

FARM LOAN WAIVERS AND TAX PAYERS' MORALE: A DILEMMA

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Abstract *Pressure has been mounting on central government for announcement of farm loan waivers before the Lok Sabha election due in first half of 2019 inasmuch; three state governments of Hindi heartland viz. Rajasthan, Madhya Pradesh and Chhattisgarh in December, 2018 have announced the same for executing their pre-poll commitments. The interest rate subventions and excessive subsidized fertilizers have not so far been yielded the desired outcomes hence for viable and sustainable farming government should come out with alternative ways for supporting them rather simply banking upon blanket waivers without analyzing the associated pros and cons and impact analysis. The repetitions of such waivers in long run would likely to demotivate the taxpayers and the cases of tax evasions probably to increase in leaps and bounds, inasmuch even after seven decades of independence the Indian tax system has not been reached to such a level of full proof as well as fraud proof. The economists have categorically warned about the adverse consequences of such blanket waivers along with taxpayers reservations have been highlighted on such political gimmicks at the costs of economic growth and development; the alternative ways for addressing farmers' plight have also been indicated.*

Keywords *Farm Loan Waiver, Economic Growth, Taxpayers, Informal Credit, Political Gimmick, MSP*

FARM LOAN WAIVERS - A POLITICAL BUZZWORD

Agricultural farm loan waivers have become center point of socioeconomic and political issue especially after the declaration of such waivers by the newly formed governments in three Hindi heartland states of Madhya Pradesh, Rajasthan and Chhattisgarh in mid-December, 2018. Related literature has shown multiple political parties have been using farm loan waiving as a strategy for winning the elections for the last three decades and more without giving due considerations the associated moral hazards (Desai, 2018). In the past few weeks in the print, electronic and in social media, the farm loan waivers have been debated largely from political angle rather than from the stand points of economics. The sharp fall in the prices of the farm produces in NDA-2 compared to UPA-2 period notwithstanding has been severely criticized by opposition political parties. But, from macroeconomics' perspective, such price cut has indicated a successful low inflation policy of Narendra Modi led NDA-2 government. The consistent high food prices would actually create strain in household budgets of lower and middle class Indians rather unlikely to bring any cheers for the farmers inasmuch too many cultivators have been producing too much produces. A latest, the survey report of NABARD has pointed out in 2016-17 that loan waivers have actually benefited only 30 percent farmers since such benefits were confined to big farmers rather small farmers whose quantum of loans were almost double of that of small farmers. Surprisingly, a CAG report has also affirmed that loan waivers scheme of the UPA-1 government was not been properly implemented due to number of irregularities and

lack of technology adoptions, and even substantial number of beneficiaries failed to get any relief due to lapses. Further, the report has affirmed that one-third of the benefited farmers were not been provided any acknowledgement letter for such loan waivers, a requisite document for applying fresh loans as mostly been happened in Bihar and Andhra Pradesh. Inasmuch small and marginal farmers lack collaterals for loans, they seldom could access formal credit. Interestingly, substantial numbers of Indian farmers have been borrowing from multiple sources beside institutional credit such as from *mahajans* (informal money lenders) and landlords and the borrowings of small and marginal farmers from these sources stand around 30 percent. All India Debt and Investment Survey, ICRIER, Working Paper No.-302, has categorically pointed out moneylenders have actually been providing informal credit to hoping 36 percent of the total agricultural debt with exorbitant interest rates ranging from 24 to 48 percent. The waiver politics have been worked at least since last 30 years have been established as double-edged swords for the farmers. On the one side, the problem of moral hazards persist; the farmers have been borrowing either beyond their affords or more than their requirements on the presumption that one day under the growing political pressure government would likely to waive the entire amount of loans, a deadly mechanism adopted for ruining the rural credit system. As far as the effect on banks' credit offtake especially in rural areas has been concerned, the waivers are likely to accelerate the stress and could lead to another agrarian crisis. The waivers has to hit the credit-deposit ratios for farm lending banks which, in turn, would probably de-motivate the banks for extending fresh farm loans due to NPA phobia.

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TAXATION - A FISCAL TOOL

Macro economists have preferred the term ‘public economics’ over ‘public finance’ inasmuch the objective of the former have included the application of economic analysis for addressing the problems of public policy, taxation, planning, role of government, inflation and management of public enterprises (Johansen, 1965).

