Chapter - 1

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INTRODUCTION AND REVIEW OF LITERATURE

1.1 Introduction

1.2 Review of Literature

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The Constitution of India sets forth in detail the political and governmental structure of the country. India has adopted a federal form of governance, in which there are two important layers of the government i. e. Central and States. The Constitution employs a three fold classification in the division of expenditure responsibilities between the Centre and State governments i. e. the Union List, the State List and the Concurrent List.

Under the Indian Constitution, the State Governments have been entrusted with the important function of maintaining law and order and also with many nation-building activities such as education, public health and medicine, irrigation, agriculture etc. Like the Union Government, the State Governments too have adopted the policy of building up welfare states, i. e. raising agricultural and industrial prosperity of the states and looking after the needs of the poor and the downtrodden. A study of the expenditure of the states since independence reveals the importance given by them to development as well as to other requirements of the society at large.

States have important functions and responsibilities in various economic and social sectors. To accomplish the tasks assigned to them they have access to substantial revenues flow, including both taxes they collect themselves and shares in certain taxes collected by the Central Government. Mobilisation sharing and utilisation of financial resources plays a very crucial role in the federal governments across the word and can give rise to difficult problems unless handled in a spirit of mutual understanding and accommodation.

A number of difficult issues and problems are evident regarding state finances in India. State Government of Maharashtra has been facing a worsening budgetary squeeze, which has adversely affected their its development expenditure. Rapid growth of current expenditure mainly on administrative services, servicing of debt and interest payments, pensions and miscellaneous general services have been major factors which are responsible for the fiscal crisis. State's revenue receipts do not reflect commensurate growth on account of the state government's failure to mobilise the source of revenue to the optimum level. Similarly subsidies and declining cost recovery rates for economic and social service provided by the state governments have been responsible for the sluggish performance of state non-tax revenues and has contributed to the budgetary problems in a major way. Also the problems have emerged from the structure of centre state transfers and the incentives and distortions created thereby.

In recent years correcting fiscal imbalance has become the crucial task of macro-economic management in India. A series of measures towards this end have already been initiated and some more are contemplated by the Union Government as per the recommendations of the expert committees. One on tax reforms and the other which looked into the financial sector reforms.

The fiscal health of almost all states has been under the severe stress in recent years as is evidenced from negative Balance from Current Revenues (BCR) and rising deficits. The BCR turned negative and reached massive figures of minus. The fiscal deficit of the states has multiplied and emerged as a major impediment, threatening the fiscal stability of the states. The fiscal crisis have reached to an extent that ? several states are finding it very difficult even to meet cost of the salaries of their employees. The state of Maharashtra though ranks above the country's average per capita income among the states; occupying foremost position in industrialization in generating factory employment, is also prone to this crisis. The fiscal position of the Maharashtra State started deteriorating since last decade and it has now reached an acute and precarious condition. The state's increased non-plan revenue expenditure swelled the revenue deficit. This is the main culprit of increasing states fiscal deficit which caused to increase unsustainable public debt. Such a deteriorated fiscal health is attributable to the state's inability to meet revenue growth targets, restrict non-plan revenue expenditure and contain the fiscal deficit. If this situation remained unchecked at a certain level, it may create further economic consequences and destabilize the economy in the near future.

Expenditure pattern ~~at~~ of the state government in 2000-01 revenue account expenditure constituted 82.9 percent of aggregate expenditure in 2000-01. High absorption of resources towards current expenditure in which wages and salaries constitute a major component is leading to decline in investment expenditure. Non-development expenditure at the state level in India recorded a growth of 13.9 percent in 2000-01. Rise in this expenditure is mainly due to the growth of committed expenditure mainly interest payments, administrative services and pensions which together accounted for 85.5 percent of total non developmental expenditure and 30.6 percent of total state expenditure in 2000-01. Rapid increase in revenue expenditure has led to rise in revenue deficits. In case of Maharashtra Revenue Deficit increased from Rs. 316 crores in 1985-86 to Rs. 9984.0 crores in 1999-2000 (RE) subsequent to which GFD also rose from Rs. 1234 crores in 1985-86 to Rs. 13913.3 crores in 1999-2000 (RE). Growth in Revenue Deficit is the main cause for growth of GFD at state level and also fall in investment expenditure, which has reduced state capital outlays significantly. This has an adverse impact on the economic and social welfare performance level of State Government of Maharashtra.

Thus, the State Government of Maharashtra faces a critical situation. This situation calls for a serious review of Revenue Expenditure of the Government of Maharashtra. It is against this background that the present study attempts to examine the growth and composition of Revenue Expenditure of the Government of Maharashtra and review the steps taken for Expenditure Reform by the State.

