

Opinion

FRIDAY, APRIL 14, 2017



DON'T BLAME THE EVM
 SY Quraishi, former chief election commissioner

The EC should be more vocal because the nation wants to hear the reassurances from it and not from me or previous officials. They have to ... aggressively demonstrate that EVM tampering cannot happen.

And who ensures this FRBM's targets are met?

Apart from the CEA's dissent, recall FY18's fiscal deficit is higher than the 3% that had to be reached by FY09

CHIEF ECONOMIC ADVISOR Arvind Subramanian makes a powerful point when, in a dissent note in the new FRBM committee report, he says the debt target of 60% of GDP is arbitrary, and the path to achieving it serpentine. While the committee talks of, on average, emerging markets with similar ratings as India having a debt/GDP ratio of 40% as compared to India's 70%, Subramanian points out that India experienced its greatest-ever growth in the mid-2000s when its debt was 10 percentage points (ppt) higher than now. When, after the global financial crisis, many advanced economies crossed even the 100% debt-to-GDP that was previously considered dangerous, he adds, interest rates actually fell to historically low levels—while this suggests a focus on only debt levels is misplaced, it would appear the direction in which debt is moving may even be more important than its level.

And while the committee has done well to bring in the element of contracyclicality—spend more in a bad year and less in a good one—that was missing in the original FRBM Act, the triggers are too severe to really help; indeed, Subramanian argues they even aggravate the problem. If real GDP falls from 5% to just above 2%, it fails to meet the 3 ppt trigger allowed for a 0.5 ppt relaxation in the fiscal deficit target, and if GDP growth rises from 6% to just below 9%, once again, the trigger is not set off. In other words, the relaxations are not enough to allow more spending in a bad year or to slow spending in a good year. In a situation of weak growth, as now, the new FRBM doesn't give the required flexibility to ramp up public spending. Nor is there any real logic to why, after a sharp 0.5 ppt compression in the fiscal deficit in FY18, there is a pause for two years or the subsequent path of compression.

While economists will debate whether the committee has adequately countered Subramanian's critique, the real issue is how to ensure the new targets are not 'paused' or put on 'hold' as they have in the past—the FY18 budget targets a fiscal deficit of 3.2% while the original FRBM saw a 3% level being achieved in FY09. The idea of an autonomous Fiscal Council—more than 35 countries have this—to monitor adherence to the targets and prepare independent reports on the government's fiscal performance is a good one, but it can't make the government stick to the target if it doesn't want to; a debt ceiling embedded in the law is a possibility but would make India vulnerable to US-style government shutdowns. Since market discipline is required, lowering mandatory SLR requirements could be one way to make bond yields more responsive to central government debt levels though it wouldn't help if, as now, SLR holdings of banks are much higher than what is even mandated. In the case of state governments, if some doubt was created over RBI's complete back-stop to their debt, this would ensure states would be penalised for poor debt dynamics. Allowing more FII presence in debt markets would also impose more discipline since such flows are more sensitive to debt levels but RBI needs to examine the larger implications of how much volatility is desirable.

Crafting new farm policy

More incentives for farmers, stable policy critical

THE STORY OF agriculture produce in India has been one of farmers mostly not getting their due, middlemen eating up a chunk of their profits and inadequate storage facilities resulting in big wastages. Although successive central governments have attempted to remedy this, few state governments have followed through with the policy changes. For instance, only a few states have taken fruits and vegetable out of the purview of APMC laws which is critical if farmers are to get better prices. In rewriting the APMC Act, the Centre is hoping to remedy the monopolistic nature of agricultural markets. If the states agree, most of the amendments proposed—a single unified market within a state, a single trading licence, allowing private wholesale market yards and farmer-consumer market yards to flourish and promoting e-trading—should ideally result in both the farmer and the buyers getting a better deal.

While the proper regulatory framework needs to be in place, what is more critical is the follow-up support from governments both at the Centre and in the states in creating the necessary infrastructure. The reason farmers sell their produce to aggregators, who then take it to the *mandis* in truckloads, is because it doesn't make sense for them to incur the cost of transporting small lots of produce across long distances. Bulk producers, in turn, prefer to buy from the *mandis* where they can pick up sufficient quantities even if they're paying more. The Azadpur *mandi* in Delhi, which sees a daily throughput of 8,000-9,000 tonnes, has remained the biggest market in the region with the *arhatiyas* holding sway despite APMC laws being changed. So, since it is hard to see the private sector bearing the cost of the necessary infrastructure, if the government wants new *mandis* to come up after the law is changed, it must come forward with financial support like, for instance, providing free land for new *mandis*.

