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India's Union Budget: Changing Scope and the Evolving Content

Rajeev Malhotra

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India’s Union Budget: Changing Scope and the Evolving Content

Rajeev Malhotra*

Abstract: The paper reflects on the changing scope of the Union Budget and the Finance Minister’s speech and assesses the evolving content of these policy instruments in recent years. The analysis undertaken is based on a framework highlighting some inter-related objectives that government budget serves in public policy making. These objectives include the use of budget as a tool for implementing fiscal policy, as an accountability tool for government functioning, a planning tool to operationalise a multi-year plan perspective and as a tool for anchoring policy coherence and coordination. The paper identifies some assessment criteria implicit in these objectives for assessing the budget content and its preparatory process. It suggests several measures and some pending reforms in fiscal policy and the underlying budget processes to address the identified objectives more effectively and makes a case for speeding up their implementation.
Key words: Government budget, fiscal policy, economic reforms, policy coherence, public accountability.

Introduction

On the Indian economic policy canvas, the Union Budget, in general, and the Finance Minister’s budget speech, in particular, has a unique relevance. As a policy event, the attention it receives stands out in comparison to other domestic policy announcements and the routine presentation of government budgets in the developed world or even in the emerging economies. In part, this is due to the nature of the Indian economy, where development process until well into 1990s has been largely state-dependent, driven predominantly by the public sector and where discretion in respect of tax and expenditure policies enjoyed by the government of the day have been amenable to influences exerted by different interest groups. Indeed, multiplicity of tax

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rates, the constant lobbing for tinkering those tax rates and the demand for expanding tax exemptions, though contributing to avoidable policy risks in the medium term, have been relentlessly pursued by investors and rent seeking business houses and entrepreneurs. As a result, the Union Budget has acquired unusual importance and there is significant hype, led by the media looking for sound bytes, in the days leading up to its presentation in Parliament.

Fortunately, this aspect of the budget is gradually changing. With the launch of the economic reforms in 1991, the policy thrust has been on creating a stable and liberal fiscal policy regime based on moderate tax rates. Moreover, this trend is set to be further reinforced with the implementation of the proposals on the Direct Tax Code (DTC) and the Goods and Service Tax (GST) in the near future.

There is another reason because of which the Union Budget and the Finance Minister's budget speech has become an important economic policy event in the country. It relates to the limited public involvement and the nature of discussions on economic issues within and outside Parliament. One has to just recall the debate on inflation in Parliament in the last two years, especially in the lower house, to recognise this. While the engagement on topical economic issues is perhaps at its best during the budget session of Parliament, in general the quality of discussions by political parities on economic and development policy issues leaves much to be desired. There is paucity of professional talent in Parliament and inadequate expertise in the secretariat supporting various Parliamentary Committees that are tasked to examine the demand for grants (budget proposals) of various ministries. A related factor that contributes to the quality of public debates is the near absence of institutionalised backstopping and research capacity in the mainstream political parties to support and lend credence to their political agendas. This handicaps the quality of their engagement on economic policy issues.

The Union Budget and its attendant process has not only reckoned with these realities of public policy making in India, but over the last two decades

has become an important instrument of policy change and implementation of economic reforms in the country.

In this context, a question that begs an answer is - has the Union Budget and the Finance Minister's budget speech evolved sufficiently in its scope and content in recent years to respond to the changing domestic and international economic policy context? This issue merits consideration from another perspective also. Given that tax reforms, currently being contemplated, covering the direct and indirect taxes are likely to be in place in the course of the coming year or two, a large portion of the space in the budget speech would be available for addressing issues that require fundamental changes in policy content, coordination, institutions or procedures. Should the Budget speech be an instrument to concert and present these measures? Perhaps, the answer is yes. Some issues that need be considered in this context are discussed in what follows.

The paper reflects on the changing scope of the Union Budget and the Finance Minister's speech and assesses the evolving content of these instruments. It makes a case for speeding up progress in this regard and advocates for an early implementation of some of the pending reforms in fiscal policy and the underlying budget processes. The analysis is organised in five sections. The first section, following the introduction, briefly lays down a framework that highlights the objectives that a government budget serves in public policy making and brings out the assessment criteria implicit in those objectives for assessing the budget content and its preparatory process. The subsequent four sections analyse India's Union budgetary developments in the last few years, particularly since 2003-04, with respect to the identified objectives and the corresponding criteria and discuss the gaps that remain to be addressed. The concluding section brings together some of the suggestions that emerge from this analysis.

I. Budget Imperatives and Criteria for Assessment

Typically, a budget for a household or an organisation is a statement of accounts reflecting the flow of receipts and expenditure on different ends. However, for a government the budget is much more. It is an instrument that

reflects the operational content of government policies for now and signals the policies to come in future. The details on annual revenue and public expenditure capture only a part of those policy priorities. With development and economic reforms, the focus of economic activity has decidedly shifted towards the non-governmental actors, not all of whom are directly affected by the allocations to various public programmes and activities. For them the Union Budget is important for its implications on the economy, including the macroeconomic parameters that set the tenor of expectations on growth and inflation for the investors as well as the consumers. Potentially, the budget (including Finance Minister's speech) by presenting a coordinated policy framework that goes beyond fiscal measures, on one hand, and the means to bring about some coherence and convergence of public and private economic activities towards common development goals, on the other hand, is a vital instrument for conducting public policy.

A government budget serves some interrelated objectives, which help in operationalising public policy and implementing the consequent programme of action. These objectives include:

- **budget as a fiscal tool** to align government spending with its revenues and ensuring macroeconomic balance, thereby creating an environment for economic stability, growth and development sustainability;
- **budget as an accountability tool** to lay down the framework for monitoring and regulating public expenditure in accordance with (budgeted) allocations and revenues;
- **budget as a planning tool** to operationalise a multi-year plan perspective by providing resources for meeting expenditure on activities in accordance with plan objectives and targets. By prioritising development activities and effecting allocation of resources among competing ends, in keeping with political manifesto of the ruling party, the budget is also an important political tool for the government and the opposition parties in the legislature; [1] and
- **budget as an anchorage for policy coherence and coordination** to address macroeconomic concerns and challenges with multifaceted, cross-sectoral and economy wide implications.

From these objectives that a government budget is expected to address, one could identify several criteria to assess the budget process. For example,

as a principal tool for conducting fiscal policy in an economy, the budget measures could be assessed for promoting growth (or private economic activity), equity (inter-personal, inter-regional and inter-generational), economic stability (impact on inflation and macroeconomic parameters) or the sustainability of the fiscal policy, which would include assessing the relative role of tax and expenditure policies in meeting these objectives. Similarly, as a tool for promoting accountability of public expenditure and government's power to mobilise revenues, it is important for the budget proposals (documentation) and the budget process to be accessible, transparent, non-discretionary (non-discriminatory), participatory (reflecting stakeholder interests) and result (outcome) oriented.[2] Adherence to these principles not only helps in making the public authorities accountable both *ex ante* and *ex poste*, but also contributes to realising other objectives of public policy, including those related to priority setting (planning) and policy coherence. Therefore, criterion based on these principles could be used to assess budget developments over a period of time.

In recent years, there have been several deliberate, but apparently isolated changes in practices and policies that have influenced the Union Budget process, the presentation of data related to the budget and its substantive content. Let us assess how some of these changes measure up to the criteria that are embedded in the objectives that government budgets are meant to address. At the same time, identify areas where further action is needed in making this instrument more effective and comprehensive in its scope to tackle domestic and global economic policy imperatives.