Objectives of the Study

The following are the main objectives of the study :

a) To Review the fiscal reforms at the sub national level in India

b) To Study the growth and composition of the total expenditure pattern of the State Government of Maharashtra

c) To Analyse the Revenue Expenditure growth and composition pattern in Maharashtra

d) To Study the expenditure reforms initiated in Maharashtra

e) To Make policy suggestions and recommendations.

1.2 Review of Literature

Amaresh Bagchi and Tapas Sen[1] have examined overall budgetary trends and plan outlays and it's financing in the States. There is also some analysis of trends on both revenue and expenditure sides. The authors note that states have shown an increasing tendency to allocate plan resources to 'current' or revenue expenditure. One of the main conclusions of the paper is that without better control over expenditure states plan expenditure will be further squeezed. As far as tax buoyancy is concerned, the paper finds that, indirect taxes have been relatively buoyant, whereas agricultural direct taxes and entertainment taxes have largely lost their significance.

R. K. Sinha[2] in his paper found that almost all the states have gone through three phase deterioration in the revenue account balance. In the first phase (1951-52 to 1986-87), the non-plan account surplus was larger than plan deficit and to that extent it was yielding an overall revenue surplus. Between 1986-87 and 1991-92, the magnitude of plan revenue deficit increased sharply and it became larger than the non-plan surplus which itself had been declining. Third and final phase began in 1991-92, when the non-plan revenue account went into deficit. All the Good
states have had almost identical turning points, which suggest that there are systemic factors underlying this deterioration rather than state specific reasons.

Further He stated that there is no change in the budgetary position of the states even in the liberalised era. The deficit in the revenue account is increasing in all states. He has listed the irritants which have emerged during the last 50 years and stated the major policy change since 1991. He has set new goals for the plans and the public sector has suggested that to help achieve these goals, the complex resource sharing needs to be simplied, giving more resources at the disposal of the states who have to meet the cost of social and economic infrastructure in the changed economic environment.

Finances of State Government : 1998-99[3] is an article prepared in the division of Fiscal Analysis of the Department of Economic Analysis and Policy. An overview of finances of State Governments in 1998-99 based on their budgets is presented in this article. It provides a detailed analysis of all the 26 state governments in a consolidated form regarding the quantum and nature of their receipts, expenditure, outlays and deficits. Statewise features and fiscal indicators are also analysed in this article. An important observation stated in this article is that the fiscal health of states has been under severe stress in recent years. Consequently, the internal debt and debt servicing burden of the state governments have increased. The articles states that the options for the state governments include reduction in non-essential expenditures, widening the tax base, raising the user charges and cutting down subsidies wherever warranted.

In a speech, Dr. Y. V. Reddy[4] mentioned a few observations from the supplement on Finances of State Governments to RBI Bulletin, February 1998 and explained the recent initiatives undertaken by Reserve Bank of India, in respect of State Finances. He concluded his speech by reiterating the importance of states in furthering reform. He also stated that the positive elements of redefining the relationship between the state and the market have to occur in India at the state level even more than an

at the central level and that is not easy task. Such a reform has to be based on reliable data and sound analysis.

Dr. Y. V. Reddy[5] has presented new realities that emerged from the new economic policy especially globalization and stated that will find it difficult to maintain macro-economic stability, if we are away on macro economic stability parameters, especially on the inflation and fiscal deficit front. In the light of these new realities, he expects the revenue and expenditure assessment by the Eleventh Finance Commission should reflect the broad macro-economic concerns of reducing the revenue and fiscal deficit of the combined government sector. This may require working towards a consensus on the desirable path of fiscal deficit of centre and states. While fixing the target levels of fiscal deficits for the combined government sector. Some redistribution of revenue deficit and perhaps even creation of revenue surplus would be needed.

S. Gurumurthi[6] in his paper describes that, both the central and state governments have embarked on a massive attempt to reform the commodity taxation regime in India, with Maharashtra and Tamil Nadu being the first states to introduce value added tax. Tamil Nadu has introduced several changes in the regime and a long term taxation policy which will establish a stable sales tax regime. This paper takes a critical look at the new policy.