If the government is looking to improve the marketing of agri-produce and reduce wastage, it must re-think its stand on allowing 100% FDI in multi-brand retail or conditions for food-retail. Large logistics players are likely to invest in transport and storage facilities if large global retailers are permitted to operate in the F&B sector. The presence of big retailers in the food chain could also pave the way for more contract farming; a stable and sensible export policy, similarly, would reassure players as global markets offer large and predictable volumes. Since very high *mandi* taxes, such as the 14.5% one in Punjab, are a big barrier to trade, increased government procurement in states like Madhya Pradesh and Chhattisgarh (and now UP) can help break Punjab/Haryana's stranglehold over procurement for ration shops—since 60% of the ₹13,000 crore of annual *mandi* taxes go to Punjab and Haryana, a reduction will both boost trading and increase farmer incomes.

Quite UNFAIR

Abhay Deol does well to show the mirror to celebs for endorsing fairness products

ACTOR ABHAY DEOL'S searing takedown of his Bollywood peers endorsing fairness products is perhaps one of the wake-up calls the latter needed, coming as it does against the backdrop of the attack on African students in Delhi and Rajya Sabha member Tarun Vijay's gauche attempt to explain away the racist streak in Indians by saying we are not racist as we co-exist peacefully with South Indians (an oblique reference to the stereotype of South Indians being dark complexioned). Deol posted ads featuring Shahrukh Khan, Sonam Kapoor, John Abraham and Deepika Padukone, amongst others, on his Facebook page with scathing comments. Translating the caption in the one featuring Khan, he said, SRK was “clearly trying to make you a man, becoming whiter in the process is just a side effect”.

Whatever the response from his target eventually turns out to be, Deol's schooling of Bollywood on its casual endorsement of skin-colour bias needs to percolate down to the *aam aadmi*. The signs are all there—the nation has an unhealthy obsession with fair skin. If the “seeking fair complexioned partner” bit repeated *ad nauseam* in matrimonial ads doesn't offer a convincing measure of this, the fact that fairness products make for more than half of the \$1.58 billion skincare industry in the country should. The sales of fairness products, in terms of revenue, outstrip the sales of Coke, as per a report in *The Guardian*. Underlined by such overwhelming preference for fair skin is a rejection of dark skin. Public icons endorsing fairness products only reinforces this bias. Deol's not alone in calling out Bollywood on the issue, actor Nandita Das, too, had launched a campaign a few years back. Tinsel town must pay heed to sane voices like theirs.

ADDRESSING AADHAAR'S FLAWS

THE AADHAAR ACT AND THE REGULATIONS PLACE NO ACCOUNTABILITY ON THE UIDAI TO PROTECT THE DATABASE OF PERSONAL INFORMATION PROVIDED BY CITIZENS

Audit Aadhaar database to weed out fakes

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As a result, Aadhaar remains an unverified database, containing crores of entries with no certification that the name against the biometric is correct.

Databases are only as good as what you put in them. However, sections 3(3) and 4(3) of the Aadhaar Act create the perception that the UIDAI guarantees the authenticity of all Aadhaar information, on the basis of which various government departments now require it as ID proof, unaware or unconcerned that the database is plagued with fake and ghost entries.

The minister for law and justice and for information technology has given an assurance on the floor of Parliament, that the government is sure of the authenticity of the data collected from 2010 to 2016. He has assured the House that the system created by the UIDAI is robust, safe and secure with no data leaks and no systematic problems. He also assured that the UIDAI is accountable to him and, through him (and along with him), accountable to Parliament. However, there have been numerous previous incidents of fake entries, including the recent case where Pakistani spies obtained Aadhaar cards under fake names but with their biometrics. If this results in a terror attack, who should the victims approach? The UIDAI? To truly deliver on the directions of sections 3(3) and 4(3), the UIDAI must immediately audit, clean up and re-verify the database to weed out fake and ghost entries. Ignoring this is unacceptable in view of the national interest.

Another issue is the debate on “mandatory” and “non-mandatory” use of Aadhaar for better delivery of subsidies. This debate is misplaced. It is really an issue of “exclusion” and “non-exclusion”. Aadhaar must be developed as the gateway for the delivery of subsidies because leakages in subsidies ultimately harm the poor and needy.

But Aadhaar should be made mandatory only after ensuring that it will not lead to the exclusion of the poor and needy.