II. Fiscal Policy and the Budget

The enactment of the Fiscal Responsibility and Budget Management Act (FRBMA) 2003 gave a new mandate to government budgets and lent credibility to the fiscal reforms process. It created an institutional framework for conducting prudent fiscal policy and contribute to public accountability by promoting inter-generational equity in fiscal management and ensuring long-term macroeconomic stability. It sought to achieve this by creating sufficient revenue surplus, removing fiscal impediments in the effective conduct of monetary policy and encouraging prudent debt management

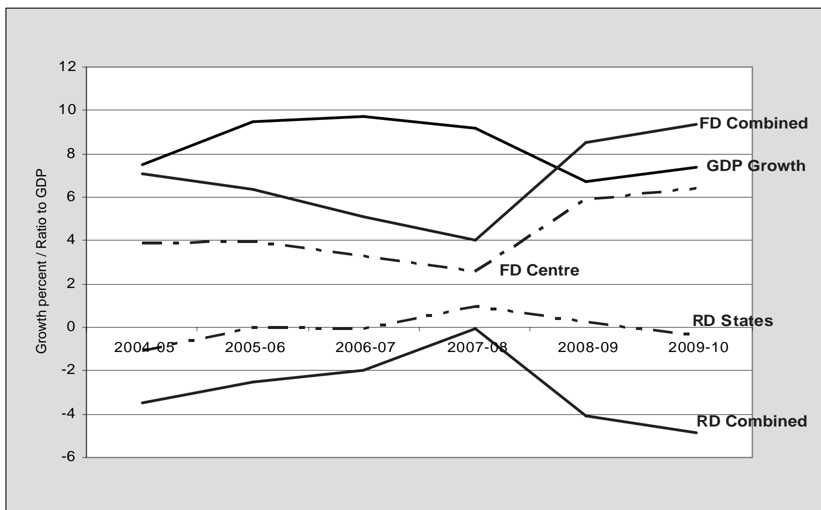
through limits on borrowings and deficits. The Rules framed to implement the FRBMA in 2004 not only made explicit annual reduction targets in the revenue and fiscal deficits, management of contingent and total liabilities (domestic and external debt), but also the requirement for a macroeconomic framework and the medium term fiscal policy and strategy statements. The Rules also made it mandatory for the Central Government to disclose any changes in accounting standards, policies and practices that had a bearing on the fiscal indicators. This requirement of statutory annual fiscal targets guiding the preparation of successive budgets, while integrating the annual budgets, helped in placing the fiscal policy in a medium term perspective.

The gradual liberalisation of the interest rates in the economy, the decision (reflected in the FRBMA 2003) to not borrow from the Reserve Bank of India (RBI), except by way of advances to meet temporary excess of cash disbursements over cash receipts and the RBI ceasing to subscribe to the primary issue of Central Government securities (discontinuing the use of quantitative easing as a policy tool) from 1 April 2006, contributed to policy independence of the monetary authority while enforcing prudence in the conduct of fiscal policy.

The frontloading of fiscal consolidation (from 2004-5 to 2007-08) against the backdrop of a medium term fiscal perspective under the FRBMA 2003 demonstrated Government's resolve and improved it credibility. It created a conducive environment for high growth in the economy. Thus, the fiscal deficit (which indicates the total borrowing requirements of the Government from all sources and is defined as the difference between revenue receipts plus certain non-debt capital receipts and the total expenditure including loans, net of repayments) for the Central Government declined from about 3.9 per cent of Gross Domestic Product (GDP) in 2004-05 to 2.6 per cent in 2007-08 and the corresponding decline in the combined fiscal deficit for Centre and States was from 7.1 per cent to 4.0 per cent (Figure 1). During this period the revenue deficit (defined as the excess of revenue expenditure over revenue receipts) of the Central Government declined from -2.4 per cent to -1.1 per cent of the GDP. For the States taken together the revenue deficit of about -1 per cent of the GDP turned into a

revenue surplus of an equivalent amount with the result that the combined revenue deficit for the Centre and States declined from about -3.5 per cent to -0.1 per cent of GDP in 2007-08.[3]

Figure 1: Budgetary Deficits and GDP Growth



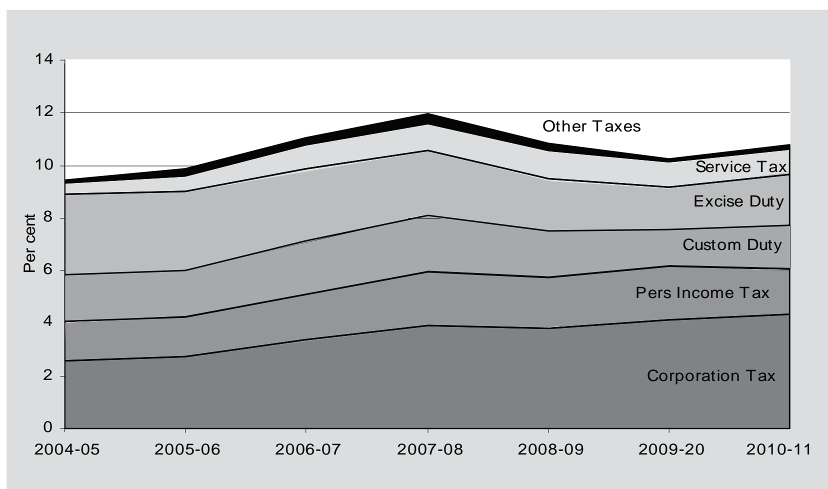
The impact on GDP growth was almost instantaneous with the economy recording an average real growth of nearly 9 per cent per annum in the four year period from 2004-05 to 2007-08. The synergy between high GDP growth and improved tax revenues yielded faster fiscal consolidation. Fiscal consolidation was expansionary in its effect on the economy. Growth in GDP was led primarily by rapid expansion in private investment (total investment demand grew at over 15 per cent per annum between 2005-06 and 2007-08), which benefited from lower cost and larger availability of capital for equity and debt. Moreover, the setting-up and the implementation of prudent fiscal rules gave a boost to the domestic capital market and business sentiments and reduced cost of risk capital for Indian firms borrowing abroad. The period saw a substantial increase in (tax) revenues, enabling the government to launch new social sector and social security programmes in support of its inclusive development agenda.

This early success in fiscal consolidation, when the economy was rapidly expanding, created the necessary fiscal space by 2008-09 for the Government to implement a countercyclical fiscal policy as growth slowed in the wake of the global financial crisis. In 2008-09 and 2009-10 the Central Government fiscal deficit, as per the revised figures now available, rose by 3.4 per cent and 4.1 per cent of GDP respectively, over the 2007-08 fiscal deficit of 2.6 per cent.[4] This magnitude of fiscal expansion and its composition in favour of shoring up consumption demand to offset the sudden negative growth (-2.4 per cent) in investment demand in 2008-09, helped in not only moderating the decline in GDP growth to an average of 7 per cent per annum in the two post-crisis years of 2008-09 and 2009-10, but also facilitated a quick rebound of the economy to the pre-crisis growth momentum.[5]

The FRBMA adjustments have been revenue-led, mainly through tax buoyancy realised with improved growth performance and aided by incremental steps in lowering of tax rates and some policy reforms. The gross tax revenue as a percentage of GDP (or simply the tax ratio) increased from 9.4 per cent of the GDP in 2004-05 to 12.0 per cent in 2007-08 (see Figure 2). It then declined to 10.9 and 10.3 per cent of GDP, respectively during 2008-09 and 2009-10 due to the slowdown of growth, lowering of certain tax rates and some tax concessions extended as a part of the stimulus measures. The gradual lowering of tax rates since the late 1980's, improvement in tax administration, a limited introduction of service tax in 1994, along with reforms to change the regressive nature of the tax system with its excessive dependence on indirect tax collections (excise and customs duties) to maintain tax-GDP ratio also contributed to improved tax performance in the post-FRBMA 2003 period. The reforms in case of the direct taxes (income tax) and excise tax were of the politically easy variety, entailing a reduction in the marginal tax rates. Service tax was introduced as an excise on a few services, without integration with the value-added tax chains. However, a major progress was achieved by rationalising custom duties in keeping with the needs of a liberalised trade regime and WTO requirements. This brought down the share of custom revenues in the Centre's gross tax collections from a peak of nearly 36.5 per cent in 1987-88 to 15.5 per cent in the budget

estimates for 2010-11. At the same time, the share of direct taxes in the gross tax collections rose from an average of around 19 per cent in the second half of 1980s to nearly 53 per cent in 2007-08. It continues to be the majority contributor to the tax kitty since then. The challenges that remain in taking the tax policy reforms forward cover the more difficult areas of eliminating tax exemptions, modernising excise tax policy and extending taxation of services, which accounts for around 55 per cent of the GDP but provides only about 1 per cent of GDP as service tax.

