
CHAPTER-II

ECONOMICS OF PROHIBITION

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Section-I

2.1 A Brief Review of Prohibition Policy :

In India, any study pertaining to State excises always confronts the issues regarding prohibition policy.¹ The prohibition policy dates back to the period of British rule in India. Central Government has been given regulatory powers regarding production, distribution and consumption of opium, Indian hemp, charas, ganja and bhang etc. (Narcotics and narcotic drugs) by the provisions of the Indian Constitution.

The Government of India appointed the Indian Excise Committee in 1905-6 to look into the problem of alcoholic consumption and also to suggest a broad frame-work for prohibition policy. The consumption of both Indian and imported liquors was increasing in India. The Indian Excise Committee took into consideration the situation and recommended a prohibition policy comprising moderation with emphasis on minimising alcohol temptation and discouraging excess drinking. This was to be achieved by high taxes on liquor. But it was suggested that taxes should be moderate to avoid illicit production and consumption. The number of liquor shops were to be reduced and restrictions were to be introduced on location of shops and quality of liquor. As a principle, it was stated

that "all considerations of revenue must be absolutely subordinate."² This policy continued upto 1938 during which period in practice maximum of revenue and minimum of consumption became the effective policy.³

Prohibition policy in Maharashtra (then Bombay) was introduced in 1938 but the real thrust of the policy became evident in 1946 when the popular Government introduced a comprehensive prohibition policy effective from April 1947. The main features of the prohibition policy were as given under :

- i) 2 dry days in a week.
- ii) Reduction in the number of liquor shops.
- iii) Reduction in the strength of the liquors.
- iv) Limits on the possession of liquor.
- v) Increased excise taxation.
- vi) Introduction of the permit system.
- vii) Increased punishment for breaches of these provisions.

The policy had some success because it led both to a reduction in consumption and reduction in revenue from the excise taxation. On 6th April, 1960 complete prohibition was brought in. However, subsequently started an era of increasing doses of moderation in prohibition policy. In 1970s, the State virtually went almost fully wet.

State excises are one of the most productive sources of State Revenue. The relaxation in prohibition policy can be attributed mainly to revenue considerations and only secondarily to other non-economic aspects. It is really true that vicissitudes of prohibition policy are simply a phenomenon related to whims and fancies of changing political rules of the country.⁴ As the economics of prohibition is more relevant to this study, it is, discussed at a later stage.

2.2 What is Prohibition ?

Prohibition policy of a Government generally aims at restricting and, if possible, reducing production and/or consumption of various intoxicants, mainly alcoholic drinks and narcotics and narcotic drugs. The policy is mainly justified on grounds of dangers to social health and peace and individual health and economic security. On the basis of a cursory survey of the various experiments with prohibition tried in different States,⁵ we can enumerate various forms which the prohibition generally assumes.

- 1) Licensing and supervising the production of alcoholic drinks.
- 2) Restricting number of wet days in a week.
- 3) Restricting the places of alcohol production and/or consumption.
- 4) Reducing the alcohol content of the hard drinks.

- 5) Barring people below a certain age from the consumption and/or possession of hard drinks.
- 6) Introducing permit system for consumers of liquor.
- 7) Prohibiting consumption and/or sale of hard drinks on certain national or regional holidays.
- 8) Punishing illicit production and unauthorised consumption of hard drinks.
- 9) Totally banning production and/or consumption of alcoholic drinks.
- 10) Framing rules and regulations regarding production, bottling and distribution of hard drinks.
- 11) Increased excise taxation.

2.3 Need for Prohibition :

Prohibition is generally discussed in moral and non-economic terms. Prohibition policy is a moral issue rather than an economic problem. Infact according one economist economists in general are unanimous that "prohibition may or may not be good ethics but it is down-right bad economics."⁶

However, the need for prohibition policy can be supported more rationally on the following grounds.⁷

- 1) Prohibition releases purchasing power for better use.
- 2) Prohibition improves economic conditions of the workers. It also improves their health. It reduces absenteeism and irregularity of the workers, which in turn increases their productivity.