The mandatory-non-mandatory confusion is being created by vague regulations made by the UIDAI, specifically Regulation 12 of the Enrolment and Update Regulations which seems to encourage a breach of Section 7 of the Act. This is a result of lack of proper oversight of the UIDAI. The UIDAI must be subject to stringent oversight, possibly through a Parliamentary Standing Committee on national identity.

The third issue is the issue of data integrity and the broader issue of privacy. As more and more people have become aware of Aadhaar and with its expansion to new areas, more concerns about its design, operation and misuse have surfaced. There are fears that such data shall be misused for surveillance. While some concerns are legitimate, many are caused by a lack of understanding and a lack of communication and transparency by the UIDAI. Such fears shall be misplaced if the government articulates clear safeguards to prevent such misuse.

This is an issue regarding the lack of reciprocal accountability on the part of those who collect, store and provide access to sensitive personal data of citizens. The Act and the regulations place no accountability on the UIDAI to protect the database of personal information provided by citizens. They are silent on the liability of the UIDAI and its personnel in

The confusion over the mandatory/non-mandatory nature of Aadhaar is being created by Regulation 12 of the Enrolment and Update Regulations which seemingly encourage a breach of Section 7 of the Aadhaar Act

case of non-compliance with the provisions of Section 3 and Chapter VI that require verification and protection of such data. How can this database be the gold-standard for identity if its entries are unverified, fake or fraudulent? Who is responsible? The recent fiasco of the storage and reuse of e-KYC data without permission is also widely known.

Privacy is a broader and more fundamental issue that goes beyond Aadhaar. It raises legitimate questions about the role and responsibilities of the state and other entities that are the custodians of our digital footprints at a time of rapid digitisation of our lives. The finance minister had stated during the debate on the Aadhaar Bill that privacy is a fundamental right, echoing my position in a PIL. The current provisions regarding privacy and data protection under the Aadhaar and the Information Technology Acts are skewed in favour of those who hold our data and places an extraordinary burden on the individual to get justice.

As the world's largest democracy, soon to be its largest digital democracy, we should lead the world in taking an enlightened approach to balancing our citizens' right to privacy with our national security considerations. The law minister (who also holds the IT portfolio) has stated that there are enough safeguards in the Aadhaar and the Information Technology Acts. With great respect, he is wrong. I would encourage the government to initiate a discussion on this and not take a rigid position. It is better for the government to take the lead rather than have the courts step in.

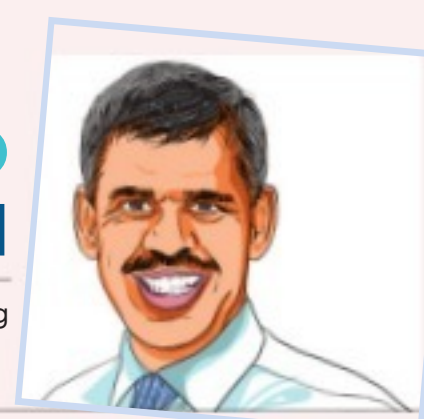
Constant change is normal in the digital world. The risks outlined here need to be addressed. There is a real need to be adaptive and changing, especially in the case of evolving Aadhaar from an unverified biometric database into a robust, reliable and authentic national ID platform.

Lessons from the United Airlines debacle

Its crisis-management effort lacked strategic underpinnings, a large slippage in times when crises are amplified by social media

MOHAMED A EL-ERIAN

Bloomberg



US-BASED UNITED Airlines is in the midst of a major reputational crisis after it decided to forcefully “re-accommodate” a passenger from an overbooked flight on Sunday. Yet, judging from a series of informal conversations I had with passengers at United's Los Angeles terminal and on one of their cross-country flights this week, the airline's frequent fliers don't seem to share the sense of outrage that's ubiquitous on social media. Some of the reasons for this discrepancy speak to important lessons about crisis management and prevention that United, and other companies, should take away from this now-notorious event.

Frequent travelers do not appear as shocked as others. They know that airlines overbook their planes almost routinely, betting that some passengers will change their travel plans at the last minute. They know that airlines offer passengers incentives to give up their seats when flights end up oversold, that sometimes passengers are involuntarily bumped off a flight, and that the airline has a legal right to do so.