Figure 2: Composition of Tax Revenue (per cent of GDP)



Going forward, as the economy reverts to its new GDP trend growth rate of around 8.5 to 9 per cent per annum[6], it is time to implement FRBMA-II. The temporary derailment in the fiscal consolidation process, due to implementation of the fiscal stimulus measures during 2008-09 and 2009-10, needs an early correction through a calibrated rewinding of the fiscal expansion.

The Central Government revealed its intent in the Budget 2010-11, notably by laying down the medium term fiscal road-map. It targeted a

reduction in fiscal deficit from 5.5 per cent of GDP in 2010-11 to 4.1 per cent in 2012-13 and reduction in its total outstanding liability (including external public debt at current exchange rates) from 51.1 per cent of GDP at the end of 2010-11 to 48.2 per cent at the end of 2012-13. Both these targets improve upon (see Table 1), though only marginally in case of fiscal deficit, the corresponding targets under the fiscal roadmap suggested by the Thirteenth Finance Commission (13th FC).[7] However, this is not true of the target set for reduction in revenue deficit. The Governments medium term fiscal road map seeks to bring down revenue deficit from 4 per cent of GDP in 2010-11 to 2.7 per cent in 2012-13, which is considerably higher than the target of 1.2 per cent of GDP as per the fiscal roadmap suggested by the 13th FC.[8]

Table 1: Medium Term Fiscal Roadmap (as per cent of GDP)

	Revised Estimates 2009-10	**Budget Estimates 2010-11**	**Target 2011-12**	**Target 2012-13**
Revenue Deficit 13th Finance Commission	5.3	4.0 3.2	3.4 2.3	2.7 1.2
Fiscal Deficit 13th Finance Commission	6.7 -	5.5 5.7	4.8 4.8	4.1 4.2
Gross Tax Revenue	10.3	10.8	11.5	11.8
Outstanding Liability (year end) 13th Finance Commission	51.5 -	51.1 53.9	50.0 52.5	48.2 50.5

Source: Budget documents 2010-11 and 13th Finance Commission Report.

On the whole the conduct of fiscal policy, both during expansion (2004-2008) and during growth slowdown (2008 and 2009) has been fairly effective (as reflected by the relevant macroeconomic parameters), though scope to strengthen 'automatic stabilisers' through tax reforms exists. However, the question is whether the required fiscal consolidation as the economy recovers is sufficiently thought out and fully factored in by the Government in laying down its fiscal road-map for 2010-11 to 2012-13 and beyond. Is there scope to do better with a more pro-active fiscal adjustment, especially as the current indications are that the economy is well on its way to regaining its

pre-crisis growth momentum? [9] This needs a closer examination of tax and expenditure policies and the prospects of respective reforms in those areas.

Tax Policy

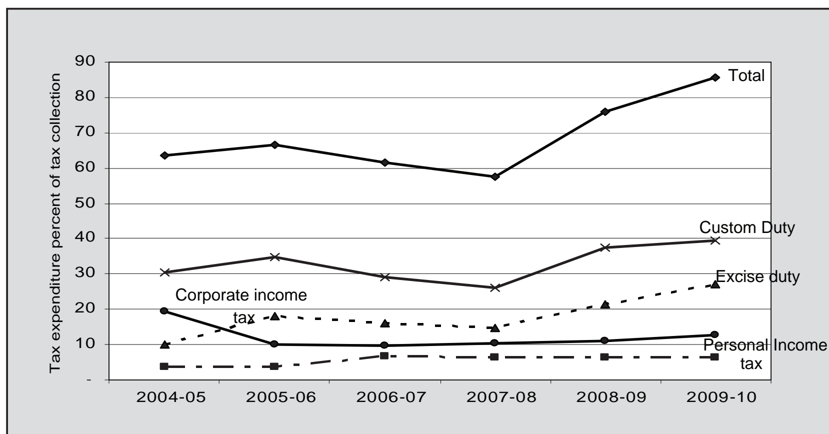
The tax policy reforms which have been contemplated for a while need to be pursued for an early implementation of the proposed DTC and the GST. It would provide the economy with a modern, broad-based, equitable and non-distortionary tax system to promote allocative efficiency along with sustained growth in tax revenues. Without going into the details of the two sets of proposals and even as one awaits their much anticipated implementation in the near future,[10] there are some issues that have a bearing on the short-run tax performance of the economy and, in general, on budget formulation that have to be addressed at an early date.

First, by invoking the experience of FRBMA 2003, it could be argued that specification of statutory fiscal consolidation targets has a salutary effect on macroeconomic management, with the Finance Minister becoming obliged to do his best to adhere to the said targets. In the absence of such exogenously specified targets (at a point in time), as was the case while preparing the budget proposals for 2010-11, the resolve may have been just that bit relaxed, with a preference to play it safe. As a result, in comparison to an average 0.65 percentage points annual increase realised in the tax ratio in the pre-crisis high growth period from 2004-05 to 2007-08, the average increase in the tax ratio projected in the Medium Term Fiscal Policy Statement 2010-11 for the period 2009-10 to 2012-13 was only 0.38 percentage points per annum. This is not only a conservative assumption,[11] but also overlooks the fact that some of the measures undertaken to improve tax administration and compliance in the recent past are likely to bear fruit in the current period.[12] Thus, there is a case for making more realistic projections on tax revenues and the resulting fiscal consolidation targets. There is also a case for an early enactment of the FRBMA-II and its operative rules for conducting a prudent fiscal policy in the coming years.[13] These are important considerations as they have significant bearing on the behaviour of private investors and critical macroeconomic parameters that underpin expectations and the consequent transactions of economic agents.

Secondly, and this goes back to the point made earlier in the introduction, tax proposals, at any point of time, should not only be anchored in a medium-to long term perspective on tax policy (preferably a statutory obligation such as the FRBMA 2003), but it is equally important that such proposals be insulated from the pulls and pressures of lobbies seeking tax concessions and exemptions to maximise their respective gains. The trend in the revenue forgone, also referred to as tax expenditure, on account of tax preferences implemented by the Central Government in the period since 2003-04 is very instructive in this regard (Figure 3).

Tax expenditure, which is essentially an implicit tax subsidy extended to certain tax payers as per the preferences exercised by the government of the day, is implemented through a range of measures such as special tax rates, tax exemptions, deductions, rebates, deferrals and credits. It impacts the overall magnitude of tax collections and the tax incidence. In principle the use of tax expenditure as an instrument for incentivising economic activity (savings, exports, infrastructure investment, charity, scientific research and technology development) and to encourage tax compliance is desirable (and enshrined in the relevant taxation Acts); however its indiscriminate use has compromised resource mobilisation efforts of the Government and created scope for exercising patronage and corruption. Moreover, tax exemptions and concessions also violate the principle of equity in taxation, primarily because of the process underpinning their implementation.