Taxation policy has been supporting investments and structural transformations of the emerging and under developed economies for fostering the long-term growth and development. The basic objective of taxation is to allocate adequate amount of resources for ensured growth and development as well as for providing public services. The literature on taxation has defined ‘tax’ as a compulsory levy imposed by the governments on the residents’ incomes and wealth irrespective of any direct quid pro quo (Song & Yarbrough, 1978). Tax policy has been identified a vital mechanism by applying which private sector resources have being transferred for financing the public services (Rao, 2018). It has been argued that whenever taxes have been levied, it lead to distortions as these adversely affect private spending, saving and even risk absorbing capability. Taxation, in a wider perspective has demonstrated the associations between the state and the citizen. Literature has indicated taxpayers’ attitudes towards taxation have been identified as a vital predictor for tax compliance or tax evasion decisions (Jackson & Milliron, 1986), but, interestingly, Indian income tax saga has indicated a tug of war between the revenue-seeking government and the exemption-seeking taxpayers. The progressive tax structure designed for large corporates has multiple effects such as for the shareholders in the forms of lower earnings, dividends and market values; for the employees slim growths in the compensation levels and for the end users price escalations of goods and services. The need for a ‘straight forward and ease to interpretation’ and market friendly Indian tax system has been highlighted by scholars. Social scientists have been in consensus that taxations have been performing the role of catalysts for social and political changes. In addition, in Indian context the enactment of GST in July, 2017, has been taken positively as evident after the Gujarat poll result where the people have given a referendum in favor of NDA-2. Even though GST has been launched with due considerations of states’ demands, it has been covered merely 40 percent of Indian GDP and sectors such as real estate and petroleum have still remained excluded from its ambit.

THE FLIP SIDE

Statistically speaking, blanket farm loan waivers are unlikely to improve the farmers’ socioeconomic status; rather, these had created huge pressures on the governments’ exchequers. Data has shown that the 1989 farm loan waiver

had adversely affected nation’s GDP by almost 1.7 percent; even the Uttar Pradesh government’s farm loan waiver of 2017 was in tune to INR 363 billion, around 4 percent of the state’s GSDP (Mohanty, 2018). The least debated point was that banks’ agricultural loans have been insured by Agricultural insurance Company of India; hence, such blanket waivers would hamper the fiscal discipline. Farm loan waivers have been used as in the election manifesto of most of the political parties without considering the adequate fiscal space to absorb the same and the ruling political have been compelled to implement the NABARD has written the state governments who have declared waiving of farm loans to clear off the banks’ outstanding dues before any fresh cycle of loans processing. Adding to that, It has been well settled that the states have been bearing the fiscal burden of the farm loan waivers at the cost of the planned expenditure which adversely affecting the states’ growth momentum and employment generation. It has to be pondered that after the implementation of the recommendations of the Fourteenth Finance Commission and after redistribution of revenues between the states and center, the state governments are likely to incur higher capital expenditures than the central government. As far as consequences of the farm loan waivers have been concerned, it has been argued that the banks unlikely to extend any further loans to the farmers unless the state governments take initiatives to pay off the dues and such deferment would create the vicious cycle of poverty for the farmers. The central government had emphasized on improving the conditions of the distressed farmers and has planned in developing infrastructure like constructing new cold storages, developing new food processing industry; but, probably, it has committed a grave mistake by promising to enhance the minimum support prices (MSP) of the farm produces by one-and-half times ignoring the theory of free market economy. The consequences of the farm loan waivers likely be multiple such as the formal bank credits would substantially cut, unprecedented hikes in the interest rates of informal credits and increased probabilities of false reporting and scheme diversions. Furthermore, it would destroy the fiscal balance and by vitiating the loan repayment culture would likely to send a wrong message to the future entrepreneurs.

