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Economic Survey & Government Plan Programme & Policies

for Civil Services Preliminary (CSAT) & Main Examination 2013

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- Important points are highlighted for quick revision
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Chapter 3

PUBLIC FINANCE

CONTENTS OF THE CHAPTER

INTRODUCTION

The fiscal outcome of the Central government in 2012-13 so far indicates significant improvement over 2011-12. The fiscal outcome in 2011-12 was affected by macroeconomic developments of growth slowdown, high global crude oil prices, and sluggish financial market conditions for effecting the budgeted disinvestment programme. These developments continued through the first half of the current year. The government then pushed harder for reforms. An initial step was to set up the Kelkar Committee. Following its recommendations, the government unveiled a revised fiscal consolidation roadmap. The fiscal position of states has continued to progress with fiscal deficit budgeted at 2.1 per cent of gross domestic product (GDP). Staying on the indicated fiscal consolidation path is critical to sustaining the desirable macroeconomic outcomes not only in terms of higher growth in real GDP and lower inflation, but also in easing the financing of the widening current account deficit (CAD), for which India's sovereign credit rating is important. Widening of the tax base and prioritization of expenditure are key factors in effecting the desired reduction in the Central government's fiscal deficit over the medium term, and in reducing the key risks to fiscal marksmanship (the difference between actual outcomes and budgetary estimates as a proportion of GDP).

Latest available data indicate nascent signs of a turnaround in the macroeconomic environment. The stress witnessed in 2011-12 continued through the first half of the current year delaying the recovery process. This was manifest with growth continuing to be below 5.5 per cent, inflation moderating somewhat but continuing to be above 7 per cent, and only a brief moderation in the global crude oil prices. A pickup in financial markets, which gained steam as reforms were rolled out, the moderation in WPI inflation to 6.6 per cent in January 2013 and a bottoming out of industrial slowdown are broad indications of the turnaround. Indicating the trends in fiscal outcome in the first half of the current fiscal, the Mid-Year Economic Analysis 2012-13, pointed out that the mid-year threshold benchmarks in terms of fiscal responsibility and budget management (FRBM) rules had not been met and with the corrective measures proposed, fiscal deficit was likely to exceed budget estimates by 0.2 percentage point. The seriousness of the challenge can be seen by comparing the assumptions that were made when the Budget was presented with the actual outcome so far.

The continued high levels of global crude oil prices and domestic pressures that were manifest in persistent inflation, which necessitated keeping interest rates high, had their impact on aggregate demand (both consumption and investment). The Budget for 2012-13 attributed India's growth slowdown in 2011-12 to weak industrial growth and underscored the recovery in core sectors at that time which was seen as a sign of gradual recovery. Real GDP thus was projected to grow at around 7.6 per cent with inflation moderating on year-on-year basis.

Recognizing the need for funding the higher levels of outgo on subsidies on account of elevated levels of global crude oil prices, higher provision was made for the same in Budget 2012-13. However, as part of the fiscal consolidation process, the Budget also announced the intent to restrict expenditure on central subsidies to under 2 per cent of GDP.

The second important feature is the introduction of the provision for 'Medium Term Expenditure Framework Statement' in the FRBM Act. This medium-term framework provides for rolling targets for expenditure, imparting greater certainty, and encourages prioritization of expenditure. Together with the measures proposed to raise the tax-GDP ratio, the expenditure reforms are expected to yield better fiscal marksmanship, thereby mitigating key fiscal risks.

Fiscal outcome is also affected by the underlying assumption regarding the nominal GDP. Declining fiscal deficit as a ratio of GDP may be an outcome of either declining growth of fiscal deficit over time or increasing growth of GDP over time or both. In the post-FRBM period prior to 2008-9, the declining fiscal deficit to GDP ratio was mainly an outcome of a decline in the growth of the fiscal deficit. In the year 2011-12 a sudden overshooting of the growth of the fiscal deficit as compared to growth in GDP over the previous year caused a higher fiscal deficit to GDP ratio.

NON-DEBT RECEIPTS

At the time of the annual budget, fiscal adjustment is essentially about the assumptions regarding the growth in total non-debt receipts and total expenditure of the Central government. The Budget for 2012-13 envisaged a growth of 22.7 per cent in non-debt receipts (revenue receipts plus nondebt capital receipts) and in total expenditure of 13.1 per cent over 2011-12 (revised estimates [RE]). Revenue receipts were estimated at Rs.9,35,685 crore in BE 2012-13, which comprised net tax revenue of Rs.7,71,071 crore and non-tax revenue of Rs.1,64,614 crore. Together with recoveries of loans of Rs.11,650 crore and disinvestment receipts of Rs.30,000 crore, the Budget for 2012-13 placed non debt receipts for the year at Rs.9,77,335 crore.