Figure 3: Tax Expenditure as percent of Tax Collections



Consider Figures 3 and 4, which reflect the data on tax expenditure or revenue foregone by the Government since 2004-05.[14] The total tax expenditure (including on account of export promotion concessions) as a percentage of Central gross tax collections increased from less than 64 per cent in 2004-05 to 67 per cent in 2005-06, before declining over the next two years to less than 58 per cent. It then rose significantly in 2008-09 and 2009-10, mainly as a consequence of the selective tax concessions extended during the economic slowdown phase, taking the total revenue foregone to around 86 per cent of the gross tax collection. It was also aided by the need for oil price management in the face of the global cost push in the first half of 2008, followed by the implementation of fiscal stimulus measures in 2008 and 2009. During this period, the tax expenditure on account of export promotion concessions (input tax neutralisation or exemption schemes) remained stable, varying between 10 to 11 per cent of the gross tax collection until 2007-08 and declining to between 6 and 7 per cent thereafter, due to slowdown in India's exports. After netting this element out from the gross revenue forgone on account of custom duties, the relative contribution of custom duty and excise duty in the total revenue forgone is at a comparable level. The revenue forgone on account of corporate tax after declining by nearly half between 2004-05 and 2005-06 has remained steady at around 10 per cent of the gross tax collections, though with a slightly rising trend. The implementation of corporate tax preferences have ensured that the effective tax rate at sectoral and overall level remains well below the statutory tax rate (Table 2). Moreover, tax expenditure incurred by the government in respect of the private sector companies turns out to be higher than that for the public sector companies.

Figure 4: Tax Expenditure (Revenue Foregone)

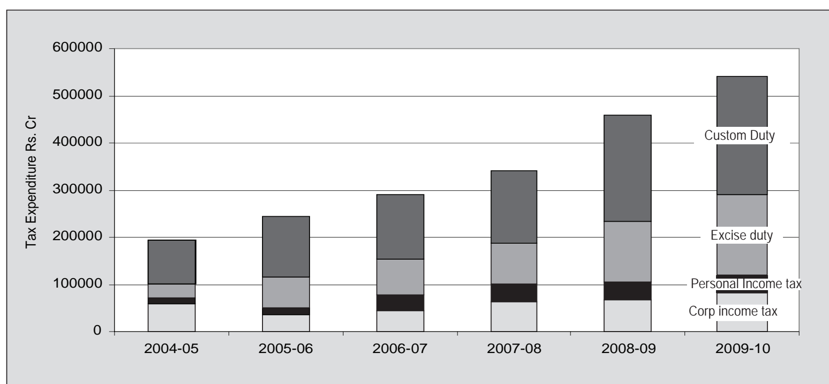


Table 2: Effective Corporate Tax Rates

Sector	2008-09	2007-08	2006-07
Public	27. 14	25. 69	23. 35
Private	21. 56	21. 28	19. 50
Manufacturing	21. 97	22. 46	21. 91
Services	23. 53	22. 00	19.01
Overall Effective tax rate	22. 77	22. 24	20.60
Statutory tax rate	33. 99	33. 99	33.66

Source: Budget documents for various years.

Note: The effective tax rates are based on sample companies and include surcharge and education cess.

At nearly 5 to 6 per cent of the GDP during 2004-05 to 2007-08 and 8 per cent in 2009-10 (after netting out the tax revenue foregone on account of export promotion concessions), Central tax expenditure is a huge cost on the tax system for incentivising a reasonable growth in tax revenues. To put these figures on tax expenditure in a broader perspective, the revenue deficit of the Central Government was -3.57 per cent of GDP in 2003-04, declining to -1.06 per cent of GDP in 2007-08 and then rising to -4.33 and -4.54 per cent of GDP in 2008-09 and 2009-10, respectively. Clearly, there is a case for an early implementation of the proposed DTC and the GST regimes with emphasis on few and lower tax rates and minimal tax concessions and exemptions. It also highlights the fact that in exercising discretion in implementing tax preferences, the government needs to carefully assess each proposal for its opportunity costs (in terms of tax revenue forgone) and the implications that has on the allocative efficiency of the economy. There cannot be any place for political weakness in entertaining requests for tax concessions in a modern liberal tax system. Moreover, in the absence of a determined policy resolve in this regard, the prevalent tendency of individuals and firms alike to base their decisions on savings and investments on consideration of their tax liability, rather than economic efficiency, would continue to hold sway and undermine the emergence of a competitive economy and an inclusive development process.

The *third* issue relates to temporary shoring-up of revenue receipts by using non-tax revenues, mainly proceeds from disinvestments, for a possible narrowing down of the Central revenue deficit. There has also been an unexpected revenue bonanza for the Government from the 3G telecom

spectrum auctions conducted in the first quarter of the current fiscal year which could also help in this regard. Though not related to tax policy concerns as such, these proceeds can assist in restoring the revenue balance of the Central Government in the short-run.[15] By using these proceeds (or at least a part of them), which incidentally are likely to add up to at least 2 per cent of GDP in the fiscal 2010-11 (of which only half was anticipated in the budget proposals presented in February 2010), the high revenue deficit of 4 per cent of GDP budgeted for 2010-11 can be brought down without compromising other items under revenue expenditure. At the same time, the revenue outflow on account of interest payments on government borrowings in the current and the subsequent years could also be moderated.[16] This is perhaps necessary and the fact that it can be easily done, due to the current favourable market conditions (for supporting public disinvestment programme), presents an opportunity that should not be missed.[17]

The concern that such a step is usually a one-shot affair, invariably discounted by markets, and, therefore, not likely to have a lasting impact on the medium term macroeconomic and fiscal balance, or on the overall economic environment, is not well founded. The realised buoyancy in tax collections, as a result of improved growth in manufacturing and services sectors in the high growth phase (2003-4 to 2007-08), is likely to be restored with the roll-back of tax concessions (implemented as a part of the fiscal stimulus) and as the economy reverts to its trend GDP growth path of 8.5 to 9 per cent per annum. This would help offset the temporary enhanced revenues due to higher disinvestment proceeds, or due to the one time spike in non-tax revenues (3G spectrum proceeds) in the short-term (i.e. 2010-11 and if required also in 2011-12). Moreover, the imminent implementation of the DTC and the GST, with the latter alone expected to add another 2 percentage points to the tax ratio, as per the estimates of the Task Force on the implementation of the FRBMA 2003 (Government of India 2004, page 7 and Appendix B), there are good reasons for a more optimistic growth in tax revenues over the next few years. Therefore, there is a case for undertaking a more confident and aggressive fiscal consolidation in the remaining period of 2010-11 and 2011-12, which will help boost business confidence, cut policy ambiguity and create the required thrust for the much needed reforms of public expenditure.

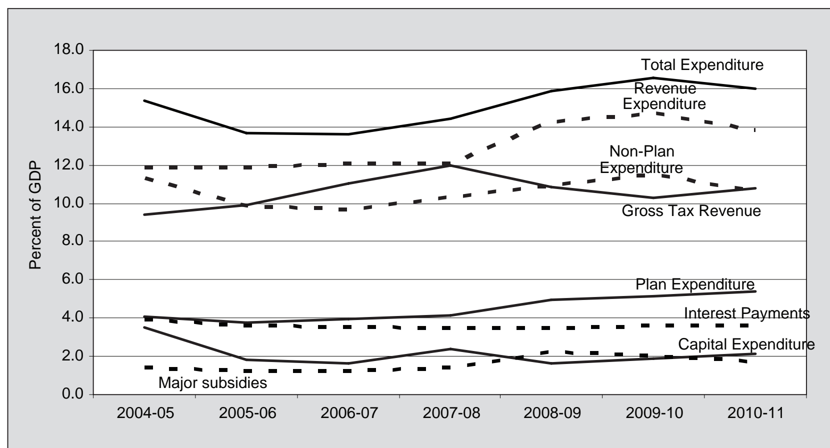
Expenditure Policy

Attention has to be accorded to expenditure policy management, not necessarily to consolidate public expenditure, but to better orient it towards the production of public goods (defence, law and order) and quasi public goods (education, health and certain kind of infrastructure).[18] There are at least three facets of the expenditure policy that are interrelated and need urgent attention with a view to realise the fiscal policy objectives of the Union Budget.

