

CUTS intervention leads to rise in State revenues in Rajasthan

Following a research study by CUTS, the Government of Rajasthan changed its excise policy, which led to a quantum jump in excise revenues by nearly one third, when the increase in preceding seven years was between two to four percent per annum. As another consequence, consumers are also getting better choice and optimal prices.

Backdrop

Various policies/practices of state governments lead to anti-competitive outcomes and regulatory failures at the local level but remain unaddressed due to lack of awareness and vested interests. However, concerns arise when government policies themselves create favourable conditions for the formation of cartels. In such cases, the government ends up paying a high price for its own policies with a resultant loss of state revenue. One such example is the state excise policy of the Government of Rajasthan.

The dominance of a select group of traders in the liquor trade resulted in a suppression of bids with the government losing revenue in the process, while consumers were denied good choice and also optimal prices. Let us clarify that we are not supporting liquor consumption by this advocacy but because consumers do buy liquor legitimately, their rights have to be defended. And that of the state, which loses revenues and thus has less money for developmental expenditure.

Till 2004-05 the state of Rajasthan followed the 'Exclusive Privilege System' for liquor sales. As per this system the state was divided into regions for liquor vending contracts. Contracts under each region gave the licensee-contractor the exclusive right to trade in liquor in the specified area for one year. In this system a number of malpractices developed and competition was restricted to a few contractors who had sufficient money and muscle power. Over time, it encouraged cartelisation, resulting in high prices and concentration of business in the hands of few licensees. Bids were also suppressed and state excise revenue remained almost stable in spite of the increase in demand over time.

CUTS Initiative

CUTS International in a research report published in 2005 on the need for a competition policy for India¹ highlighted various anticompetitive outcomes and regulatory failures at the local level caused by state government policies. The report stressed that restrictive policy regimes are often characterized by entry restrictions which limit participation in the industry to a few participants. Smallness in numbers encouraged either monopoly or cartelisation and consequently industry outcomes which were inefficient and costly both to the consumer in terms of welfare and the government in terms of revenue losses.

¹ "Towards a Functional Competition Policy for India", Pradeep S Mehta (Ed), Academic Foundation and CUTS International, 2005

“In 2005-06, for Excise Policy changes in State of Rajasthan, the basic precincts are based on the findings of the CUTS report entitled “Towards A Functional Competition Policy for India”. This resulted in quantum jump close to 30% in excise revenue for the State. Against the backdrop of 2 to 4% per annum revenue growth for the immediate preceding 7 years, it is certainly a quantum leap. The suggestions in the report obviously point out to this direction. Policy deficiencies for a full fledged market play is essential to the designing of a policy regime”².

The report was presented to the Chief Minister of Rajasthan in a pre-budget consultation meeting in 2005. The state government was influenced by the Report and made changes in the excise policy with a view to break the liquor cartel. The government also established the Rajasthan State Beverages Corporation Ltd. (RSBCL) to take over the role of purchaser and supplier of liquor, dispensing with exploitative middle men. Furthermore, in a significant departure from its earlier policy of exclusive privilege system, the government introduced a two-tier system of licensing – licenses for wholesaler as well as retailer --- on the basis of a fixed license fee. The process of allotment was based on a lottery system. The new system provides liquor selling rights to a large number of vendors. The lottery system meant that the selected vendors were not necessarily known to each other. The large numbers selected meant that cartel formation and implementation had been rendered impracticable.

Tax Revenue and Excise Duties, Government of Rajasthan
(Rs in Crores)

Year	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Own tax revenue	7246	8414	9880	11608	12841 (RE)	14562 (BE)
Increase in %	15.88	16.12	17.42	17.49	10.62	13.40
Revenue from Excise	1163	1276	1522	1591	1750 (RE)	1910 (BE)
Increase in %	1.84	9.72	19.28	4.53	9.99	9.14

Source: Budget for different years, Government of Rajasthan.

These anti-cartel measures resulted in a significant jump in excise revenues from 2004-05 onwards. While there was a rise in revenue from excise by only Rs. 113 crores from 2003-04 to 2004-05 (see table), over the course of the next year excise revenues increased by as much as Rs. 246 crores, following these anti-cartel measures .

² Views expressed by Dr Shyam Agarwal, a senior bureaucrat in Government of India, having worked as Secretary in the Finance Deptt of Rajasthan, in a communication to CUTS

Other states

Rajasthan is not an exception, cartelisation has also been witnessed in other states like Andhra Pradesh, Tamil Nadu, Karnataka, M.P. and U.P. These states have also replaced the tender cum auction system by a system where liquor shops are allotted by a lottery system for a fixed licence fee. These states also saw quantum jump in the excise revenue to the state exchequer. Recently Haryana has also adopted the lottery system for allotment of shops from this year and the government is expecting a record revenue rise.

New excise policy evokes good response in Haryana

Haryana's new Excise Policy for 2008-09 has evoked overwhelming response for allotment of vends to be carried out through open draw of lots. As many as 76,000 application forms netting about Rs 38 crore have been sold compared to 53,000 last year. The new Excise Policy is geared towards breaking of monopoly of a liquor cartel and making available good quality liquor at an affordable price. Initiatives taken by the Government have made investments in liquor vends more profitable and government is hopeful to generate a record revenue of Rs 1440 crores.

Source: The Hindu, March 7th, 2008

Thus, gains have been considerable – more revenues for the government and more money for purposes of development, lower prices for consumers and therefore higher consumer welfare. The CUTS initiative shows how policy changes can be brought about to overcome the seemingly insurmountable problems posed by cartels.

3rd April, 2008