Tax buoyancy is a measure of the responsiveness of tax receipts with respect to GDP or National Income. A tax is buoyant when revenues increase by more than 1 per cent for a 1 per cent increase in GDP. In the post FRBM period, both direct and indirect taxes remained buoyant except in the crisis years (2008-9 and 2009-10) and 2011-12. During 2011-12, both direct and indirect tax revenues grew at a lower rate than what the BE envisaged as well as the 2010-11 growth rate mainly because of economic slowdown, weak market sentiment, slow investment growth, global uncertainty, and persistent high inflation. This led to a sharp fall in tax buoyancy in 2011-12. The decline has been more in corporate taxes than personal income taxes. During this period, direct tax buoyancy (ratio of direct taxes growth to nominal GDP growth) also declined and has been less than 1. This may be on account of lower profitability of corporates considering higher inflation.

DIRECT TAXES

There has been a compositional change in gross tax revenues since 2007-8. As a proportion of GDP, direct taxes accounted for 5.5 per cent in 2011-12, well below the peak of 5.9 per cent in 2007-8. The Budget for 2012-13 envisaged a growth of 13.9 per cent in direct taxes over 2011-12 (RE). Continuing with the policy of moderation of tax rates, the Budget has further broadened the slabs for individual taxpayers. The exemption limit for individual taxpayers below the age of 60 years has been enhanced from Rs.1,80,000 to Rs.2 lakh. The income slab for 20 per cent tax rate has been broadened for all individual taxpayers irrespective of their age and will now be applicable to total income between Rs.5 lakh and Rs.10 lakh instead of the earlier slab of Rs.5 lakh and Rs.8 lakh. The tax rate of 30 per cent will now be applicable to total income exceeding Rs.10 lakh. Securities transaction tax on certain transactions in specified securities has been reduced from the existing 0.125 per cent to 0.1 per cent.

The two specific measures aimed at expanding the direct tax base in the Budget for 2012-13 were the introduction of the provisions of GAAR in the Income Tax Act and extending the provisions of alternate minimum tax (AMT) to all non-company assessees. In an environment of moderate rates of tax, it is necessary that the correct tax base be subject to tax in the face of aggressive tax planning and use of opaque low tax jurisdictions for residence as well as for sourcing capital. The need for making statutory provisions for codifying the doctrine of 'substance over form' has been realized by introducing the chapter on GAAR. However, in view of the apprehensions raised about the Rules and the recommendations of the Shome Committee, the provisions have been deferred.

Sector-Specific Proposals in Central Excise

1. **CEMENT:** The excise duty structure on cement manufactured and cleared in packaged form rationalized. The graded retail selling price (RSP) slabs for the purpose of charging of duty on cement manufactured and cleared in packaged form done away with. The duty rates on cement and cement clinkers revised as follows:

Description	Revised rate of duty
1. Cement manufactured and cleared in packaged form:-	
(a) from mini cement plants	6% + Rs.120 per tonne
(b) from other than mini cement plants	12% + Rs.120 per tonne
2. Cement cleared other than in packaged form.	12%
3. Cement clinker	12%

Cement also notified under section 4A, that is RSP-based assessment with an abatement of 30 per cent on RSP.

2. **PRECIOUS METALS:** (i) Excise duty on gold jewellery sold from export-oriented units (EOUs) into domestic tariff area (DTA) increased from 5 per cent to 10 per cent; (ii) Excise duty on refined gold increased from 1.5 per cent to 3 per cent; (iii) Excise duty on gold produced from copper smelting increased from 2 per cent to 3 per cent; (iv) Excise duty on silver produced from copper smelting reduced from 6 per cent to 4 per cent; (v) Gold coins of 99.5 per cent and above purity and silver coins of 99.9 per cent and above purity manufactured out of duty paid gold fully exempted from excise duty; (vi) Articles of gold /silver jewellery exempted from excise duty.
3. **MASS CONSUMPTION ITEMS:** (i) Refills and inks used for the manufacture of writing instruments of value not exceeding Rs.200 per piece fully exempted from excise duty subject to actual user condition;(ii) Exemption limit on footwear enhanced from Rs.250 per pair to Rs.500 per pair. Footwear above Rs.500 per pair to attract excise duty of 12 per cent; (iii) Excise duty on iodine reduced from 10 per cent to 6 per cent.
4. **ENVIRONMENT-FRIENDLY GOODS:** (i) Excise duty reduced from 10 per cent to 6 per cent on battery packs supplied to manufacturers of electric vehicles for use as spares and original equipment manufacturers subject to enduse condition; (ii) Excise duty reduced from 10 per cent to 6 per cent on specific parts of hybrid vehicles supplied to manufacturers of hybrid vehicles subject to end-use condition; (iii) Excise duty on LED lamps reduced to 6 per cent.
5. **PETROLEUM:** The rate of cess leviable on indigenous petroleum crude oil under the Oil Industry (Development) Act 1974 increased from Rs.2500 per metric tonne to Rs.4500 per metric tonne.
6. **TEXTILES:** For the purpose of charging excise duty on ready-made garments bearing a brand name or sold under a brand name, the level of abatement from RSP increased from 55 per cent to 70 per cent.
7. **MISCELLANEOUS:** (i) Full exemption from excise duty provided to food preparations containing fruits and vegetables falling under Chapter 20, which are prepared in a hotel, restaurant, or retail outlet, whether or not such food is consumed in such hotels/restaurants/retail outlets; (ii) The composite rate applicable to automobile chassis converted into an ad valorem rate and fixed at 14 per cent for diesel driven buses, lorries, and trucks; (iii) Excise duty on parts of mobile phones, other than those cleared to a manufacturer of mobile phones, reduced from 10 per cent to 2 per cent, provided no Cenvat credit is taken; (iv) Excise duty reduced from 10 per cent to 6 per cent on matches manufactured by semi-mechanized units and processed food products of soy; (v) Full exemption from excise duty withdrawn from mega/ultra mega power projects except 113 specified projects.