First, there is a need to rationalise revenue expenditure (or non-plan expenditure) so that revenue surplus can be realised quickly and in a sustained manner with the objective of bringing down public debt. This includes expenditure on interest payments, subsidies, defence, salaries and pensions, which are all relatively less flexible and politically (and even strategically in case of defence) difficult to curtail. *Foremost*, the focus has to be on addressing the growing burden of subsidies (Figure 5), which in recent years have ballooned to more than 2 per cent of the GDP (or more than 16 per cent of revenue expenditure and 24 per cent of revenue receipts in 2008-09) insofar as only the major subsidies are concerned.[19] There has been some progress in this regard. Following the announcement in the Budget speech on 6th July 2009, the Finance Minister was able to keep to his promise of rolling out a new nutrient based subsidy policy for fertilizer with effect from April 1, 2010. While this policy is expected to promote balanced fertilization through new fortified products and focus on extension services by the fertilizer industry, over time it is expected to reduce volatility in the demand for fertilizer subsidy and contain the subsidy bill. There has also been some deregulation in the prices of administered petroleum products in June 2010, though only partially (confined initially to petrol and some adjustment in prices of other petroleum products). At the same time, the provision for expenditure on major subsidies for fiscal 2010-11 at Rs. 11, 6224 (or 1.68 per cent of the estimated GDP for 2010-11) is considerably lower than the revised estimates for 2009-11 and marginally lower then the budget estimates for subsidies in 2009-11. This is already a good start, though the final figures under this head for 2010-11 would be known only at the end of the fiscal year.

Similarly, the decision announced in the Budget speech 2010-11 to make explicit all expenditure on subsidies by reflecting what have been described as 'below the line items' in the budget accounts, creates a scope for greater fiscal responsibility in public spending and improving transparency and accountability in the conduct of fiscal policy. With revenue buoyancy and improved non-tax receipts, the Government should be able to stick to this decision in the short-run. In the long-run it would depend on the strength of the commitment of Indian polity, price movements in global fuel oil and commodity markets and sensitivity of the Indian consumer to global (and domestic) cost-push (inflationary) impulses. Meanwhile, it may be worthwhile to place a cap on the public expenditure devoted to the major subsidies, for instance as a proportion of GDP (say 1.5 to 1.75 per cent of GDP). This could continue at least until such time that the *'Aadhaar'* programme of the Unique Identification Authority of India (UIDAI) is rolled out in the country and government is able to deliver its major subsidies efficiently.

Figure 5: Central Budgetary Transactions as per cent of GDP



The other important item of revenue expenditure which needs to be tackled is interest payments. It was nearly 4 per cent of the GDP in 2004-05. Though it declined to about 3.4 per cent of GDP in 2008-09, it accounted for more than 24 per cent of the revenue expenditure and about 36 per cent

of revenue receipts. Since then it has risen to 3.6 per cent of GDP due to the increased government borrowings due to the implementation of fiscal stimulus measures. It is a function of the size of the revenue deficit, fiscal deficit and interest costs (inflation) and can be tackled through better tax and non-tax revenue mobilisation, using proceeds from disinvestments in the short-term (as discussed in the earlier section of the paper) and, in the medium to long-term, through better management of inflationary pressures on hardening of interest rates.

Expenditure on pensions has been among the fastest growing items of public spending. It has doubled from 0.36 per cent of GDP in 1990-91 and accounts for nearly 50 per cent of the expenditure on pay and allowances. To address the growing burden of pensions in the face of improving longevity, the Government initiated (with effect from January 2004) a new defined pension system for new entrants to Central Government, other than defence services. The new scheme provides for a defined contribution to be shared equally between the employees and the employer. In respect of other elements of revenue expenditure, including expenditure on defence services, police and economic and social services of the government, the feasibility of rationalising expenditure is less obvious, though there is considerable scope to improve the efficiency of public spending in these areas as well.

The *second* issue in respect of the expenditure policy relates to the composition of public expenditure. While the dual economic and functional classification of public expenditure is not free of categorisation problems (some of these and related issues are discussed in a subsequent section), it is helpful to consider trends in plan and non-plan expenditure on one hand, and in revenue and capital expenditure on the other hand. The Plan expenditure which has been averaging around 4 per cent of the GDP from 2004-05 up until 2007-08, jumped by nearly one percentage point of GDP in 2008-09, as the Government unveiled its stimulus spending to counter the economic slowdown (Figure 5). It has retained the upward trend over the last two years and is budgeted at 5.4 per cent of the GDP in 2010-11. While this upward trend in plan spending is welcome, there is need to exercise caution on the nature of this spending. Ideally more of plan spending should be directed

towards capital formation as conventionally defined and on human capital formation (through expenditure on education and health services) rather than on social transfers that mostly influence consumption expenditure. Thus, programmes like Mahatma Gandhi National Rural Employment Guarantee Scheme (NREGS) accounting for nearly 8 to 9 per cent of the total Central Plan outlay in the last two years, though useful in transferring purchasing power to the rural poor, especially in times of economic stress and labour displacement, has a limited role in capital formation for sustaining growth over time. Moreover, there is need to forge and strengthen the link between such programmes and creation of public and quasi public goods, including through a larger provision for capital expenditure, so that plan expenditure is better oriented to meet the objectives of India's public policy.

The trend in capital expenditure reflects this concern with the composition of plan spending. The total capital expenditure witnessed a sharp decline from 3.5 per cent of GDP in 2004-05 to 1.8 per cent in 2005-06 and further to 1.6 per cent in 2006-07. This was mainly on account of a steep decline in non-plan capital expenditure though the plan capital expenditure also fell. There was some improvement in 2007-08 as capital expenditure touched 2.4 per cent of GDP, but it declined again in the next two years before recovering to 2.2 per cent of GDP in the budget estimates for 2010-11. In the most recent years since 2007-08, expenditure on subsidy shows a strong negative correlation with capital expenditure. Also there has been a significant rise in grants to State and Union Territories since 2005-06 (nearly a doubling in nominal terms between 2004-05 and 2005-06 from Rs. 14,784 crore to Rs. 30,475 crore, or an increase from about 0.45 per cent of GDP in 2004-05 to on an average of 0.8 per cent of GDP in the subsequent years) to fund the implementation of the Government's flagship programmes. These grants are classified as non-plan revenue expenditure, even though a part of expenditure from these grants is for capital works of the flagship programmes. This has not only led to an underestimation of capital expenditure in the total government expenditure, but increase in these grants has also contributed to crowding out of the total capital expenditure of the Government. This trend needs detailed analysis and correction for the medium to long term sustainability of the growth process.[20]

The *third* set of issues in respect of the expenditure policy relates to the urgent need for institutional reforms to improve the efficiency of government expenditure. This includes some system-wide issues like the review and modification of public procurement policy, the need for overhauling the prevalent incentive structure in public sector for ensuring administrative efficiency, addressing infirmities in planning and public implementation process at the Central, State and local levels, and tackling weaknesses in monitoring and evaluation systems. There are some sector specific issues, for example the role of public-private partnerships in improving the effectiveness of government spending (infrastructure), improving development delivery and targeting of benefits (poverty alleviation and social security), strengthening of regulatory frameworks (education, health, insurance and consumer protection) and outsourcing or withdrawal of public sector from the production of certain goods and services. While all these issues have a bearing on the fiscal (expenditure) policy outcomes, they need not be addressed in the context of the budget process alone. Some of these issues are elaborated in the following section of the paper, where an attempt has been made to assess the Union Budget at its preparatory process for the progress that has been made in promoting accountability in the use of public resources.

