Taxing Agricultural Income

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From time to time, people both from within and outside the Government have talked about the necessity and feasibility of taxing agricultural income. There are no two opinions about the need for bringing this hitherto untaxed sector within the tax net and correct the distortions it is causing otherwise in the economy, as the agricultural sector remains a conduit for money laundering and concealment of black income. Committee after committees have recommended in favour of taxing large agricultural incomes but successive Governments have shied away from this for fear of losing potentially large vote banks. The paper argues that while the loss of potential vote banks remains a myth, the available data clearly prove that the small and marginal farmers would not be affected by any tax imposed on agricultural income.

(I)

In March 2016, in response to an RTI application filed in May 2015 by a retired Indian Revenue Service official, Mr. Vijay Sharma, the Income Tax Department revealed that agricultural income recorded an exponential increase from 2004 to 2013. The agricultural income earned by the 6.57 lakh assessees who filed returns in 2011, stood at nearly Rs. 2,000 lakh crore, which was over 20 times the country's gross domestic product of over Rs. 84 lakh crore in that year. During this period, the total area under cultivation and agricultural production had remained almost constant. In 2012, the agricultural income from these farmers exceeded six times the country's GDP. The data provided by the Department were mind-boggling:[1]

Table 1: Agricultural Income Tax Data Provided by Income Tax Department

Year	No. of individual taxpayers disclosing agricultural income	Average income per individual assesse (Rs)
2004	1	3.12 lakh
2005	1	1.2 lakh
2006	85	1.9 lakh
2007	78794	2.9 lakh
2008	205671	8.2 lakh
2009	245731	6.7 lakh
2010	425085	19.7 lakh
2011	**656944**	**30.4 crore**
2012	812426	83 crore
2013	914506	1.8 lakh

[1] The Hindu, "Farmers Grow Massive Incomes for Select Few", New Delhi, March 19, 2016.

Expectedly, the news rocked the Parliament which was then in session. The Government admitted that many prominent people were being investigated by the Income-Tax Department for masquerading taxable income as agricultural income. Mr Sharma again filed another RTI application seeking access to details of top 100 assessees in the past five years. However, the Income-Tax Department refused to provide any further data stating that the disclosure of personal information was prohibited under Section 8 1(J) of the RTI Act, unless there was an overriding public interest, and in its opinion there was none. Mr Sharma then approached the Patna High Court which prompted the CBDT to issue an internal letter to verify the genuineness of agricultural income exceeding Rs 1 crore made by taxpayers in their income tax returns pertaining to the period 2010-11 to 2012-13. There were 1080 such cases. Even at the threshold value, it meant declared agricultural income of at least Rs 1080 crore, which pointed to the strong possibility of laundering of black money in the garb of agricultural income.[2] The Income Tax Act, 1961, indeed prescribes for punishment of those misrepresenting their income.

The Income Tax Department then launched an investigation on those reporting farm incomes of more than Rs 1 crore a year. Official data pegged this number at 307 in the assessment year 2015-16, up from 180 in the assessment year 2007-08. Of the total of 2,746 such cases pertaining to the period 2006-07 to 2014-15 that the Department was probing, Bengaluru recorded the highest of 321 followed by Delhi with 275 and Kolkata with 239 cases from across the country. Other cities were not much behind, Mumbai reported 212 cases, Pune 192, Chennai 181 and Hyderabad 162. These assessees had filed their returns from these cities, and it raised eyebrows on the existence of all these cultivable land that produced such huge agricultural incomes. After the enforcement of land ceiling act in different states, the land holding had come down drastically. With the existing small holdings, it was well-nigh impossible for genuine farmers to extract crores of rupees of income from the land.[3]

Subsequently, however, in January 2017, the Income Tax Department, in a response submitted to the Standing Committee on Finance, attributed the reason for reporting such huge agricultural incomes in IT Returns primarily to data entry errors that erroneously extrapolated farmer incomes over 300 times the actual, on verification of 2,517 of the 2,746 cases by field authorities. It found that in 838 cases, the corrected agriculture income actually amounted to Rs 1,395 crore as against Rs 4,31,617 crore entered by assessing officers or taxpayers in I-T returns. Another 324 cases showed data entry errors in agriculture income or misclassification of income. It also detected some cases where non-genuine income was shown as agriculture income.[4] Even extrapolation of the reduced income for all the identified cases would account for more than Rs 4000 crore of agricultural income lying outside the tax net during these years.