INDIRECT TAXES

The Budget for 2012-13 estimated revenue from indirect taxes to grow by 26.7 per cent over 2011-12 (RE) on the strength of assumed economic recovery. The Budget for 2012-13 also made the following other changes: raised the concessional rate of excise duty on non-petroleum products from 5 per cent to 6 per cent; increased the lower rate on non-petroleum products without Cenvat Credit from 1 per cent to 2 per cent with the exception of coal and fertilizers; enhanced the rate of excise duty from 22 per cent to 24 per cent and from '22 per cent+ Rs.15,000 per vehicle' to 27 per cent on certain categories of automobiles; increased the rates of specific excise duty on cigarettes (both filter and non-filter) of length exceeding 65mm; raised the excise duty on cigars, cheroots, and cigarillos to '12 per cent or Rs.1,370 per thousand, whichever is higher'; increased the basic excise duty on handrolled bidis from Rs.8 to Rs.10 per thousand and on machine-rolled bidis from Rs.19 to Rs.21 per thousand.

Sector-specific changes in Customs:

1. **AGRICULTURE/AGRO PROCESSING/ PLANTATION SECTOR:** (i) Basic customs duty on sugarcane planter, root or tuber crop-harvesting machine and rotary tiller and weeder and parts and components for their manufacture reduced from 7.5 per cent to 2.5 per cent; (ii) At present, project import status available for installation of mechanized handling systems and pallet racking systems in mandis or warehouses for foodgrains and sugar, with concessional rate of basic customs duty of 5 per cent. Such systems also exempt from additional duty of customs (CVD) and special additional duty of customs (SAD). The same dispensation extended to such systems installed in mandis or warehouses for horticultural produce; (iii) Project import status granted to greenhouses set up for protected cultivation of horticulture and floriculture produce with concessional basic customs duty of 5 per cent; (iv) Basic customs duty reduced from 10 per cent/7.5 per cent to 5 per cent (until March 2014) on specified coffee plantation and processing machinery; (v) Basic customs duty reduced from 10 per cent to 5 per cent (until March 2014) on coffee brewing and vending machines (commercial type). Basic customs duty also reduced to 2.5 per cent on parts required for manufacture of such coffee- brewing and -vending machines; (vi) Basic customs duty reduced on specified soluble fertilizers and liquid fertilizers, other than urea, from 7.5 per cent to 5 per cent and from 5 per cent to 2.5 per cent respectively.
2. **AUTOMOBILES:** Basic customs duty on completely built units (CBUs) of large cars/ MUVs/ SUVs permitted for import without type approval (value exceeding US $ 40,000 and engine capacity exceeding 3000 cc for petrol and 2500 cc for diesel) increased from 60 per cent to 75 per cent.
3. **METALS:** (i) Basic customs duty on coating material for manufacture of electrical steel reduced from 10 per cent to 5 per cent subject to actual user condition; (ii) Basic customs duty on ammonium meta-vanadate used in the manufacture of ferro-vanadium reduced from 7.5 per cent to 2.5 per cent; (iii) Nickel oxide/ hydroxide and nickel ore/ concentrate fully exempted from basic customs duty; (iv) Exemption from SAD currently available to CRGO steel restricted to prime quality of such steel; (v) Basic customs duty on flat rolled products (HR and CR) of non-alloy steel increased from 5 per cent to 7.5 per cent.
4. **PRECIOUS METALS:** (i) Basic customs duty on standard gold bars and platinum increased from 2 per cent to 4 per cent; (ii) Basic customs duty on non-standard gold increased from 5 per cent to 10 per cent; (iii) Additional customs duty on gold ore/concentrate and bars for refining increased from 1 per cent to 2 per cent; (iv) Basic customs duty of 2 per cent imposed on cut and polished coloured gemstones.
5. **CAPITAL GOODS/INFRASTRUCTURE:** (i) Basic customs duty on capital goods, plant, and equipment imported for setting up or substantial expansion of iron ore pellet plants or iron ore beneficiation plants reduced from 7.5 per cent to 2.5 per cent; (ii) Full exemption from basic