III. Budget as an Accountability Tool

There are two aspects to the use of budget documentation (including the Finance Minister's budget speech) as an accountability tool for the functioning of the government. The *first* relates to the need for information sharing and transparency in documentation to facilitate a broad based understanding of the budgetary transactions and the methodology for the preparation of the budget. This includes availability of the documentation in the public domain, amenability of the documentation to support social monitoring and evaluation, and the need for it to be based on a process that while reflecting the development vision of the government, takes into account the views and concerns of the major stakeholders in the economy. The *second* aspect of the budget as an accountability tool requires it to focus on outcomes rather than mere outlays. The budget needs to periodically (annually where feasible) present an assessment of the underlying planning and implementa-

tion processes of public programmes for the delivery of intended outcomes. Thus, the budget has to support both *ex-ante* and *ex-poste* accountability of government activity.

On these two aspects of accountability, the budget process and its documentation as it has evolved in the last few years, has made significant progress. [21] Some tasks, however, remain to be addressed or require further improvement.

There are several recent steps that have contributed to an improvement in the transparency and accountability of the budgetary transactions. These include: the discontinuation of 'below the budget line' modality of issuing government bonds to finance some of the major subsidies (oil and fertilizers) and the decision to extend all future subsidies in cash, thereby including all subsidy related liabilities explicitly in the budget accounting (budget 2010-11); placing the tax reform proposals covering the DTC and the GST in the public domain with a view to build consensus and informed decision making (2009-10); the presentation of information on revenue forgone on account of implementation of the Central Government's tax preferences in the budget documents (since budget 2006-07 and as a separate statement since budget 2010-11); the decision to prepare 'outcome budgets' to reflect the physical dimensions and attainments of the financial outlays under the budget (budget 2005-06 onwards); the setting up of a 'National Investment Fund' outside the Consolidated Fund of India in January 2005 for depositing the disinvestment proceeds and the use of income from the said fund for investment in social sectors projects and for meeting capital investment in profitable and revivable Public Sector Enterprises; the enactment of the FRBMA in 2003, the adoption of its Rules in 2004, along with the presentation of the Macro-economic framework Statement, the Medium-term Fiscal Policy Statement and Fiscal Policy Strategy Statement (budget 2004-05); introduction of a statement as a part of the budget documentation outlining the implementation status of announcements made in the budget speech (since budget 2001-02); and making explicit some of the assumptions on the projected variables (viz. nominal GDP growth) in the budget documentation.

Even as this paper was being written, the Government of India published a 'Budget Manual' (Government of India 2010b), which for the first time brings together the information on content and process of Union Budget preparation and its larger Constitutional and procedural details. It is a significant contribution to strengthening of institutional memory, transparency and continuity in a vital tool of governance and policy making. It provides all guidelines and instruction in one place for those civil servants who are, or become part of the budget making process at some points in their career. More importantly, this manual goes a long way in demystifying a process that has been an enigma to all the stakeholders who do not have a hands-on experience in the preparation of the Budget, including the policy analysts, media and the people who are the object of this exercise.

Some further steps for making the budget more transparent and improve its use as an accountability tool for monitoring public expenditure could be grouped in three broad areas. The *first* relates to changes and improvement in information presentation and budget documentation. The *second* relates to areas where the budget process could benefit from coordinated and qualitative inputs for reforming certain institutional practices related to budget preparation and its implementation. The *third* relates to the importance accorded to and the capacity improvement required in undertaking budget analysis, including at the legislative level (before the proposals for the ensuing year are voted and accorded Parliamentary approval), in the executive oversight process and among the civil society stakeholders. Some measures in each of these three areas are briefly discussed in the remaining part of this section.

A system of performance monitoring for government ministries/ departments that were implementing development programmes was introduced in 1969. However, in the absence of a clear one-to-one correspondence between the financial outlays and the performance budgets, and the fact that there has been inadequate focus on physical target setting in the annual departmental budgets, the performance budgeting exercise become ineffective. In order to address this weakness in performance budgeting and, more importantly, to forge a link between the measurable

intermediate 'physical outputs' and the somewhat distant 'outcomes' they support, led to the introduction of 'outcome budget' by the Government in 2005-06. The intention being to assess and monitor the conversion of outlays into outcomes or impacts, which are the ultimate objectives of state intervention. Though expenditure incurred is an important indicator of the progress of public programmes, it does not measure the effectiveness of the expenditure undertaken in generating the desired outputs and outcomes. It is, therefore, desirable to move away systematically from financial to output and outcome monitoring.

Detailed guidelines have been issued by the Department of Expenditure in the Ministry of Finance for preparation of outcome budgets. These guidelines require ministries to separately prepare their outcome budgets, as per a standard template, and table the document in Parliament well before the concerned Parliamentary Standing Committees examines the budget proposals of that ministry (and also release it to the public through their website). The full impact of this initiative is yet to be felt.

The real value of outcome budget lies in its role as a vital instrument of 'closure' for the budgeting and planning process. The lack of effective feedback loop of evaluation and assessment into planning and implementation process, neglect of efficiency in transforming public outlays into outputs and desired outcomes, a general apathy in the use of government resources, chronic weaknesses in public delivery systems, leakages and sub-optimal targeting of intended beneficiaries have compromised accountability of public agencies.

Some of the measures that have been identified, but need to be rapidly and effectively implemented in order to make outcome budgets a potent tool in improving public accountability of government agencies include improvement of statistical systems and identification of monitoring indicators (output and outcome) for public programmes at the level of ministries/ departments; setting-up independent evaluation or external peer-review of on-going public programmes; linking-up the release of budgeted funds with quarterly monitorable targets on selected indicators; making the continuation

of public programmes over successive years and plans a function of attaining targets on specified indicators; and presenting a consolidated outcome document on the performance of Central Government as a part of the Union Budget documentation (as distinct from the separate outcome budget documents that each ministry/department places in Parliament as present). The latter would contribute to improving the visibility and hence relevance of the outcome budget exercises. The success of the outcome budget exercise also requires an active engagement of civil society for which web-enabled dissemination of information and details on the exercise by the concerned ministry is of vital importance.

There are also specific issues related to modification in the presentation of budget allocations and expenditure, such as providing in one place the total annual flow of resources from the Union Budget to each State Government by way of all modalities, including Central Plan Assistance, Additional Central Assistance, special assistance, Centrally Sponsored Schemes, Central Sector Schemes, etc. At present the scheme wise flow of resources to the States is also not readily available in the budget related documentation. If this gap is addressed, it will reveal underlying motivation of the Central Government in the transfer of resources (where it enjoys some discretion) to States and contribute to transparency and accountability in an era of coalition politics, proliferation of regional parties and a multi-party polity in the country. There are issues related to the classification of public expenditure as well that need to be addressed for more effective use of public resources. Some of these issues are addressed in the next section where the budget is assessed for its role as a planning tool.