- 3) Children of the addicted people get proper education better food and adequate clothing.
- 4) Prohibition ensures the security of the savings of the poor family, particularly the ornaments and utensils of regular use in the family.
- 5) Prohibition may result in increased supplies of producer and consumer goods in the long run.
- 6) Prohibition may result in a significant reduction in indebtedness of the poor classes.
- 7) It is claimed that real losses due to unrestricted consumption of intoxicants are greater than financial losses. So fiscal loss should not form an argument against prohibition.
- 8) Prohibition improves family and social relations.
- 9) Revenue from excise taxes is inequitable, regressive and anti-social.
- 10) Excise taxation leads to undesirable effects on the distribution of national income.

2.4 Experience of Prohibition :

The question of prohibition is often discussed on sentimental grounds. People are either opposed to it, being a restriction on the private life of individuals, or they support it vehemently.⁸ Prohibition leads to illicit distillation in dry areas and smuggling out from wet areas. Complete prohibition cannot come by legislative acts. Whenever

the Government tries to implement prohibition illicit distillation, distribution and consumption of liquor increased automatically. This entails increased public expenditure on regulatory administrative machinery. This, at the same time, brings in corruption. On 1960-63 average, it has been estimated that total loss of revenue for the dry areas as a whole was Rs. 40 crores.⁹ Added to this was an amount of Rs. 5.4 crores on enforcement of prohibition. This was based on the assumption that 10% of expenditure on police, excise, jails and law courts is incurred for prohibition. In Maharashtra and Gujarat the combined revenue loss was of the order of Rs. 10.21 crores on 1960-63 average.

Even if there is prohibition in the entire State the State boundaries touch wet areas in other States. The gangs of smugglers exploit these borders to supply liquor to the dry areas. This has increased corruption amongst officials.

As Gibbon¹⁰ pointed out, "Reform must come from within, not from without. You cannot legislate for virtue. Death penalty for a dog's crooked tail will not make the tail straight". It is impossible to change habits suddenly. It is true that all the ex-addicts are not able to obtain supplies of liquor through smuggling or illicit distillation and many of them do not get an opportunity to consume liquor. But the sacrifice of revenue for such abstinence enforced on some people is not justifiable. Quite a large number are still

able to satisfy their craving for liquor. Even those who have no contact with the smugglers or illicit distillers tend to avail of the opportunity as soon as they get it.

2.5 Effects of Prohibition :

The most outstanding and undisputed beneficial effect of prohibition is on the social life of the people.¹¹ Different people have different habits. Cigarettes, tobacco, bidi, wine, beer, ganja, bhang etc. are the things to which people get habituated. The consumption of such intoxicants, mild and hard, generally tends to increase with increasing income but happens to be price-inelastic. In case of those who are addicted, expenditure on intoxicants does not decrease and as a result, expenditure on more essential items is reduced, more so at lower levels of income. It is on this background that following effects of prohibition have to be understood.

The homes of addicts present pitiable scenes. The family members generally suffer both physical and mental agonies, the wife of the addict being the worst sufferer. Children of a family require peace and love from and between the spouses, for healthy physical and mental growth. Due to negligence and careless attitude of the addicts, their children do not get proper education, adequate food and appropriate clothes. It is not only the members of the family but neighbours who also are the victims of the misbehaviour of the

addicts. If prohibition does really succeed in weaning away the addicts from their addictions, or atleast bringing in moderation, all the above mentioned pernicious effects can be avoided completely or their frequency and intensity reduced significantly.

2.6 Reasons for Failure :

However, failure, more or less is the fate of prohibition. The reasons for the failure of prohibition policy are as follow ;¹²

- 1) Prohibition leads to a serious loss of public revenue.
- 2) It may create problems of unemployment and rehabilitation of those who are engaged in the production and distribution of intoxicants.
- 3) Prohibition always leads to illicit production, distribution and consumption of liquors resulting in deathly hazards to the people and shameless corruption.
- 4) It increases expenditure on the administration of police, judiciary and prisons.
- 5) It can also be argued that relaxation resulting from moderate drinking may increase efficiency.
- 6) It leads to a loss of markets for the farmers.
- 7) The usual arguments for prohibition are fallacious.