customs duty until March 2015 provided for initial setting up and substantial expansion of fertilizer projects; (iii) Steam coal fully exempted from basic customs duty. CVD reduced from 5 per cent to 1 per cent on such coal (valid up to 31.3.2014); (iv) Natural gas/liquefied natural gas imported for power generation by a power generation company fully exempted from basic customs duty; (v) Full exemption from basic customs duty provided to uranium concentrate, sintered natural uranium dioxide, sintered uranium dioxide pellets for generation of nuclear power; (vi) Full exemption from basic customs duty, CVD and SAD extended to equipment imported for road construction projects awarded by metropolitan development authorities; (vii) Full exemption from basic customs duty and CVD presently available to tunnel boring machines and parts for hydel and road projects extended to all infrastructure projects without end-use condition; (viii) Full exemption from basic customs duty and CVD extended to tunnel excavation and specified lining equipment also; (ix) Full exemption from basic customs duty extended to coalmining projects; (x) Basic customs duty for machinery and instruments for surveying and prospecting reduced and unified at 2.5 per cent; (xi) Basic customs duty on railway safety (train protection and warning system) equipment and railway track-laying machines reduced from 10 per cent to 7.5 per cent.

6. **AIRCRAFT AND SHIPS:** (i) Full exemption from basic customs duty and CVD provided to new and retreaded aircraft tyres; (ii) Full exemption from basic customs duty and CVD extended to parts of aircraft and testing equipment for maintenance and repair of aircraft imported by maintenance, repair, and overhaul (MRO) units; (iii) Customs duties on foreign-going vessels on conversion for coastal trade now to be charged on proportionate basis depending on the period for which they operate as coastal vessels in India; (iv) Full exemption from SAD extended to import of dredgers.
7. **ENVIRONMENT PROTECTION:** (i) Equipment for setting up of solar projects fully exempted from SAD; (ii) Concessional rate of 5 per cent basic customs duty extended to raw materials for the manufacture of intermediates, parts, and sub-parts of blades for rotors for wind energy generators; (iii) Full exemption from basic customs duty extended to tri band phosphor for use in the manufacture of compact fluorescent lamps; (iv) Full exemption from basic customs duty and SAD along with 6 per cent CVD available to specified parts for the manufacture of hybrid vehicles extended to some additional parts; (v) The customs duty regime of 6 per cent CVD and nil SAD extended to lithium ion batteries for the manufacture of battery packs for supply to electric or hybrid vehicle manufacturers.
8. **HEALTH/NUTRITION:** (i) Basic customs duty reduced from 5 per cent to 2.5 per cent on iodine; (ii) Basic customs duty reduced on isolated soya protein and soya protein concentrate from 15 per cent and 30 per cent respectively to 10 per cent; (iii) Basic customs duty reduced from 10 per cent to 5 per cent on probiotics; (iv) Customs duty on six specified lifesaving drugs/vaccines and their bulk drugs reduced from 10 per cent to 5 per cent with nil CVD; (v) A concessional import duty regime of 2.5 per cent basic customs duty with 6 per cent CVD/excise duty and nil SAD prescribed for specified raw materials for the manufacture of syringes, needles, catheters, cannulas subject to actual user condition. (vi) A concessional import duty regime of 2.5 per cent basic customs duty with 6 per cent CVD and nil SAD extended to parts and components for the manufacture of blood pressure monitors and blood glucose monitoring systems (glucometers); (vii) Full exemption from basic customs duty and CVD extended to steel tube and wire, cobalt chromium tube, Hayness Alloy-25, and polypropylene mesh for the manufacture of coronary stents/coronary stent systems and artificial heart valves subject to actual user condition.
9. **TEXTILES:** (i) Basic customs duty on new shuttle-less looms, along with parts and components for their manufacture reduced from

5 per cent to nil; (ii) Basic customs duty on new automatic silk-reeling and -processing machinery and raw silk testing equipment reduced from 5 per cent to nil; (iii) The concessional rate of basic customs duty of 5 per cent restricted only to new textiles machinery; (iv) Basic customs duty on wool waste and wool tops reduced from 10 per cent and 15 per cent respectively to 5 per cent; (v) Basic customs duty on titanium dioxide reduced from 10 per cent to 7.5 per cent; (vi) Full exemption from basic customs duty extended to Aramid yarn and fabric when used in the manufacture of bulletproof helmets for supply to defence and police.