There are at least two institutional practices related to the process of budget preparation that could help in improving the overall transparency, credibility and accountability of government functioning in the formulation and implementation of economic policy. The *first* concerns the Finance Minister's pre-budget consultations with the stakeholders. The normal practice in this context has been to organise meetings with different interest groups such as those representing agriculturalists and agriculture research, labour and trade unions, industrialists, exporters, civil society organisations,

academics and economic policy analysts, and financial institutions. Occasionally, the Finance Minister also meets with the State Finance Ministers, as was the case in the course of the budget exercise for 2010-11. It would be desirable to make the meeting with the State Finance Ministers a regular part of the pre-budget consultations. With the policy content of the Union Budget, beyond the resource allocations to Central ministries, set to increase and the economy becoming more integrated domestically (the impending GST will add to that trend), as well as globalized, the State Governments will have a greater stake in the formulation and implementation of Central Government policies. At the same time, there is also a case for including inputs from market regulators (as to how they see their respective markets developing in the ensuing period), ensuring a more robust engagement with the civil society and scheduling these discussions appropriately in the calendar for the preparation of the budget. These consultations not only allow for a broad based public participation in the policy making process, but also enable the policy makers to have a better understanding of the stakeholders expectations and concerns.

The *second* institutional practice issue relates to implementation of the budget proposals, particularly when the normal process is challenged by certain unanticipated or sudden developments (viz. failure of monsoons, natural calamities, etc.) necessitating a revision in the budgeted tax and expenditure proposals. The preferred course of action in such instances has been to either place an across the board cut on spending (as a part of austerity measures), or to raise resources through surcharges on taxes. Such measures though scoring high on considerations of policy transparency and administrative convenience invariably undermine allocative efficiency and accountability in the use of public resources. They may end up sending a strong contractionary signal to the markets (viz. influencing consumption spending), even though their direct impact on the economy may not be so, or create expectations among the economic agents that may be contrary to the intended policy measure.[22]

Moreover, given the inflexibility in curtailing revenue expenditure, adjustment process ends up cutting down on capital (developmental) expenditure, compromising the medium to long term capacity of the economy to sustain growth. There are also instances where expenditure on some

public programmes have a lumpy character or when some ministries are more efficient in implementing their programmes and may, therefore, end up being treated on par with others due to this 'one-size fit all' approach in administering expenditure cuts. It results in sub-optimal budgetary outputs and outcomes. Further, there is the issue related to delay in the release of approved budgeted funds in the course of the year, resulting in bunching of public expenditure in the fourth quarter and in many instances on 31st of March- the closing day of the fiscal year. This yields sub-optimal outcomes for expenditure undertaken. These concerns in implementing the budgeted programmes require a flexible, more evolved and a coordinated, but transparent procedural approach. Though there have been some refinements, such as benchmarking of releases for each quarter of the year, it has not yet solved the problems of expenditure bunching, diversion, delay and cost over-runs in implementation of programmes. Some of these concerns relate to the weakness in planning process and have to be addressed by overcoming the weaknesses therein.

Finally, any tool is only as useful as the use to which it is put. There is a need to improve the capacity for budget analysis, particularly among the political parties and the civil society organisations in the country, if the budget has to play its role as an instrument for enforcing public accountability. In recent times, Parliament has not devoted adequate time for discussing budget proposals. Invariably, other political issues have hijacked the time usually kept aside for budget discussions. As a result Parliament (Speaker) has resorted to using the 'guillotine', a device (practice) to bring the debate on financial proposals to an end within a specified time, with the results that several demands for grants have to be voted by the members of Parliament without discussions. This undermines public oversight of government policies and the potential role of a budget in enforcing accountability and transparency of public action.

There is paucity of expertise available in the Parliament Secretariat to assist the various Standing Parliamentary Committees in the examination of the budget proposals from different ministries /departments. At the same time, as pointed earlier, there is practically no institutional backstopping

research and capacity for budget analysis in the mainstream political parties to support their deliberations in Parliament. In some countries, there are well established civil society organisations and 'think tanks' that specialise in undertaking budget analysis and budget monitoring to assess the use of public resources. In India also there are a few organisations that work in this area, however, there is considerable scope to strengthen capacity on this issue in the civil society domain.

Indeed, the Indian political system needs to learn and evolve, for example like the Westminster model, where a continuous tracking of government performance enables the shadow ministers (from the opposition party) to build a ready knowledge on policy issues and governance practices of specific (their shadow) ministries. In the process, they contribute to the public oversight capacity, raise the quality of debates in the public domain and 'hit the ground running' when they form the government. The major political parties, for example in the USA, the Netherlands and Australia, among others, use either in-house professional expertise supported by interns and volunteers for undertaking research on issues being politically debated, or they commission studies through independent think-tanks that provide the necessary knowledge for the parties to present their case. Political parties not only work out the fiscal implications of implementing their political manifestos, but they also seek alternative growth and policy scenarios to pitch their programme agenda at operationally realistic levels. Presently, the recourse to such measures, when undertaken by the mainstream political parties in India, is entirely ad hoc and individual-driven.[23] It is essential that the capacity to undertake meaningful budget analysis and, more generally, economic policy analysis and development monitoring is encouraged in the civil society to support political parties and other social interest groups in their oversight of public bodies.

IV. Budget and the Planning Process

The budget operationalises the annual plan, which in turn implements the agreed national development objectives, strategy and the programme of action as reflected in the Five Year Plans of the country.[24] While the Annual

Plan is anchored in a five year planning cycle,[25] up until recently the fiscal policy framework of the Budget was bereft of an explicit medium term perspective.[26] It was with the enactment of the FRBMA, 2003 that fiscal policy acquired a multi-year perspective based on statutory medium-term fiscal targets, with the objective of sustaining long-term macro economic stability. To the extent there are weaknesses in the planning process, and in particular in the annual planning cycles, there would be weaknesses in the preparation and implementation of the budget. At the same time, improvement in the budget formulation and its implementation would have beneficial consequences for the planning process in the country.

There are several conceptual issues that arise from the extant planning methodology and the adopted structure of plan financing that have a bearing on the transparency and the overall effectiveness of the budget in delivering on its objectives, including as a vital planning tool. Some of these have been summarised in the Eleventh Plan document (see Government of India 2008, Vol. I, page 47-51). These include issues related to the classification of public expenditure, which has implications for overall public expenditure management and hence on fiscal policy; the mechanisms and the criteria for Central Plan transfers (also horizontal devolution of Central grants); the treatment of investment financed by own resources of the public enterprises and other innovative methods of raising resources for public investment.

The practice adopted for the classification of public expenditure in India has been much debated, but the multiple layers of issues that it throws up remain largely unaddressed so far. The *foremost* concern relates to the distinction adopted between plan and non-plan expenditure. There has been misconstrued understanding of the distinction between the two categories of expenditure, with non-plan expenditure being seen as wasteful - to be checked for ensuring fiscal prudence. Over the years this practice has become dysfunctional and even counterproductive in the face of other fiscal developments. On one hand, it has led to proliferation of plan schemes and the tendency to let them linger from one five-year plan period to another, with little effort or incentive to complete them. This is largely due to the in-built procedural difficulties in creating employment on the non-plan side

or due to an outright ban on creating non-plan employment. A case to point is the numerous plan schemes for building irrigation capacity both in the Central and the State domains, some of which were initiated as far back as the Second and the Third Five Year Plans in the 1950s and early 1960s and remain incomplete to date. On the other hand, it has compromised the maintenance of assets built during the course of earlier plans. Once an asset is completed during a plan (for example a new road or a new school building), it is transferred to the non-plan head from the ensuing plan period, where its maintenance suffers due to limited funds that are spread thinly across competing demands.