It is to be mentioned that the authenticity of these data can be established only when these are audited by the CAG. The Economic Times erroneously reported that the CAG had initiated an audit of entities claiming tax exemption on agricultural income amid suggestions from some political parties and income tax authorities that a blanket exemption be done away with and tax be levied after a threshold. As per

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[2] Times of India, "As 'Crorepati' Farmers Mushroom, Tax Officials Go Digging for Evasion", March 13, 2016.
[3] Deccan Chronicle, "Time to Tax the Farms", April 2, 2016.
[4] Indian Express, New Delhi, "Income surge behind farm tax proposal was data entry error", January 26, 2017.

this report, the CAG had written to the Finance Ministry seeking details of entities which have declared agricultural income and the amount of tax exemption granted to them. Finance ministry data showed that nearly four lakh people declaring farm income had been granted exemption during 2013-14. Total agricultural income exempted from tax in 2013-14 was Rs 9,338 crore, going by the returns filed till November 2014.[5]

(II)

In June 2016, at the Rajasva Gyan Sangam, a two-day conference of tax administrators, suggestion was made by tax administrators to the Prime Minister "on the need to target farmers with non-agricultural income above a certain threshold, an idea that was pitched as a low-hanging fruit that could potentially bolster ongoing efforts to widen the country's taxpayer base."[6] It may be mentioned that of the 25 crore taxpaying households in the country, 15 crore households are designated as agriculturalists and the remaining 10 crore are non-agriculturalists, according to estimates produced at the conference.

Agriculture is exempt from income tax, under Section 2(1A) of the Income Tax Act which defines agricultural income as rent/revenue from land, income derived from this land through agriculture and income derived from buildings on that land. Further, unless there is specific taxing entry in the Union or State List under the Seventh Schedule to the Constitution, no tax can be imposed by the Union or the State. The tax on agricultural income is listed under the State List (Entry 46), and hence the Central Government cannot tax such income. As such, section 10 (1) of the Income Tax Act, a Central Act, excludes agricultural income from the computation of total income. This exemption would, however, be available only in cases where the income in question constitutes agricultural income within the meaning of Section 2(1A). Thus farmers who have no other sources of income are not required to file income-tax returns. It is only those farmers who derive income from sources other than agriculture who are required to file returns in which agricultural income exceeding Rs 5000, where the total income excluding net agricultural income exceeds Rs 2.5 lakh in a year, is to be reported for determination of their appropriate income slab for chargeability of tax. Tax on agricultural income is deducted from the total tax thus computed for the assessee.

Any decision to tax agricultural income by the Centre will require an amendment to the Constitution. For that a taxing entry need to be inserted in the Union List and appropriate changes should be made in Part XII of the Constitution, dealing with Finances of the Union and the States, and an appropriate arrangement of assignment of such taxes to the states should be worked out. Of course, states have to be involved in the process, as at present it is the states that can impose any tax on agricultural income. It will be foolish to e3xpect that states, already reeling under agitations by farmers, will take the plunge. For the Centre also, it will be a contentious issue, with various lobbying groups trying to protect the interests of the big

[5] Economic Times, "CAG lens on entities avoiding tax with 'farm income' claim", Oct 03, 2016. Actually the CAG could not initiate any audit for want of relevant data to be supplied by the Income Tax Department.
[6] Indian Express, New Delhi, "Income surge behind farm tax proposal was data entry error", January 26, 2017.

farmers. But the danger of avoiding or postponing this will spell doom for the economy and defeat the Government's earnest attempts to eliminate black money, as the untaxed agriculture sector will continue to absorb black money. It is also extremely unfair on the considerations of equity and simplification of tax administration.

Various Committees appointed by the Government in the past had proposed bringing the agricultural sector under the tax net. But agriculture being the holy cow of the economy, such proposals always met with the most vociferous disapproval from the strong farmers' lobbies and also from the Government on the supposed loss of vote banks. It is a no brainer that the vote bank consideration is based on pure myth. Even if the sector is brought under the tax net, it is only a miniscule percentage of the total number of agricultural workers who would be affected by such a tax. Even at present, hardly 2 percent of the assessees declare any agricultural income.

In December-2015, the Ministry of Agriculture released data pertaining to the Agriculture Census 2010-11.[7] The Census estimated the total number of operational holdings in the country at 138.35 million and total operated area at 159.59 million hectare. The average size of the holding was estimated as 1.15 hectare, which has been declining steadily trend since 1970-71. The Size Group wise percentage of number and area of operational holdings are as follows.