TAXPAYERS’ CONCERNS

It has been well settled that in the developing countries the role of governments for promoting growth and development is paramount inasmuch capital has been scared and contribution of private investments have remained insignificant. Governments have been attaining the objectives of growth and development through taxation policy. The role of taxation in economic growth and development has been multiple such as for resource mobilization, reduction in inequalities, social welfare, inflation controlling, balanced

regional economic development, and even earning and managing foreign exchanges. Literature has validated that indirect taxes have been playing prominent role in developing countries due to its wider coverage whereas direct taxes have primarily being levied for minimizing the income inequalities (Akani, 2010). Literature has indicated public economics has few distinctive features in developed countries such as prominent role of the governments for promoting growth and development and in the capital formations vis-a-vis in the developing economies (Musgrave & Musgrave, 1984; Prest, 1972). As far as impacts of direct and indirect taxes on individual taxpayers have been concerned, the former have substantial impacts on men since they have greater opportunities on employments and earnings (Elson, 1988) while the latter have significantly impacted the women notwithstanding the women have to manage their household budgets (Lodhi, 2000). Public investment-to-GDP ratio has shown inverse relationships, i.e., reduction in tax rates increases the disposable incomes which accelerate the demands for goods and services boosting GDP and creation of employment opportunities. On the flip side, due to fiscal consolidations, public investments have been adversely affected and for ensuring public debt sustainability, public investments are treating as an adjustment variable (Mehrotra & Valila, 2006). Taxations have reflected the state-society relationships with the taxpayers as fiscal relations have been identified as social relations formed by excellence and the sovereignty of the governments (Morar, 2015).

Related literature on tax compliance and evasions have documented that the psychological impacts of taxations have primarily been determined by the quantum and burden of taxes notwithstanding the taxpayers have been skeptical and trying to minimize their tax payments by contravening the taxation rules to the extent possible (Epstein & Gang, 2010). Literature has documented the objectives of taxations such as investing in defense equipment to protect the nations' territorial boundaries from the invasions (Scheve & Stasavage, 2010), to attain equality through redistributions (Farhi et al., 2012), and even to secure political loyalty (Bueno de Mesquita et al. 2003); but politics is likely to distort the game (see Carbonell-Nicolau, 2009). The recent announcements of farm loan waivers by three states have been antithetical in all its essence and scope such as public economics to financial system; which could lead to less tax compliances (Alingham & Sandmo, 1972) and to motivate towards parallel economy (Hibbs & Piculescu, 2010) for shunning the taxes, as related literature has validated. Interestingly, the modern approach of development has indicated political motives and institutional roles have been reflected in social changes (Engerman & Sokerloff, 2002). The *Ayushman Bharat Yojana* – world's largest public health program, launched in 2018 covering around 40 percent population with whopping budget of USD 800 billion – has acknowledged health as a wealth and for successful

implementations the current budget allocation of 1.4 percent of GDP has to be increased to at least 3.7 percent (Patel, 2018). After exhausting its initial allocated funds of INR 20000 million, the National Health Agency, the implementing agency, has sent a requisition to the Finance Ministry for additional INR 45000 million for the current fiscal 2018-19, and this points out the pressure it has put on the exchequer. Moving to the higher education sector, India has been spending merely 3.5–4 percent of her GDP even though UPA-2 had promised to increase the share to 6 percent, which is likely to remain an illusion. For the economic growth and development, creation and dissemination of knowledge has been identified as essential and lack of funding has been one of the prime impediments in achieving the target. For development and maintenance of the infrastructure, funds' crunch has been identified as a major roadblock. The private investments in the sector have been pumping along with public private partnership models, but such funding will likely be not sufficient due to longer gestation periods and stringent rules and regulations. Further, highly leveraged private investors have remained shy for high fluctuations in cash flows resulting minimal fresh capital infusion in the new projects. The equity market scenarios have also remained unreliable for the inherent uncertainties attached to it coupled with sluggish growth rates of the global economy. A close look on NDA-2 period infrastructure development expenditure data has indicated investments in roadways and railways have been significantly increased in the last 5 financial years but, massive increase of around 90 percent in the food subsidy bill has been reported with a static position in the fertilizer subsidy bills. The budgetary allocation for school education for the same period has remained almost unchanged while higher education funding has been boosted up by approximately 40 percent; but, on the other hand, fund allocation has witnessed a sharp cut in civil aviation sector. Surprisingly, capital expenditure in defense sector has been reported an increase of 19 percent while that of revenue expenditure has also been shoot up by 48 percent for the corresponding period. The substantial chunks of funds have been channeled for few projects such as *Bharatnet*, *Krishi Sinchi Yojana*, and *Namami Gange* beside others and Agricultural Ministry has witnessed highest funding in during the last five fiscals (Ninan, 2019). The blanket waivers likely to have long term dire consequences in the socio-economic arena in several ways e.g., there would be substantial cuts in the budgetary allocations for the development activities, sharp fall in the investments, damage in the rural credit culture with associated sharp increase in the problems of moral hazards. Eventually, repetitions of such waivers in long run would likely to demotivate the taxpayers and the cases of tax evasions probably to increase in leaps and bounds, inasmuch even after seven decades of our independence the Indian tax system has not been reached to such a level of full proof as well as fraud proof.