10. **ELECTRONICS/ HARDWARE:** (i) Full exemption from basic customs duty provided to LCD and LED TV panels of 19 inches and above; (ii) LEDs required for the manufacture of LED lamps exempted from SAD; (iii) The scope of full exemption from basic customs duty, CVD, and SAD extended to parts of memory cards until March 2013; (iv) Full exemption from basic customs duty currently available to copper, brass, phosphor bronze strips, and similar items imported for the manufacture of connectors withdrawn; (v) Full exemption from basic customs duty currently available to poly-laminated aluminum tape and poly-laminated steel tape if imported for the manufacture of cables and conductors for telecom use withdrawn.
11. **EXPORT PROMOTION:** (i) Basic customs duty reduced from 10 per cent to 5 per cent on marine seawater pumps with fibre impellers and automatic fish/prawn feeders for aquaculture; (ii) Basic customs duty on artemia reduced from 30 per cent to 5 per cent.
12. **PAPER:** Waste paper fully exempted from basic customs duty.
13. **SAD:** Brass scrap and timber logs fully exempted from SAD.
14. **MISCELLANEOUS:** (i) A basic customs duty of 10 per cent imposed on digital still cameras of certain specifications; (ii) Basic customs duty on boric acid increased from 5 per cent to 7.5 per cent; (iii) Basic customs duty on boiler quality tubes and pipes for the manufacture of boilers reduced from 10 per cent to 7.5 per cent subject to end-use condition; (iv) A concessional customs duty of 5 per cent basic customs duty + 6 per cent CVD+ nil SAD prescribed for imports of hydrophilic non-woven, hydrophobic non-woven, and super absorbent polymer for manufacture of adult diapers subject to actual user condition; (v) Full exemption from customs duty withdrawn from mega/ultra mega power projects except 113 specified projects.

SERVICE TAX

In 2011-12, growth in service tax revenue was 37.4 per cent amounting to Rs.97,579 crore, which indicated that service tax has been emerging as an important source of revenue. Budget 2012-13 envisaged a growth of 30.5 per cent in the revenue from service tax vis-à-vis 2011-12 (RE). This was based on the increase in the rate from the existing 10 per cent to 12 per cent and a change in the tax base. As against the usual practice of expanding the list of services, the Budget for 2012-13 introduced a 'negative list' approach effective 1 July 2012. For operationalizing the negative list approach, a number of changes have been made in Chapter V of the Finance Act 1994 (when service tax was initially introduced). Service of transportation of passengers with or without accompanied belongings by railways in first class or an air conditioned coach and services by way of transportation of goods by railways has been subjected to service tax effective October 1, 2012. Following the revision in the rate of service tax, changes have also been made in specific and compounding rates of tax for services in relation to purchase and sale of foreign currency including money changing; promotion, marketing, organizing, or in any manner assisting in organizing lottery; and reversal of Cenvat credit under rule 6(3)(i).

A number of amendments in the Finance Act 1994 and changes in the rules governing the levy of service tax have been made. These include: the Place of Provision of Service Rules 2012; new reverse charge mechanism; Cenvat Credit Rules 2004; Service Tax Rules 1994; and Point of Taxation Rules 2011.

TAX EXPENDITURE

In the Receipts Budget for 2012-13, tax foregone on account of exemptions under corporate income tax for 2010-11 and 2011-12 was estimated at Rs.57,912 crore and Rs.51,292 crore respectively net of MAT. In the case of corporate taxpayers, deduction on account of accelerated depreciation, deduction for export profits of export-oriented units located in special economic zones (SEZs) and profits of businesses in the power and telecom sectors were some of the major incentives. The absolute amount of deductions has decreased as a result of phasing out of profit-linked deductions. Further, the levy of MAT has led to a higher effective rate of taxation in the case of corporates from 20.55 per cent for 2006-7 to 24.1 per cent for financial year 2010-11. Tax forgone on account of exemptions under personal income tax for individual taxpayers was estimated at Rs.30,653 crore and Rs.35,698 crore respectively in 2010-11 and 2011-12. The bulk of the revenue foregone under personal income tax was on account of the exemptions given for certain investments and payments under section 80 C of the Income Tax Act.

Nevertheless, there is merit in limiting the exemptions or their grandfathering on a case-by-case basis so as to realize fuller tax potential through a wider tax base.