Table 2: Operational Holdings according to Size Groups in the Country

Sl.No	Size-Group	Percentage of number of operational holdings to total	Percentage of area operated to total
1	Marginal (below 1.00 ha.)	67.10	22.50
2	Small (1.00 - 2.00 ha.)	17.91	22.08
3	Semi-medium (2.00 - 4.00 ha.)	10.04	23.63
4	Medium (4.00 - 10.00 ha.)	4.25	21.20
5	Large (10.00 ha. & above)	0.70	10.59

Thus about 86 percent of the operational holdings are with the small and marginal farmers only, accounting for about 45 percent of the total area under cultivation. Only nine States, viz., Andhra Pradesh, Karnataka, Gujarat, Madhya Pradesh, Maharashtra, Rajasthan, Uttar Pradesh, Punjab, and West Bengal together account for about 78 per cent of the Gross Cropped Area estimated at 193.76 million hectares in the country. Out of the net total irrigated area of 64.57 million hectare, 48.16 percent is accounted by small and marginal holdings, 43.77 percent by semi-medium and medium holdings and 8.07 percent by large holdings.

Small and marginal farmers are not required to file any income tax returns under the present dispensation if agriculture is their only source of income, and even if the sector is brought under tax, in all likelihood, their income threshold will be below the tax limits. It is only the semi-medium, medium and large farmers

[7] Press Information Bureau Release, Government of India, Dec 09, 2015.

who account for only 14 percent of the operational holdings and 55 percent of total cultivable land who will be affected by any tax imposed on agricultural income.

The agricultural census showed that there were 138 million holding in India in 2010-11, of which 118 million were held by marginal and small farmers (93 million – marginal; 25 million – small). This figures can be related to the 2011 census figures, according to which there were 313 million main workers in the country, of which 176 million (56.6%) were engaged in 'Agricultural and allied activities'. The number of cultivators were 127 million. Thus roughly we can estimate that the number of small and marginal farmers were 118 million, the same as their number of holdings - they account for about 93 percent of the total farmers in the country. The remaining 7 percent farmers who share between them 55 of the total cultivable land would be the target group for the incidence of any future tax on agriculture. They certainly do not constitute a major vote bank, though their voice may be loud enough for any political party to yield to their demands for continued exemption from the tax net. Further, going by the past trends which indicate that the number of small and marginal farmers and their share in the total number of operational holdings have increased continuously since 1970-71, and which trend is likely to continue, the number of medium and large farmers are not likely to increase in the future so as ever constitute a major vote bank for any party. It is also to be remembered that agriculture sector contributes only 16 percent to our GDP in which the share of crops is around 10 percent only.[8] Its growth has been stagnant, the percentages of growth during 2012-13 to 2016-17 being 1.5, 4.2,-0.2, 1.2 and 4.1 respectively.

Table 3: Number of holdings, operated area and average size of holdings – All Social Groups

Sl. No.	Size Groups	1970-71	1976-77	1980-81	1985-86	1990-91	1995-96	2000-01	2005-06	2010-11
1	Marginal	36200	44523	50122	56147	63389	71179	75408	83694	92826
2	Small	13432	14728	16072	17922	20092	21643	22695	23930	24779
3	Semi-Medium	10681	11666	12455	13252	13923	14261	14021	14127	13896
4	Medium	7932	8212	8068	7916	7580	7092	6577	6375	5875
5	Large	2766	2440	2166	1918	1654	1404	1230	1096	973
	All Sizes	71011	81569	88883	97155	106637	115580	119931	129222	138348

Source: Agricultural Census, 2010-11, Table 1(a)

According to the Situation Assessment Survey (SAS) of Agricultural Households conducted in the 70th Round of NSSO Survey during January 2013 to December 2013, the average monthly income per agricultural households during the agricultural year July 2012 - June 2013 was estimated as Rs 6426.[9] The net receipt from farm business (cultivation and farming of animals) accounted for about 60 percent of the

[8] 2014-15 figures at 2011-12 constant prices: http://mospi.nic.in/publication/national-accounts-statistics-2016, accessed 30/07/2017.

[9] Income, Expenditure, Productive Assets and Indebtedness of Agricultural Households in India, NSS 70th Round, (January– December 2013), Government of India

average monthly income per agricultural household. The average monthly consumption expenditure per agricultural household was Rs 6223, while the income was Rs 6426. Only for the large farmers (>10 ha. of holding), the income was Rs 41,388 per month, above the income tax threshold. These data show that only the large famers who account for a miniscule 0.70 percent of the total operational holdings will only be liable to pay any income tax.