Some of us have even been on flights, seated and ready to leave the gate, when suddenly there is a need to make space and someone has to deplane. I saw it happen when an acquaintance was asked by airline officials to wait for a later flight on a United Express commuter plane that was determined to have a weight issue, given updated information on prevailing winds. And most frequent travelers have witnessed irate passengers in one situation or the other, whether at the gate or on the plane. As such, and judging from my admittedly limited and far-from-representative survey, frequent fliers seem to be a lot less outraged and surprised about what happened on that flight from Chicago to Louisville than the rest of the world is. Yes,

United and law enforcement personnel exercised very poor judgment, and, critically, the use of force was totally and absolutely inappropriate. But planes get overbooked, and passengers get irate. It happens, as regrettable and disappointing as that is.

Contrast this with the general sense of outrage and dismay. And it's global: An event on a small US domestic route ended up being the No. 1 trending topic on Chinese social media, raising possible challenges for a company with greater aspirations for its Asian lines of business and beyond.

One of the major reasons for this discrepancy is that customers with different levels of information have different expectations about what “normal” looks like. And that is something that companies like United should reflect much better in their contingency planning.

In the critical minutes of crisis management following the highly unfortunate incident, United failed miserably in explaining the context for its decisions. Its first set of communications was not just poor and badly structured. It was also overly ambitious in trying to differentiate between different stakeholders operating on an information playing field that was far from level. With its dismal failure to get the facts out quickly, United actually fueled rather than diffused the spread of outrage. Rather than stumble through the difficult exercise of reconciling multiple constituencies using different messages, United should have initially focused on their most important ones—their customers. The company could (and should have) expressed up-front genuine remorse for a customer who—remember—sadly ended up in hospital, rather than calling him “disruptive and belligerent.” Moreover, in this day of rapid video dissemination, it took the air-

line way too long to counter the awful images of the incident with its own video of genuine apology and proper explanation.

Then there was the biggest failure of all: United should have dealt with the oversold situation before starting the boarding process. Did they not know about their personnel requirements at that time? Denying someone a seat on a plane is bad enough; doing so when the person is already sitting in it is a disaster to be avoided at all cost. If anything, it doesn't provide the airline with much of an opportunity to explain to passengers why they were selected. Indeed, the most important takeaway from any crisis-management discussion is the need to strengthen crisis prevention!

Finally, and in what may be the most relevant lesson for the business community as a whole, it seems that United's management had not done spent enough time and energy on effective scenario planning. Apparently, there was insufficient focus on the “what ifs,” both internally generated (as was the case here) and in response to fake news.

Lacking a clearly anchored tone and a well-established approach, their crisis-management effort came across as unprofessional, disjointed, and—especially—lacking in strategic underpinnings. This is a particularly large slippage at a time when companies have to live with a lot more “unusual uncertainty”, seeing any mishap easily amplified by social media. And it happened in a world in which companies already have to deal with a much longer list of improbables becoming reality. While this awful incident is unlikely to change United's business outlook in a material way over the long-term, it carries important lessons. The faster they are absorbed by the business community as a whole, the better it is for customers, too.

LETTERS TO THE EDITOR

Cow politics sidelines growth focus

APROPOS OF THE article ‘Cow vigilantism—or Muslim hunting?’ (FE April 12), in ancient India, beef always figured in banquets for guests and saints. In Kosala, the kingdom of Raghava Rama, venerable visitors to the court used to be served the choicest dishes of beef, with curries and honey. Mahatma Gandhi, a redoubtable Hindu with an unflinching commitment to secularism, never subscribed to the idea of a ban on cow slaughter. And the article in the Directive Principles of State Policy is for framing laws to help sustain the economic benefits of the livestock and not to buttress the devotion to cow. However, the violence that has been unleashed invoking the Directive Principles, completely negates the philosophy of the document. One is compelled to read the script of this madness. First, the overt incidents of aggression were to intimidate, provoke and subjugate the minority, the Muslims. Secondly, the states in the East, South and North East, which had never shown empathy for this project, needed to be tamed and made subservient to the Northern hegemony. And, lastly, the current regime is convinced the holy cow is the one divisive and emotive symbol, a sure bet for success, as the pithy promise of governance and development might not garner many votes in the next round. Caught in this viciousness is the struggling economy. India is home to roughly 200 million domestic cattle and exports 2 million tonnes of beef and veal in a year. Indigenous beef/buffalo consumption is about 2.5 million tonnes. Meat exports grow at 14% every year. Along with farmers, beef ban could render many jobless; about 2.5 million in the leather industry alone. India has to push the cow necessarily to the sidelines to clear the path for progress.