Madhav Godbole[7] in his article comments that the Maharashtra Government budget for 1999-2000 has belied all expectations and has raised more questions than what it has answered. He has stated a number of disturbing features regarding the financial position of the Maharashtra Government. He has examined the performance of the state government in respect of resource mobilization. His conclusion is that the efforts of the state government in resource mobilization are much less than are warranted in the present situation. He also states that the performance is equally disappointing in respect of all major taxes. He has pointed out the most retrograte step taken by the government by proposing the abolition of value added tax (VAT) system. He has stated a number of populist scheme and programmes, which the budget contained like the previous budgets of Maharashtra Government (especially SS-BJP combine). He concluded his article with the remark that in pursuit of populist policies the Maharashtra Government has taken several hasty decisions which are harmful to the financial health of the state.

J. L. Bajaj[8] in his paper studies the impact of pay revision on the finances of Uttar Pradesh, Madhya Pradesh and Maharashtra. The paper reveals that gross fiscal deficit of states will increase due to pay revision and revenue expenditure of states will increase by Rs. 20,000 to 30,000 crores.

N. J. Kurian[9] in his paper attempts to highlight the deteriorating trend in State Finances in recent years. Failure of states to control wasteful expenditure and reluctance to raise additional resources on the part of the states are the main causes of this, according to the author. Implementation of recommendation of the Fifth Pay Commission by states has also led to steep increase in state expenditure. The author notes that almost all indictors of fiscal health of the state economies are steadily declining. He reaches the conclusion that unless drastic measures to correct the situation are resorted to, very quickly finances of several states will collapse.

Madhav Godbole[10] in his article comment that the burden of subsidies in Maharashtra is so large and is growing so rapidly that it can no longer be overlooked in any programme for structural adjustment of state's finances. Agricultural sector has escaped the net of taxation once again. The agricultural tax which was imposed in the state in the 1970s was quickly withdrawn and has remained a dead letter since then. The government has missed an opportunity to set its house in order Reformist rhetoric not with standing, agriculture continues to escape the tax net, procurement schemes for cotton continue to make losses and the state government continues to be downgraded by the credit rating agencies.

Madhav Godbole[11] in his article comments that given the grim financial situation in his state, the State Budget 2001-02 was expected to offer bold initiatives. However, there appears to be a lack of political and administrative will to deal with substantive issues. The budget not only fails to address issues of expenditure management the question of the burden of wages and salaries. For instance, has assumed serious proportions but only outlines temporary measures to put the state's finances on a firmer footing.

B. S. Mhaske[12] described that the major factors of fiscal management leading to the fiscal crisis in Maharashtra are deterioration in state's own tax revenue, massive negative balance from current revenue, state's unsustainable borrowing, mounting non-plan revenue expenditure, non-developmental expenditure, misallocation of sectoral expenditure and rising deficits especially fiscal deficit. These weak fiscal areas should not remain unattended for a longer time. It is now high time to put very sincere and prudent fiscal efforts to correct the fiscal imbalances emerged during last decade. However, the Government of Maharashtra requires very strong political will to minimize prudent/ irregularities in the fiscal operations. The prudent fiscal mismanagement will only help bringing Maharashtra's economy on the right path of the economic development.

S. Sethuraman[13] described in his article that states have to do much more on revenue augmentation in view of the uninterrupted rise in non-developmental expenditure which resulted in larger borrowing and higher debt servicing costs.

Madhav Godbole[14] in his article described that while presenting his government's budget for 2002-03, the Maharashtra Finance Minister has made a number of major policy pronouncements intended to set the finances of the state in order. This may be music to the ears of reformers, but two things need to be kept in mind. One, similar pronouncements have been made in the past on some matters, but the government has failed to carry them out. Two, one must look at the fine print before rushing to judgment.

Y. V. Reddy[15] in his article discussed Fiscal Reforms at State Level : Review and Prospects. The presentation is divided into five parts, viz. role of the RBI in the State finances, review of fiscal reform effort, changing role of state governments, impact of financial sector reform on state finances and prospects for and issues in fiscal improvement.

He concludes with an appropriate quote from the latest book from Mr. A. Premchand, Control of Public Money, (Oxford University Press) :

"Experience shows conclusively that a policy deficit, together with a vigilance deficit, has contributed over the years to a situation, where the fiscal machinery has not been successful in addressing the concerns of the public. Despite repeated effort at improving the machinery, the institutional recidivism has become quite common. This, in turn, was partly due to the fact that the reforms did not fully address the major concerns, and partly because they were not fully implemented. Moreover, the solutions of one era became the problems of another era. Measures sought to be implemented within the executive wing of the governments were not always matched by corresponding efforts in the external agencies, such as the audit and the legislature. There is a continuing need for a balanced approach towards improvement in the operations of the executive, audit and the legislature. This is the task of future managers."

What do you conclude from
this 14 pages' exercise?

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