Table 4: Average monthly income and consumption expenditure (Rs) per agricultural household for each size class of land

Size class of land possessed (ha.)		wage income	net receipt from cultivation	Net receipt from animals	Total income	Net receipt from non-farm business	Total consumption expenditure	Net investment in productive asset	Agricultural households	
									Estimated (00)	Sample
(1)		(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
<0.01		2902	30	1181	447	4561	5108	55	23857	1900
0.01-0.40		2386	687	621	459	4152	5401	251	287381	6344
0.41-1.00		2011	2145	629	462	5247	6020	540	315008	7203
1.01-2.00		1728	4209	818	593	7348	6457	422	154810	9808
2.01-4.00		1657	7359	1161	554	10730	7786	746	83964	7413
4.01-10.00		2031	15243	1501	861	19637	10104	1975	33519	2019
10.00+		1311	35685	2622	1770	41388	14447	6987	3499	220
all size		**2071**	**3081**	**763**	**512**	**6426**	**6223**	**513**	**902039**	**34907**
Agrl. House-holds	Estimated (000)	47281	83178	64276	8990	90089	90204	58951	xx	xx
	sample	17876	31826	24942	3637	34848	34907	21143	xx	xx

Source: Table T1, Report of the NSSO 70th Round, Page 41.

Further, the survey shows that only the farmers who are semi-medium, medium or large in terms of their landholdings have substantial non-farm income above the income tax threshold; hence they are liable to file income tax returns showing their agricultural income. It was only in respect of these farmers that the Income Tax Department had instituted the inquiry referred to earlier and admitted data entry errors, yet to be verified. They are the ones who are presently enjoying the exemptions.

Table 5: Average expenses and receipts (Rs) from non-farm business per agricultural household during a period of 30 days by size class of land possessed

Size class of land possessed (ha.)	Expenses	Receipts	Net Receipts	No. per 000 agrl. households engaged in non-farming business	Agrl. households engaged in non-farming business	
					Estimated (00)	Sample
(1)	(2)	(3)	(4)	(5)	(6)	(7)
<0.01	5990	10135	4144	111	2653	191
0.01-0.40	9901	13809	3908	121	34887	890
0.40-1.00	15336	20805	5469	89	28039	738
1.01-2.00	16129	22163	6033	98	15205	973
2.01-4.00	28750	36078	7328	76	6357	650
4.01-10.00	41353	53396	12043	72	2419	164
10.00+	156325	174351	18026	98	344	31
All sizes	**15342**	**20632**	**5290**	**100**	**89903**	**3637**
Estimated No. of Agrl Households	87225	90716	89160	89903	xx	xx
Sample No. of Agrl. Households	3539	3663	3602	3637	xx	xx

Source: Table T12, *Ibid*.

Even the agro-companies growing crops are entitled to the same tax reliefs as individuals in respect of agricultural income, which defies all logic when we consider the scale of exemptions enjoyed by these companies. Let us take a few examples. More than four lakh taxpayers claimed exemption for agricultural income in the assessment year 2014-15. The biggest beneficiaries were Kaveri Seeds, which claimed Rs 186.63 crore as exemption, and multinational Monsanto India, which claimed Rs 94.40 crore as exemption, and theyh earned Rs 215.36 crore and Rs 138.74 crore profits respectively before tax.[10] It may be mentioned that Monsanto is the company that sells the genetically modified Bt-Cotton seeds in the country and earn huge profits therefrom. If this is not inequitable and irrational, one wonders what is. According to an estimate, taxing only the richest 4.1 percent agricultural households, as much as Rs 25000 crore could be collected as tax.[11]

[10] Deccan Chronicle, "Time to Tax the Farms", April 2, 2016.
[11] Awasthi, Rajul, "Break the Agricultural Black Money Shelter and Tax the Rich Farmer", https://thewire.in/131032/agricultural-income-tax-rich-farmer/, 02/05/2017, accessed 30/07/2017.

Table 6: Inequitable Exemptions[12]

Company	Exempt Agricultural Income (Rs crore)
Kaveri Seeds	186.6
Monsanto India	94.4
McLeod Russel India	73.1
MP Rajya Van Vikas Nigam	62.6
Vandana Farms and Resorts	61.1
Karnataka Forest Devt Corp	52.8
Ankur Seeds	27.6
Nath Bio-genes	27.4
Shiv Shakti Bio Tech	21.6
Ganga Kaveri Seeds	19.6

(III)

It is not that the Government did not get similar inputs earlier. Committee after Committees appointed by it had warned the Government about the pitfalls of non-taxing the agriculture sector. As early as 1972, the K N Raj Committee (Committee on the Taxation of Agricultural Wealth and Income) had recommended "A rational system of direct taxation of agriculture, (1) should take account of the differences in productivity of land depending upon the particular crops grown in a region, (2) its incidence should be uniform in different parts of the country, and (3) it should reflect changes in productivity and prices over a period of time." To build an element of progression into such a tax, it suggested introduction of a tax on agricultural holdings.[13]