— Haridasan Rajan, Kozhikode

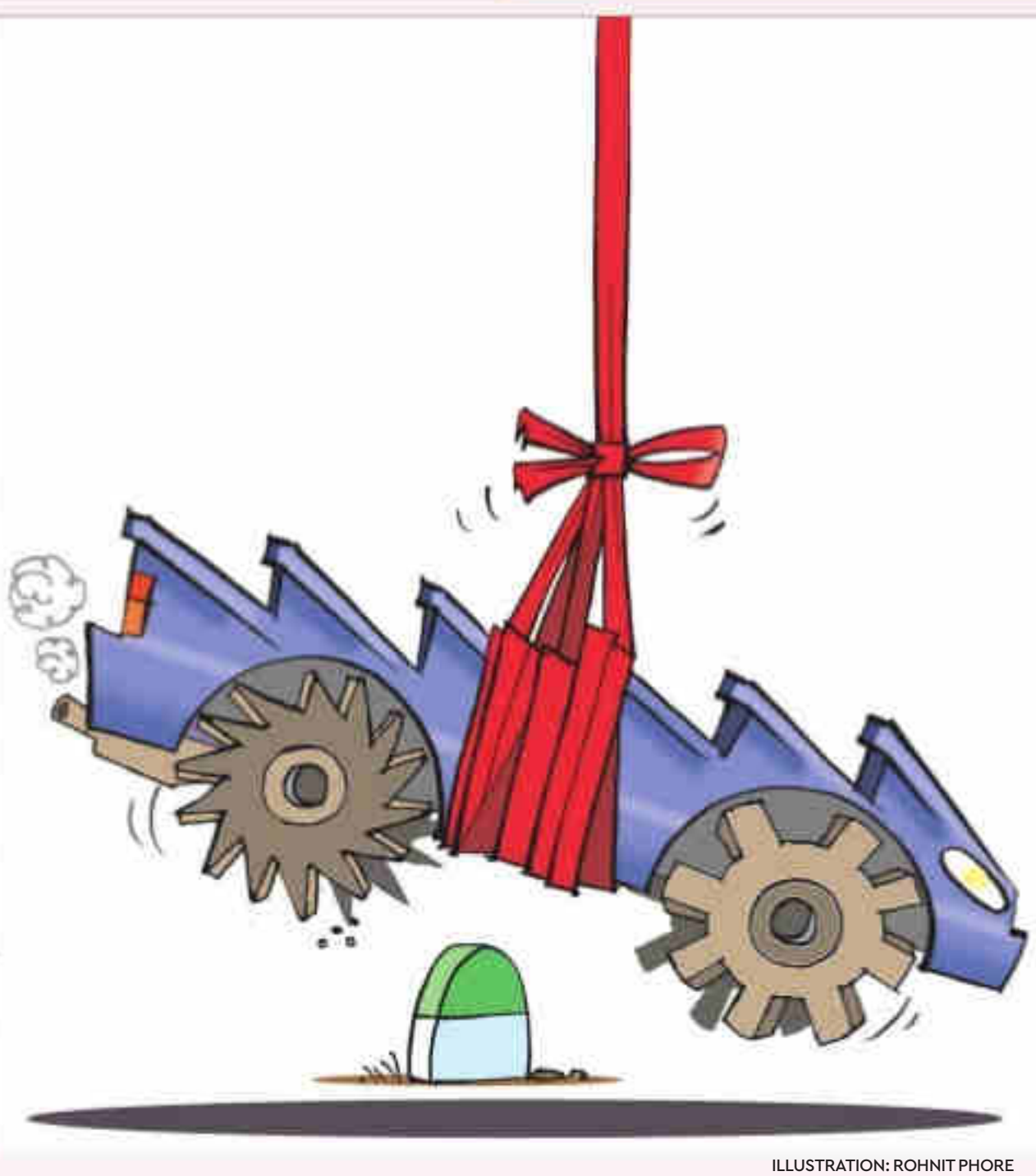


ILLUSTRATION: ROHNIT PHORE

● EASE OF DOING BUSINESS

RAGHU DAYAL



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An attack on all fronts

Government's bid to improve rank from 130th to 30th by 2020 needs more coordination

DID YOU EVER comprehend how difficult a place India is to do business? World Bank's 2017 Edition of Doing Business report offers a glimpse; it ranks India 130 among 190 economies in Ease of Doing Business (EoDB), only one spot better than the previous year.

The 2017 DB report, covering business regulations up to end-May 2016, ranks India in the top-50 in three of the ten parameters, ie, protecting minority investors (rank:13th), getting electricity (26th), and getting credit (44th). It continues to be a poor performer with regard to construction permits, paying taxes, enforcing contracts, starting a business, registering property, and resolving insolvency.