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2.7 Economic Analysis of Prohibition :

Prohibition, eventhough mainly a social and behavioural problem, has certain economic implications. It is these economic aspects which generally compel the Government eventually to moderate or scrap prohibition. The important objective of prohibition is to regulate and if possible, even to fully stop the consumption of alcoholic liquors and intoxicating drugs. However, when it is realised that direct prohibition generally is doomed to failure apart from direct controls, the Government increases the rates of excise duty. Prohibition by way of excise duties helps the Government in attaining simultaneously the objectives of getting much needed revenue and of reducing to a certain extent, the production and/or consumption of alcoholic drinks and other intoxicants. Excise duties constitute one of the more important sources of revenue of the States in India. This revenue can become an important element of financing increasing expenditure on developmental programmes. A judicious use of excise duties in respect of alcoholic drinks and intoxicants coupled with favourable tax treatment of socially more important economic activities may help in reallocating resources in a more efficient and socially desirable manner.

2.8 Revenue Consideration :

The main justification for scrapping prohibition stems from revenue point of view. Prohibition leads to a significant revenue loss to the Government. The reasons for this revenue loss are :

- 1) Prohibition does not lead to a reduction in the expenditure on liquor consumption. With prohibition in force, illicit production emerges and unauthorised consumption becomes rampant.
- 2) Eventhough the prohibition can divert expenditure, it will be mainly on food items. Food items are generally exempt from sales taxation. In this case the Government loses the revenue.
- 3) Prohibition cannot be supported by increased rates of sales taxation of other commodities. These rates are basically very low compared to rates of excise duties.
- 4) Demand for liquors and other intoxicants, as already pointed out, is both price-inelastic and income elastic positively. As such it becomes an appropriate base for taxation.
- 5) Luxury consumption and sales tax revenue from such expenditure depends mainly on increasing income and not on prohibition.

Thus, the hypothesis that due to prohibition financial loss will be more than compensated by alternative taxes, is not proved. There is a possibility that net gains will be negative atleast in economic terms. The fiscal measures like excise taxation at high levels will not serve the objective of prohibition, but will in fact serve the objective of revenue.

In view of the fact that any attempt at prohibition invariably results in a wide growth of illicit production,¹³ it is necessary that prohibition policy uses mainly non-fiscal methods. Education and propaganda are the main alternatives. But this will be a time consuming process. In the meanwhile it is pragmatic to collect revenue from those who go in for drinking any way.

2.9 Costs of Prohibition :

Apart from considerations of revenue loss, prohibition also becomes a burden on the Government due to prohibitive costs of enforcement. There are other economic and social costs which make scrapping of prohibition socially necessary. The costs of prohibition can be listed as under :

- 1) Increasing expenditure on the administration of police, judiciary and prisons.
- 2) It leads to wide spread corruption in the police and other Government agencies. This becomes a source of black money. This may have a bearing on the price level also.

- 3) Prohibition leads to illicit distribution. The alcoholic drinks of this source prove to be hazardous to the health of the people; mainly from the weaker sections of the population.
- 4) Once prohibition leads to illicit production and consumption of alcoholic drinks etc., it creates corruption. This may induce similar patterns of behaviour in other fields of economic activity, thus causing a further reduction in revenue and a general degeneration of the society.

2.10 Does Economic Analysis support Prohibition Policy ?

The economic analysis does not support prohibition policy, because -

- 1) it increases the administrative expenditures of the Government.
- 2) It reduces revenue of the Government.
- 3) Price elasticity of demand for excisable goods is very low and income elasticity is high.
- 4) It has not been proved convincingly that prohibition leads to diversion of purchasing power to more desirable goods.
- 5) Moreover, the social costs of the prohibition are very high.

R E F E R E N C E S

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