate with the Budget Estimate, the question arises whether one ought not to add this amount to the figure of Rs 15 crores specified as the "overall deficit' by the Finance Minister.

The doubt arises because though deficit financing during 1960-61 has nearly vanished, as if by a hat trick, money supply during the calendar year 1960 increased by Rs 217 crores (against Rs 80 crores and Rs 171 crores respectively in tile previous years). Deficit financing by Government is not, to be sure, the only factor responsible for an increase in money supply. To Government borrowing from the Reserve Bank has to be added the net creation of credit by the rest of banking system; and from that sum the external deficit has to be deducted. Dining 1960, Government borrowing from the banking system increased by only Rs 26 crores (Rs 175 crores from the Reserve Bank less Rs 150 crores disinvested by banks) while private borrowing from banks increased by as much as Rs 219 crores, making an aggregate of Rs 245 crores. The external deficit has taken away Rs 27 crores and money supply has thus expanded by Rs 217 crores. It seems, therefore, possible that the prime reason for the increase in money supply was private rather than Governmental 'deficit-financing'. But. one cannot be certain of tins until the transactions connected with counterpart funds are further analysed.

Inter *Corporate Dividends*

THE discrimination in taxation in favour of subsidiaries is proposed to be eliminated in the case of companies which are registered on or after April 1, this year. The present system of laxation of inter-corporate dividends is complicated and encourages foreign collaborators to seek majority control, since dividends from subsidiaries are taxed at substantially lower rates than those from other companies. To the extent that subsidiaries enjoyed a tax advantage, the proposed change would be a slight disincentive, particularly to the type of private foreign capital which does not want to share control. But this will be more than offset by the reduction which has also been proposed, from 63 per cent to 50 per cent, in the tax on royalties payable to foreign collaborators in pursuance of agreements entered into on or after April 1.

Under the existing scheme of taxation, dividends from subsidiaries are taxed at a uniform of 30 per cent. Dividends received from other companies registered before April 1. 1959, however are taxed at 45 per cent if the receiving companies are Indian and 63 per cent if they are foreign. In the case, of companies registered on or after April I, 1959. the respective lax rates are 40 and 53 per cent, It is now proposed that inter-corporate dividends paid by companies registered on or after April 1 will be taxed at 40 per cent, regardless of whether the paying company is a subsidiary or not and whether the receiving company is Indian or foreign.

While the new scheme does rationalise company taxation to some extent, it creates another special category of corporate income in that it applies only to investments in new companies. It discriminates against foreign investors who have taken up a minority interest. The scheme also discriminates against the taking up of new shares issued by older companies. The superimposition of the new on the existing scheme may consequently tend to encourage the setting up of new companies which may actually be no more than mere departments of old companies.

Whether the new scheme would help widen public participation in the ownership of joint stock companies, as the Finance Minister hopes. is, therefore, doubtful. As a matter of fact instead of encouraging wider public participation, the new scheme might only stimulate the growth of what are called 'joint subsidiaries', that is, companies which arc wholly or almost wholly owned by other companies. Many such 'joint subsidiaries' have been set up recently and not all of them involve foreign collaboration. Quite a few are the result of collaboration between Indian groups as well as companies within the same group. In other cases, ownership may be dispersed a little wider to the extent investment and other financial companies are attracted hy the lower rate of tax. But that is not wide participation in the real sense of the term.

If the purpose of the new scheme is to minimise double taxation of corporate income, it should apply to all companies, regardless of the year of their registration or at least to all companies registered since April 1, 1959. That would avoid discrimination against older companies us also against foreign investors who came in earlier.

Development Rebate and Financial Corporations

THE development rebate on new-plant and equipment installed after March 31 this year will he reduced from 25 to 20 per cent. The original purpose of this rebate was to give an incentive to new investment and to supplement the resources of companies modernising their equipment at prices much higher than the original prices on the basis of which they had made provision for depreciation. For the latter purpose, an extra depreciation allowance equal to normal depreciation was also allowed till March 31, 1959. Both these purposes have heen served, by and large. If some industrial units have Mill not modernised their equipment, it is not due to lack of tax incentives. Development rebate, along with the tax