The Tax reforms Committee (1991) headed by Raja Chelliah also examined this question and in its report stated that the absence of taxation of agricultural income had "left open a major loophole for tax avoidance and evasion and for the laundering of tax evaded money". It recommended that agricultural income above Rs 25000 accruing to non-agriculturists should be taxed "to promote equity and reduce the scope for evasion".[14]

Report of the Task Force on Direct Taxes (2002), Para 10.37, said: "With a view to encourage the States to tap the full potential of their taxing powers and to prevent laundering of non-agricultural income as agricultural income, the Task Force recommends (i) A tax rental arrangement should be designed whereby States should pass a resolution under Article 252 of the Constitution authorising the Central Government to impose income tax on agricultural income. The taxes collected by the Centre would however be assigned to the States; (ii) Tax from agricultural income for the purposes of allocation between States will

[12] Source: Rediff.com, "Not just rich farmers, even agri cos with Rs 215 cr profit pay no tax", May 16, 2016.
[13] Sreekantaradhya, B S, *Structure and Reform of Taxation in India*, Deep and Deep, New Delhi, 2000, 76.
[14] Para 79, TRC Report.

be the difference between the tax on total income (including agricultural income) and the tax on total income net of agricultural income; (iii) Where a taxpayer derives agricultural income from different States, the revenues attributable to a State will be in the ratio of the income derived from a particular State to the total agricultural income; (iv) A separate tax return form should be prescribed for taxpayers deriving income from agriculture."

The Central Board of Direct Taxes, in a white paper on black money released in May 2012, admitted that: "Giving credit to agricultural income for income-tax purposes without verification of claim allows an avenue for bringing black money into the financial system as agricultural income." Finally, the Tax Administration Reform Commission report by Parthasarathi Shome in 2014 stated unequivocally: "Agricultural income is exempt from taxation in spite of large agricultural holdings… a large number of rich farmers, who earn more than salaried employees in the cities, get away with paying no tax in view of the government's lack of will to consider an agricultural income-tax." It further said, "Agricultural income of non-agriculturists is being increasingly used as a conduit to avoid tax and for laundering funds, resulting in leakage to the tune of crores in revenue annually." The Government, however, has always remained overtly cautious and extra-sensitive to any proposal for taxing of agricultural income and all these reports were shelved.

In an article published recently, the Niti Aayog member, Mr Bibek Debroy has proposed that agricultural income should be taxed.[15] He pointed out that long before the present Income Tax Act of 1961 had come into effect, there was the Income Tax Act of 1860 which had taxed agricultural income till 1886 when it was abolished, presumably due to resentment against colonial rule. He had further pointed that acts for taxing agricultural income existed in many states of India, though mostly during colonial times, and such a tax could be, and should be, brought in again. The Government and the Niti Aayog promptly dissociated themselves from Mr Debroy's views due to the sensitivity of the issue and because of the hue and cry that followed. But it was not simply in the colonial times that such taxes were imposed. Even now it exists in the form of taxation of income from tea, coffee and rubber plantations. Under Rule 8 of the Income Tax Rules, 1962, income derived from the sale of tea grown and manufactured by the seller in India shall be computed as if it were income derived from business, and 40 per cent of such income shall be deemed to be income liable to tax. Similar provisions also exist for rubber and coffee plantations under rules 7A and 7B respectively.

Given that only 3.98 crore individuals filed returns in 2015-16 in a country of population exceeding 130 crore, and only 2.6% of population paid any taxes (39% in USA for comparison), and only 25 lakh paid tax at the highest rate - 90 percent of them from the organised sector where taxes are compulsorily deducted at source, if we are serious about expanding the tax base, this hitherto untaxed sector must be brought under the tax net. Of course given the highly informal nature of business in this sector, tax administration

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[15] Debroy, Bibek, "Twelve reasons why", Times of India, Delhi, May 3, 2017.

will pose serious problems initially, but that is expected of any new domain. It should be ensured that the tax liability rests only on the shoulders of the rich farmers while insulating the small and marginal farmers.

In 1925, the Indian Taxation Enquiry Committee had noted, “There is no historical or theoretical justification for the continued exemption from the income tax of income derived from agriculture. There are, however, administrative and political objections to the removal of the exemption at the present time.” Nine decades have since passed by, and nothing has changed. It is time to think of a beginning and correct the distortions which have long invaded and metastasized our body politic.