India's current ranking on starting a business is 155th. It takes 26 days to deal with 13 procedures, New Zealand, ranked one takes just half a day for only one. Issuance of construction permits in New Zealand takes 93 days for 10 procedures; India on the other hand takes 190 for 35 procedures, and ranks 185th. For obtaining an electric connection, South Korea at No 1 takes 18 days dealing with three procedures; notwithstanding its ranking for this index having improved to 26th, India consumes over 46 days.

New Zealand, again at the top in registering property, takes one day for two procedures; India, ranks 138th, taking 47 days for seven procedures. For paying taxes, Qatar, commanding the top position, takes 41 hours for four payments annually; India at 172nd takes 241 hours for 25 payments. Average duration of bankruptcy proceedings in India is around 4.3 years; in Singapore just 9.5 months. India takes on average 1,420 days for judicial process to be over versus 290 days in Korea.

Following a clamour from India Inc for freeing the country from complex regulatory regime, PM announced, during the 'Make in India' launch on September 25, 2014, that the government would push for India's ease of DB rank to be within the top 50.

Russian president Vladimir Putin's in May 2012 had decreed bureaucratic to improve its ranking from 120th to 20th by 2018. And, Russia has steadily moved ahead—from 120th in 2012 to 112nd in 2013, 92nd in 2014, 62nd in 2015, 51st in 2016, 40th in 2017. India, on the other hand, having remained stuck at around 130, trails behind some of the SAARC countries: Bhutan (73), Nepal (107), Sri Lanka (110). Indian government is targeting the 90th spot in 2017-18 and 30th by 2020.

But to secure a better rank, government functionaries must first acknowledge that sloganaries and shibboleths, intents and promises are of no avail; it is delivery on the ground alone that matters. That is where Indian administration has floundered.

The Economist explained how despite India's regulations for foreign investors be-

ing more attractive than in most of East Asia, its overzealous bureaucrats weave webs of red tape. For example, the e-government initiative MCA-21 in 2006 enabled registration time to be reduced, now to obtain certificate of incorporation, time available online, also dropped, but bureaucratic stranglehold came through the backdoor—the applicant was still required to wait to receive a physical copy of the certificate before starting activities!

In India, local business regulations and their enforcement differ across locations. A World Bank Group-coordinated Assessment of State Implementation of Business Reforms in India, analysed up to June 2015, revealed that states were at very different levels of implementation of the 98-point action plan on EoDB. While Gujarat, Andhra Pradesh, Jharkhand, Chhattisgarh and Madhya Pradesh scored over 60%, Odisha, Maharashtra, Karnataka, Uttar Pradesh, West Bengal, Tamil Nadu, Telangana and Haryana performed above 40% but below 60%; Delhi, Punjab, Kerala and Goa figured in the 20-40% range, and all others below 20%. On an average, only 32% of the proposed reforms were implemented across the country; implementation regarding inspection and enforcement of contracts remaining less than 20%.

Some sporadic initiatives now hold out hope of a meaningful way ahead: nodal departments have been designated for each DB indicator to accomplish well coordinated progress in key areas such as an eBiz portal providing one-stop shop for registration for PAN/TAN, EPFO, and ESIC; MCA, CBDT and ministry of labour jointly mandating to cut the number of procedures for starting a business as well as the number of days to start a business to four; Central Registry of Securitisation Asset Reconstruction and Security Interest database being integrated with RoC to create a single registry of assets; e-courts to be expedited for electronic filing of complaints, summons and payments—especially in commercial courts—enabling country's "enforcing contracts" indicator to improve; and the number of permits to be reduced to no more than eight towards an improvement in the "construction permits" indicator.

The Rajya Sabha sub-committee on EoDB recommended that a simple online single window approval mechanism coupled with self-assessment/declaration of having complied with the applicable regulations be ensured, for which a Common Application Form (CAF) needed to be notified by the state governments to make it acceptable to all agencies.

Other measures need to be pushed relentlessly—including, inter alia, simplification of taxation laws and cleaning up the Finance Act—as envisaged by the P Shome and Justice Easwar panels.

A large state is not necessarily a strong state. The very gigantism of public entities makes them slow and clumsy.