NON-TAX REVENUE

Non-tax revenues grew at a compound annual rate of 7.6 per cent in the 10 years ending 2009-10. The spurt in 2010-11 owed to higher-than-budgeted realization from the proceeds of auction of telecom 3G/broadband wireless access spectrum. As against the estimated revenue of Rs.1,25,435 crore in 2011-12 (BE), the realization fell marginally short at Rs.1,24,307 crore notwithstanding the fact that the auctions of telecom spectrum and phase III FM Radio which were to bring in Rs.14,600 crore could not take place. Budget 2012-13 estimated a growth of 32.0 per cent over 2011-12 (RE) in non-tax revenue mainly on account of estimated receipts of Rs.40,000 crore from the telecom spectrum auction. As the 2G telecom spectrum auction elicited lukewarm response on account of the high reserve price in the current year, the government has revised the reserve price downwards. As such, the proceeds from this component are as yet an important risk to the actual fiscal outcome for 2012-13. The other main component is dividends and profits, which have also in the past exhibited sluggish growth.

NON-DEBT CAPITAL RECEIPTS

Recoveries of loans and disinvestment are the two key receipts of the non-debt capital variety. As against Rs.16,897 crore in 2011-12 (provisional actuals), Budget 2012-13 has placed recoveries of loans at Rs.11,650 crore this year. The 12th Finance Commission's recommendation against loan intermediation from the centre to states coupled with the fact that such recoveries of loan have become a minor source in the receipts side has resulted in disinvestment assuming greater importance in comparison. As against Rs.40,000 crore budgeted under disinvestment in 2011-12, actual receipts were Rs.15,622 crore on account of the subdued financial market conditions. The Budget for 2012-13 has estimated that Rs.30,000 crore would accrue in 2012- 13. In April-December 2012, receipts under this head were Rs.8,178 crore. The government has taken several steps to expedite the process of disinvestment.

Apart from these, non-tax revenue in April-December 2012 is placed at Rs.86,380 crore, which is 52.5 per cent of BE, well below the last five years' average. This outcome is because of the lower realization from auction of 2G spectrum thus far. In non-debt capital receipts, there is significant shortfall as of April-December 2012 on account of disinvestment receipts, as only Rs.8,178 crore of the budgeted amount of Rs.30,000 crore has been realized. Thus the overall outcome in terms of non-debt receipts was Rs.5,86,424 crore in April-December 2012, which is 60.0 per cent of the BE, indicating the stiff challenge in the fourth quarter of the current fiscal for better marksmanship.

SUBSIDIES

As indicated earlier, while the Budget for 2011-12 had estimated total expenditure to be contained at 14.0 per cent of GDP, there was an overshooting on account of the high global oil prices and the insufficient pass through to domestic oil and fertilizer prices. The overshooting of expenditure on subsidies was also because of the accounting changes which placed all subsidies 'above the line'. The Budget for 2012-13 estimated growth in total expenditure at 13.1 per cent over 2011-12 (RE) and sought to restrict expenditure on subsidies to 2 per cent of GDP. As against a provision of Rs.23,640 crore in 2011-12 for oil subsidies, the Budget for 2012-13 provisioned an amount of Rs.43,580 crore assuming a certain level of global crude oil price. It must be noted that oil subsidies are paid to the oil marketing companies (OMC) on a calendar-year basis because only after quarterly results are declared is the subsidy released.

In the event, the Indian basket crude oil was $107.52 per bbl (April-December) in 2012 and even with the pass through effected in the course of the year, under-recoveries of OMCs surged and were estimated at Rs.1,24,854 crore during April-December 2012-13. As the bulk of the under-recoveries is accounted for by two subsidized products, viz. diesel and LPG, the government raised diesel prices by Rs.5 per litre and capped the subsidized cylinders at six per connection per year in September 2012. With continued rise in prices, on January 17, 2013 the government further permitted OMCs to raise diesel prices in small measures periodically. However, in order to protect household budgets, it simultaneously raised the annual LPG cap from six to nine cylinders per connection.

The high level of global crude oil prices also has a significant bearing on the level of fertilizer subsidies because it is not only a key input as feedstock, but also because there is inadequate pass through in urea (the major domestic fertilizer) prices. Subsidy on fertilizers had increased substantially from Rs.32,490 crore in 2007-8 to reach Rs.67,199 crore in 2011-12 (RE). It is budgeted at Rs.60,974 crore in 2012-13. The government has been calibrating pricing policies to address the issue of burgeoning fertilizer subsidies. One of the important decisions taken was to fix per tonne subsidy on key non-nitrogenous fertilizers, thereby limiting the increase in subsidy outgo to the extent of increase in consumption.

