

# THE ECONOMIC WEEKLY

Vol XVII No 13 March 27, 1965

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### THE ECONOMIC WEEKLY

Co-operative Insurance Building,  
Sir P M Road, Bombay-1

Grams: ECONWEEK  
Telephone : 253406

Annual Subscription: Rs 16

Foreign: 70 s or \$10.

## Thoughtless Move

THE general objective behind the amendment of the Income-Tax Rules setting limits on certain expenditures by companies is, let it be stated at the outset, unexceptionable. At present these expenditures are deductible from taxable profits and so companies are encouraged to inflate them—in any case, they have little incentive to control them as stringently as they might otherwise—since, in effect, something like one-half or more of the additional expenditure comes out of the Government's tax revenue and only the rest has to be borne by the company. As the Finance Minister pointed out when presenting the 1964-65 Budget: "the provisions of the Income-Tax Act allowing as deductible expenditure amounts spent wholly and exclusively for the purpose of business are being abused in respect or certain types of expenditure. Unduly large amounts are spent on daily allowance, on unnecessary bookings on planes and trains, on advertisement and on the maintenance of guest houses and suites of rooms in hotels outside the specific places of business, on providing conveyances and in paying high rents for accommodation for their officers and directors and in many other ways. . . . this tendency amongst companies is responsible in no small measure for the present high costs and the time has come to put a check on some at least of these expenses<sup>0</sup>. With these views of the Finance Minister we are in the fullest agreement; in fact, we deem it a pity that action along the lines he had proposed should have been so long in coming.

Having said that, we come to the main point of this editorial which is that in putting a ceiling on expenditure by companies on advertising, residential accommodation and travelling, the Finance Ministry has completely ignored, or missed, the distinctive character of expenditure on advertising which sets it apart from the other two types of expenditure. For the advertiser, the purpose of advertising is, of course, to make known some product or service or institution. From this point of view, the maximum now prescribed for advertising expenditure will be claimed to be inadequate to fulfil the legitimate and reasonable purposes of advertising. It is not proposed here to go into this question though, since the advertising requirements of different companies necessarily vary very widely depending on the nature of their products or services, the criticism that a uniform maximum rate is unduly harsh on certain companies has much force.

But the restriction on advertising expenditure needs to be judged as much from the point of view of advertising media (we shall be concerned here with the press) as from that of advertisers. This should be obvious if we consider the fact that advertising constitutes a major source of revenue to the press. To put the matter differently, the press is a producer of joint products — it sells copies of newspapers to readers as well as advertising space to advertisers. What the restriction on advertising by companies achieves, in effect, is to circumscribe the market for the second of the two products. The grave implications of this for the press deserve the most careful consideration, but it is clear that no such consideration has been given by those responsible for the decision to amend the Income-Tax Rules. If they had, they would certainly not have imposed the limit on advertising expenditure as casually as that *on* expenditure on residential accommodation and travelling!

It is true, of course, that advertisement expenditure as such has not been pegged, only the expenditure deductible for calculation of tax. Expenditure over the permissible limit will be disallowed and to that extent taxable profit: inflated. This amounts to a tax on advertising above the permissible maximum at the marginal rate of tax applicable to the company. No sophisticated estimates of the price elasticity of advertising are necessary to show that advertising above the deductible maximum will be severely restricted as a consequence.

Reliable data on the economics of the Indian press are notoriously non-existent, the Registrar of Newspapers' copious two-volume annual reports