● A CHANGE AGENT

Accruals from the GST regime

BAPPADITYA MUKHOPADHYAYA



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The tax can lead to a formalisation of the workforce

FINALLY, GST IS a reality. It took 17 years after inputs from four central governments, over 100 state governments, various committees, numerous discussions and a marathon seven hours debate in the Lok Sabha last week. The new indirect tax regime is all set to take over from July 1, 2017. GST is simplification of the existing indirect taxes by subsuming them into four bands of 5%, 12%, 18% and 28%. This apart, another category of tax between 40 and 65% will be imposed on luxury goods and socially 'bad' goods. Across the board, experts are hailing this as the second most important milestone in the history of Indian economy post-liberalisation of 1991. It is, therefore, imperative to ask how good and services tax (GST) will change things? To assess the benefits, we must look at both the direct and indirect benefits of GST. Estimating the direct benefits imply assessing the three major stakeholders who will get affected by the new tax code—the consumers, the enterprise and the government. The indirect benefit is that it will bring a structural change in the way businesses are conducted across the country.

It is, now, estimated that the overall impact on the consumer price index (CPI) will be deflationary, to the tune of -0.6%. This will be largely owing to the zero-tax regime on essential food items that forms a large part of the wholesale price index (WPI) basket. However, these estimates are static in nature. It compares indirect taxes to the end consumer, based on their current consumption patterns. Surely, such patterns are bound to change with the new effective prices they face, especially as more and more services make way into the consumption basket. Therefore, it may be too early to estimate how this will affect the inflationary forces. What then will be the effect on overall indirect tax collection? In the Union Budget 2017-18, the government estimates to collect nearly ₹19.27 lakh crore

GST would change the way we do business, but it may also change the political economy. The usual 'populist' tax breaks in every subsequent budgets may be history now

from indirect taxes next fiscal, up 9% over 2016-17. Undoubtedly, this is a positive step especially coming in the backdrop of an 11% increase in tax collection from services. Finally, what does it mean for the business? Initial estimates have already identified gainers and losers. What remains of primary concern to us is how will the benefits translate into employment, given India has witnessed jobless growth in the last decade? The curious case of jobless growth we have seen over the years puts all such exercises irrelevant. The true success of the GST will not be measured in terms of its impact on inflation or indirect tax collection, but on creating jobs! Does GST have anything there?

This is where the indirect benefits of GST will perhaps be more visible than direct effects. Goods and services tax has the potential to change things by making tax compliance simple. This will be an incentive for small and medium enterprises (SMEs) to be part of the formal tax structure. In fact, it would be almost mandatory now because the entire supply chain would now have to be accounted for in the tax chain. The reason is plain to see. Firms up the value chain would only contract with those below whose taxes they can write-off. This would encourage more from the informal sector to join the formal sector. Various estimates peg the share of workforce in the informal sector at about 86% of total workforce. For one, any move from informal to formal sector would benefit the workforce who will be retained. However, there will be few job losses. But this is where the enabling systems need to work well for the indirect tax to be a success.

While most experts view the main advantage of GST as making it easier for existing businesses, the advantage needs to understand the impact it will have on new start-ups and tweak incentives, if necessary. For example, the tax offsets would require maintaining higher working capital now. Thus, an accompanying thrust that makes working capital easily available would be a natural response. Goods and services tax would change the way we do business, but it is also expected to change the political economy. The usual 'populist' tax breaks in every subsequent budgets may be history now. This is investing for economies infrastructure. The issue is do we have the will and the architecture to go the distance?

Start-ups, angels and India

SUSHANTO MITRA

The author is founder & CEO, Lead Angel Networks. Views are personal

INDIA IS THE world's third largest start-up ecosystem with over 4,200 start-ups in existence according to NASSCOM. Yet, in terms of VCs and angel networks, India compares poorly to the developed world. In the US alone, there are an estimated 1,300 venture funds in operation in contrast to a paltry 156 in India. Similarly, USA has over 900 angel networks and almost a million people who invest in early stage companies.

share their experiences and interact they realised that forming groups and pooling their investment and expertise would help reducing overall risk of investing and improve their ability to support their companies. These angels got together to form angel networks to co-ordinate their activities and also to delegate some of the administrative functions to their staff.

The way an angel network works, is that the secretariat identifies promising start-ups, and then passes them on to a group of members who shortlist two to three start-ups to physically present at the monthly meetings. If members are interested in a specific company, a select group studies the business further and negotiates the terms of the investment. Evaluation in angel network delegated to experts in the group reducing risk to individuals. In all angel networks the decision to invest and the quantum of investment remains entirely with the individual. In contrast, in the case of funds, the investment decisions and subsequent support is provided by the execu-

tive team. Angel investments typically range as a group from ₹50 lakh to even ₹6 crore. Post the investment commitments; there is a financial and legal due-diligence of the company. This is essentially to analyse and validate the company's business assumptions, and also to check if its operations are within the ambit of law.