Another major subsidy outgo in recent years, growing at an annual average rate of 25.4 per cent in the last five years ending 2011-12, is on account of food. While the targeted public distribution system (TPDS) accounts for the bulk of the food subsidy outgo, there are other welfare schemes under which food subsidy is provided. A part of the subsidy outgo also owes to the carrying cost of the buffer stock, which has mounted in recent years. In terms of the merits of subsidization, priority needs to be accorded to food subsidy in view of the under-consumption of basic food by the poor and the extent of malnutrition in the country. The government has sought to correct this through the National Food Security Act though concerns have been expressed that this will lead to a higher subsidy outgo. However, as indicated earlier, it is a part of the challenge of prioritization to provide for this basic minimum need even as other items of expenditure are minimized. Further, there is need for better targeting of subsidies and for reducing leakages involved in their delivery. Direct benefit transfer (DBT) is one such initiative.

Direct Benefit Transfer (DBT)

The DBT plan was introduced on 1 January 2013 with seven schemes in 20 districts. India has embarked on a DBT scheme in selected districts wherein it has been envisaged that benefits such as scholarships, pensions, and MGNREGA (Mahatma Gandhi National Rural Employment Guarantee Act) wages will be directly credited to the bank or post office accounts of identified beneficiaries. The DBT scheme will not substitute entirely for delivery of public services for now. It will replace neither food and kerosene subsidies under the TPDS nor fertilizer subsidies. The DBT is designed to improve targeting, reduce corruption, eliminate waste, control expenditure, and facilitate reforms. Electronic transfer of benefits is a simple design change and transfers that are already taking place through paper and cash mode will now be done through electronic transfers. This has been enabled by rapid roll out of Aadhar (Unique Identity) now covering 200 million people and rapidly growing to cover 600 million (nearly half of our population), with the National Population Register covering the other half of the populace. The DBT in tandem with such unique identification will ensure that the benefits reach the target groups faster and minimize inclusion and exclusion errors as well as corruption that are associated with manual processes.

CENTRAL PLAN OUTLAY

Plan outlay comprises gross budget support (GBS) for Plan (central Plan plus central assistance to states/ union territories [UTs]) and internal and extra budgetary resources of the central publicsector enterprises (CPSEs). The Twelfth FiveYear Plan envisages GBS of 5.25 per cent of GDP. The Budget for 2012-13 placed Central Plan outlay at Rs.6,51,509 crore as against Rs.5,58,172 crore in 2011-12 (RE). GBS for Plan is placed at Rs.3,91,027 crore in BE 2012-13.

Broad sector-wise, the following are the allocations as a proportion of the total outlay: energy (23.8 per cent); social services (27.5 per cent); transport (19.2 per cent);

communication (2.4 per cent); rural development (7.8 per cent); agriculture and allied activities (2.7 per cent); and irrigation and flood control (0.2 per cent). Central assistance to state and UT plans is placed at Rs.1,29,998 crore in BE 2012-13. Reprioritization of expenditure from non- Plan to Plan would be critical in meeting the proposed Twelfth Plan outlay.

DEFICIT OUTCOME IN 2012-13

The Budget for 2012-13 estimated a deficit level of Rs.5,13,590 crore. The net outcome of slippage in non-debt receipts and expenditure restraint fed into the outcome in terms of the desired indicators of revenue deficit as well as fiscal deficit in April- December 2012.

GOVERNMENT DEBT

The high levels of fiscal deficit in the postcrisis period added to the overall debt burden of the central government. Prolonged fiscal deficits lead to accumulation of debt beyond levels sustainable for an economy and can result in higher real and nominal interest rates, slower growth in capital formation, and potentially lower the rate of output growth. The outstanding liabilities of the central government were placed at Rs.44,68,714 crore, equivalent of 49.8 per cent of GDP at end-March 2012. As a proportion of GDP, outstanding liabilities (adjusted) of the centre peaked at 67.0 per cent in 2002-3 and have fallen subsequently notwithstanding the rise in fiscal deficit in the postcrisis years. This is on account of the fact that growth in incremental assumption of liabilities has been lower than that of nominal GDP and the debt to GDP ratio dynamics is aided by the differential between nominal GDP growth and nominal interest rates, which makes it possible to achieve a greater reduction through a given primary balance.

The total liabilities for the Government of India include debt and liabilities accounted for in the Consolidated Fund of India (technically defined as public debt) as well as liabilities accounted for in the public account. Public debt constitutes 76.3 per cent of total liabilities at end March 2012.

Government of India has the following favourable features which provide some comfort.

Most of the public debt in India is at fixed interest rates. Of the total outstanding dated securities, only 1.8 per cent was on floating rate. Thus interest payments are largely insulated from interest rate volatility, imparting stability to the Budget.

The average cost of the debt (interest payments/ debt ratio) and interest payments as a percentage of revenue receipts are on a secular decline, though some rise was seen in the past two years. Ratio of interest payments to revenue receipts has declined to around 36 per cent in 2011-12 from about 50 per cent in the beginning of the 2000s.