THE WAY FORWARD

It has been argued that mass farm loan waivers unlikely become as panacea for redressing farmers' distress. Economists have recommended number of alternative solutions e.g., extending specified support amounts per household through direct benefit transfers which could be explored in pan-India as the states like Telangana and Odisha have been already practicing the same since last few years. Agricultural studies have categorically validated that Indian farmers by and large have been accessing both formal and informal credit sources simultaneously and inasmuch the loans from the latter have been oscillating between 30 and 40 percent; these should be assigned the status of non-banking financial institutions. Further, by framing appropriate rules and regulations, the exorbitant interest rates and collaterals should be managed in better ways (Mohanty, 2018). The political leadership should be refraining from announcing such waivers rather may instruct the banks to streamline their agricultural credit policies by adopting multiple measures such as extension of loan repayment tenures, rationalizing terms of repayments, cutting the margins and rate of interests. The bailout efforts, if adopted by banks, would likely support the farms for reviving which, in turn, would yield revenues and cash flows for serving the current and outstanding installments as well. The waivers should be implemented with due diligence. The implementing banks should ensure that no willful borrowers be incorporated in the list of beneficiaries. As the governments have been announcing blanket waivers, it would be a Herculean task to differentiate the stressed and willful borrowers and the problems of moral hazards exist. To counter the same and maintain the sanctity of loans, governments should chalk out eligibility criteria and comply with stringent documentation procedures before extending the benefits of waivers, if further announced by any government. The procedure, if adopted, would substantially eliminate the willful borrowers and the burden on government exchequer likely to decrease significantly. Statistics has indicated around 70 percent of the agricultural farm loan amounts have been channelized as working capital hence capital assets have not been created adequately. The government should chalk out policies. The government should chalk out policies and to implement the same appropriate strategies it should framed. Further, governments should initiate for increasing the flow of funds for irrigations, construction of warehouses, investing in research and development for producing quality seeds, for farmers' training with innovative scientific farming techniques, for use of high quality fertilizers, automations in farming and applications of solar energies in extensive ways. The enhancements in the MSPs have been used by state governments as well as central government in different timescale for addressing the farmers' financial problems; but, such efforts have also been

applied without countering its implementation challenges. 16. The small and marginal farmers have been forced to sell their produces to the middlemen and mahajans from whom they have borrowed while harvesting and such social pressures unlikely to absorb. Unfortunately, their plight even remained unaddressed as they could have been rarely reached to the big mandis (grain markets) to get the MSP. The long distance, relatively higher transportation costs and lack of adequate number of warehouses have been forcing them to sell their outputs below the MSP. The interest rate subventions and excessive subsidized fertilizers have not so far been yielded the desired outcomes; hence, for viable and sustainable farming, the government should come out with alternative ways for supporting them rather simply banking upon blanket waivers without analyzing the associated pros and cons and impact analysis. The budgetary allocation should be channelized at higher proportion towards capital intensive projects rather revenue heads along with subsidies be controlled simultaneously. Interestingly, 'fiscal marksmanship', an analysis carried out to assay the accuracy of budget forecasting and to judge whether fiscal errors were actually randomly been taken place or not; has indicated that the state governments have committed the errors largely in capital budget forecasting rather in the calculations of revenue heads (Chakraborty, 2019). Taking cognizance the forecasts should be made carefully for minimizing the scope of fiscal marksmanship at its lowest level and such accuracy would likely to ease pressure in preparing revised budget estimates and subsequent downsizing in funds allocations to ministries.

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