In India, the rise of angel investing happened post the dotcom bust with successful entrepreneurs in Mumbai and Delhi forming groups. These have seen rapid growth especially from 2014 buoyed by the success of companies like Flipkart, Ola and Redbus, and have spread to other cities such as Bangalore, Hyderabad and Chennai. More recently, even tier-two metros have seen the emergence of angel networks. In India, there are both the national networks and others that are local to a city or regional. National networks with their larger size and usually bigger secretarial team are more connected to the funds and other ecosystem players. City specific angel networks could have more local knowledge to provide

better support to the start-ups.

Most of the angel networks in India are set up as not-for-profit organisations, and are managed by elected presidents or boards and run in a similar way to clubs and residents associations. More recently there are private angel clubs that have also come up that are professionally managed. This apart, there are also electronic platforms that have also come up. These are more like marketplaces for start-ups to raise money

Going forward, as offline angel networks in both for-profit and not-for-profit categories, bring online elements such as video recording of pitches and live tele-conversations with entrepreneurs and investors, the differences between the marketplaces and angel networks will erode over time. SEBI is expected to come up with crowdfunding regulations similar to the ones in the western world. If and when that happens, the public will be able to make investments in early stage companies in a more secure way either with physical networks or with electronic platforms.

TAX TANGLE

Our love for complexity

All defects and complexity in design notwithstanding, rollout of GST would be an outstanding achievement

HARDAYAL SINGH



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many of which will be dragged to the Supreme Court, thus further clogging an inefficient judicial delivery system. High tax rates on goods consumed by the rich make for attractive socialist rhetoric, but in reality they are counter-productive, especially in a country like India. They are unjustified for another reason as well: luxury goods are usually expensive; and a person who buys them will in any case have to pay a higher price plus higher tax even at the standard rate. Why then should she be called upon to pay tax at anything more than this rate? In fact, many social scientists would argue that what a person

chooses to consume is essentially a matter of personal choice—the role of the state in determining such choices should be minimal.

All these defects and complexity in design notwithstanding, the roll out of GST in a vast, diverse country such as ours, must stand out as one of the outstanding achievements of our times. The other development relates to the field of income tax: It involves a case study which is reflective of the failures of our governance. The case itself is unremarkable, except that it is typical of the climate of uncertainty and confusion often created by hastily drafted



FM Arun Jaitley chairing the 13th GST Council Meeting in New Delhi PTI

tax laws. Yokogawa India Ltd is an Indian company, but is controlled by its Japanese parent headquartered in Tokyo. In its return of income for the assessment year 2002-03, it claimed that the income from one of its 100% export-oriented units was exempt from tax under section 10A of the Income Tax Act. This section figures in chapter III of the Act which deals with exemptions. But the section itself strangely stipulates that the profits and gains of the undertaking would be allowed as a deduction from total income. If taken literally, this concept would be impossible to implement because total income is the final

figure on which tax is computed. We can conceive of a deduction in the computation of business income or from gross total income but not a deduction from total income.

The Supreme Court has now resolved the controversy fifteen years after the assessee first made the claim, and four years after the provision was discontinued. It has ruled that the provision provides a deduction to be allowed from business profits.

Nonetheless, it does raise a number of serious concerns for everyone who wants to see governance improve: One, why should a tax instrument, devised primar-

ily for raising revenue be used for extraneous purposes? If exports are to be encouraged, or scientific research or family planning promoted, rather than provide for a tax relief, would it not make much more sense for the government to pay a cash subsidy directly to the taxpayer? If this were to happen, the line ministries too, might become less enthusiastic in sponsoring such schemes.

Two, tax officials are not the objects to ascertain whether the objectives which the government wants to achieve through such tax provisions are actually being realised or not.

Three, such provisions have contributed significantly in cluttering various judicial forums. The latest report of the Comptroller and auditor general (CAG) on direct taxes (2 of 2017) indicates that as on March 31, 2016, 70,371 cases with a revenue of ₹3.04 lakh crore were locked up in appeals filed before the Income Tax Appellate Tribunal, High Courts and the Supreme Court.

Finally, some of the best brains of the nation are involved in interpreting the scope of tax reliefs; their talent could perhaps be much better harnessed for doing something more productive.

More than a hundred years ago, Lord Macnaghten reminded the House of Lords: "Income-tax, if it may be pardoned for saying so, is a tax on income. It is not meant to be a tax on anything else."

In India, income-tax did not take this route. We hope GST would do much better.