Government debt could also arise from the assumption of liabilities associated with recapitalizing public-sector enterprises including the banking sector. It is, therefore, customary to look at their finances.

PERFORMANCE OF DEPARTMENTAL ENTERPRISES OF THE CENTRAL GOVERNMENT

Railways

The Twelfth Five Year Plan (2012-17) envisions an integrated approach for the transport sector as a whole. It states that the vision for the transport sector should be guided by a modal mix that will lead to an efficient, sustainable, economical, safe, reliable, environmentally friendly, and regionally balanced transport system. The rail network would also have to develop a strategy to be part of an effective multi-modal transport system. The Twelfth Plan identifies safety, modernization, and capacity augmentation as the focus areas, for which initiatives are underway in Indian Railways to supplement its internal resources judiciously through public-private partnerships (PPP), cost sharing with state governments and other stakeholders, and market borrowings.

The RBI's study of state budgets 2012-13 has indicated that notwithstanding the information gap, fiscal transparency at state government levels has increased. One of the main problems with states' finances is in the financial health of the power distribution companies, which continue to accumulate losses estimated at Rs.1,90,000 crore at end-March 2011. This is mainly on account of non-revision of tariffs, subsidy arrears, high aggregate and technical losses and the high cost of buying short-term power. Thus, continued reform initiatives are critical for maintaining sound finances of the states.

The 14th Finance Commission was constituted on 2 January 2013 under the Chairmanship of Dr Y.V.Reddy, former RBI Governor. Other members of the commission are (i) Professor Abhijit Sen (ii) Ms Sushma Nath (iii) Dr M.Govinda Rao (iv) Dr Sudipto Mundle.

Terms of Reference of 14th Finance Commission

The following are the broad Terms of Reference and the matters to be taken into consideration by the 14th Finance Commission in making the recommendations:

1. (i) the distribution between the union and states of the net proceeds of taxes which are to be, or may be, divided between them under Chapter I, Part XII of the Constitution and the allocation between the states of the respective shares of such proceeds;

(ii) the principles which should govern the grants-in-aid of the revenues of the states out of the Consolidated Fund of India and the sums to be paid to the states which are in need of assistance by way of grants-in-aid of their revenues under article 275 of the Constitution for purposes other than those specified in the provisos to clause (1) of that article; and

(iii) measures needed to augment the Consolidated Fund of a state to supplement the resources of the panchayats and municipalities in the state on the basis of the recommendations made by the Finance Commission of the state.

2. The Commission has been mandated to review the state of finances, deficit, and debt levels of the union and states and suggest measures for maintaining a stable and sustainable fiscal environment consistent with equitable growth including suggestions to amend the FRBMAs currently in force. The Commission has been asked to consider and recommend incentives and disincentives for states for observing the obligations laid down in the FRBMAs.

3. In making its recommendations, the Commission inter alia is required to consider: the resources of the central government and the demands on the resources of the central government; the resources of the state governments and demands on such resources under different heads, including the impact of debt levels on resource availability in debt-stressed states; the objective of not only balancing the receipts and expenditure on revenue account of all the states and the union but also generating surpluses for capital investment; the taxation efforts of the central government and each state government and the potential for additional resource mobilization; the level of subsidies required for sustainable and inclusive growth and equitable sharing of subsidies between the central and state governments; the expenditure on the non-salary component of maintenance and upkeep of capital assets and the non-wage-related maintenance expenditure on Plan schemes to be completed by 31 March 2015 and the norms on the basis of which specific amounts are recommended for the maintenance of capital assets and the manner of monitoring such expenditure; the need for insulating the pricing of public utility services like drinking water, irrigation, power ,and public transport from policy fluctuations through statutory provisions; the need for making public-sector enterprises competitive and market oriented; listing and disinvestment; relinquishing of non-priority enterprises; the need to balance management of ecology, environment, and climate change consistent with sustainable economic development; and the impact of the proposed goods and services tax on the finances of the centre and states and the mechanism for compensation in case of any revenue loss.

4. The Commission is required to generally take the base of population figures as of 1971 in all cases where population is a factor for determination of devolution of taxes and duties and grants-in-aid; however, the Commission may also take into account the demographic changes that have taken place subsequent to 1971.

5. The Commission is to review the present public expenditure management systems in place including budgeting and accounting standards

and practices; the existing system of classification of receipts and expenditure; linking outlays to outputs and outcomes; best practices within the country and internationally and to make appropriate recommendations thereon.

6. The Commission is to review the present arrangements as regards financing of Disaster Management with reference to the funds constituted under the Disaster Management Act 2005(53 of 2005) and make appropriate recommendations thereon.
7. The Commission is to indicate the basis on which it has arrived at its findings and make available the state-wise estimates of receipts and expenditure.