An aspect of the plan non-plan distinction of public expenditure is also impacting the funding of social sector programmes, which have grown significantly in recent years under the inclusive development agenda of the present Central Government. Expansion in education and public health services involves proportionately large expenditure on staff salaries which are typically categorised as non-plan (revenue) expenditure. This poses problems of service delivery. Thus, while political and administrative energies are expended in raising the plan size, year after year, public expenditure management and implementation have suffered. There are huge gaps in coverage and maintenance of public services across the country, failure in timely realisation of project/programme outcomes and depletion of existing capacity and assets, problems that are largely rooted in prevalent planning practices as they have evolved over time.

Secondly, there is the issue of the relative share of capital expenditure in total public expenditure and the categorisation of public spending between revenue and capital expenditure. This issue becomes particularly important in the context of the FRBMA, which focuses on elimination of revenue deficits. Given that more than 85 per cent of the total Central Government spending and about 75 per cent of the plan expenditure is on the revenue account alone, implementation of FRBMA has a direct bearing on the Centre's capacity to formulate plan schemes directed at national priorities and at supplementing State efforts in provisioning of public services. This would particularly impact the sustainability of social sector flagship programmes

of the present Central Government that have a large revenue expenditure component. On the categorisation of expenditure between revenue and capital, there are currently entries on both sides that require a revision in keeping with the economic classification in national accounts and the Constitutional provision and understanding for the same. Thus, as indicated earlier, the Central grants to the State Governments are classified as revenue expenditure even when some of it is being used for capital expenditure. Similarly, recapitalisation of public sector enterprises, though classified as capital expenditure, is not resulting in investment, in most instances. Equity-injection is in fact a subsidy in case of the loss making enterprises. At the same time, in seeking consistency with the Constitutional understanding on the issue of expenditure on revenue account, there may be a case to put defence capital expenditure as revenue expenditure as it is not self-financing expenditure and has to be met from government revenues. There may also be a case for conceptualising capital expenditure more broadly to include expenditure on human capital formation, such that expenditure undertaken on public expansion of education and health services could be categorised as capital expenditure. While these revisions may help in a better planning and utilisation of public expenditure, it will also contribute to the implementation of budgetary commitments on the FRBMA.

Thirdly, there has been a gradual shift in the modality of plan transfers to the States from the Normal Central Assistance route (NCA, which is untied and is allocated using the revised Gadgil formula or Gadgil–Mukherjee formula), towards the use of Centrally Sponsored Schemes (CSS, which are sector specific and governed by Central guidelines). Moreover, within the CSS a large proportion of fund transfers are made directly to the district (Panchayati Raj Institutions) and state level implementing agencies, bypassing the State Governments. This has implications for planning outcomes (accountability) and budget modalities.

The CSS provides the Central Government with an instrument that enables it to earmark resources to bridge development gaps at state-level in areas of national importance. By transferring funds directly to state and district level implementing agencies it helps in avoiding delays in the

rollout of the plan schemes and prevents diversion of funds by the State Governments to meet temporary requirements for their ways and means position, or on other issues. However, this may be resulting in an implicit precedence being given to national (Central Government) priorities *vis-à-vis* state-specific (State Government) priorities, which has implications for political commitment in the implementation of plan schemes due to the perceived ownership of these schemes and on accountability in public spending. At the same time, it means more budget related responsibilities to the Central ministries running the various CSS programmes, but with little direct control on proper utilisation of funds at the implementation level and weak monitoring and evaluation feedback loops. This has, perhaps, led to a tendency among the Central ministries to assess their success in terms of the increase managed in the outlay of their plan schemes over successive years, which in turn is dependent on the utilisation of allocated amounts in the preceding year. It has encouraged a culture of financial targeting rather than physical (outcome) targeting, led by the year-end (March end) spending frenzy of public agencies. All this has compromised the effectiveness of the budget process and public spending.

Though some measures have been taken to address these planning and budget weaknesses, a fresh conceptual rethinking is required. There is a strong case for making a larger share of transfers, including plan transfers, linked to performance benchmarks that are ratified by independent social auditing processes and are based on best practices in that regard. This is also true for the horizontal transfer of Central grants, which need to be based on revised criteria of allocation with higher weightage being given to dynamic performance criteria (for example progress of the State in moderating population growth rate as against total population or progress in bringing down the incidence of poverty rather than the proportion of poor at a point of time) to support a developmental culture as against populist governance and the urge to highlight perverse development outcomes at the State level for cornering greater share of Central Government resources.[27] This would have to be balanced by consolidation of the CSS across sectors and restoring the allocation of Central grants to the NCA route, based on the said revisions in its devolution criteria. In an effort to address development

gaps at state-level and often due to political motivation, public interventions (through the CSS and state schemes) have taken place in an ad hoc manner resulting in a labyrinth of plan schemes and programmes.[28] This has resulted in administrative overload in tracking and reporting on these schemes that has compromised effectiveness in their implementation.[29] There has been some steps taken in consolidating CSS and review of Central Schemes by the Planning Commission, especially in the course of the formulation of last two five year plans, but these steps need to be more comprehensive, based on objective assessment (free of political considerations) and time-bound.

Fourthly, the public sector domain has been gradually shrinking with privatisation and divestments of public enterprises. With the strengthening of Panchayati Raj Institutions, Public Private Partnerships (PPP) and special purpose societies and agencies, there are new modalities of implementing the public sector plan. This has implications for the size of the public sector plan and the budget and there are issues of consistency and comparability, inter-temporally and across states. There is a need to streamline the methodology to address these changes for their planning and budgetary consequences, including a more accurate assessment of available resources with these entities for public investment, monitoring and evaluation of their outcomes in so far as public funds are being contributed for their working and for identifying and strengthening policy tools (regulatory regimes and measures) in the context of their diminishing dependence on the government budgets, with a view to influence their contribution to the realisation of national development objectives and priorities.

Fifthly, some of the prevalent public accounting practices are compromising the effectiveness of planning and undermining budgeting, monitoring and policy making process. The existing accounting system does not capture transaction-oriented information, nor does it distinguish between transfers to States, final expenditure and advance payments against which accounts have to be rendered. Moreover, as pointed out earlier, it does not support State-wise and scheme wise details of fund released by the Central Government nor the actual utilisation for the intended purpose.[30]

Most of the issues that have been addressed in this section require action to be taken by the Planning Commission in consultation with the Department of Expenditure and the Central ministries. While some of the issues need to be tackled at the earliest, the preparation of the Twelfth Five Year Plan (2012-2017) presents an opportunity that cannot be missed for improving the extant planning practices. For that the action needs to be taken now on priority, so that the ground work for the relevant changes can be competed in the next 12 to 15 months and implemented with effect from fiscal 2012-13, the first year for the next Five Year Plan.

V. Budget as a Tool for Policy Coherence (and spatial diffusion of reforms)

In a globalized world, where developments unfold and get transmitted rapidly and where these impulses are further conveyed to different part of the economy through increasingly integrated domestic markets, the policy response has to be instantaneous and well coordinated. Budget as a policy instrument, with an annual operational horizon, and the flexibility to intervene rapidly and by integrating policy announcements with the required fiscal measures, is uniquely placed to respond to such challenges. This was demonstrated, for example, in the wake of recent global economic slowdown precipitated by the unprecedented financial crisis in the developed world. The Government of India addressed the crisis by executing successive tranches of fiscal stimulus between December 2008 and July 2009, synchronising several policy measures (trade, credit, social security and financial prudence) with bills seeking supplementary budgetary grants for implementing fiscal expansion. These measures created a coherent policy response which worked to arrest the slowdown in the Indian economy and helped in a quick recovery of the growth momentum.

While policy announcement in the course of a year can be linked *post facto* to the required fiscal measures, but by doing so in the Budget Speech, especially when there is scope to do so, creates policy synergies and positive externalities, including through convergence of expectations among investors (business sentiments) and consumers (consumer confidence), which then creates a better chance for the policy measures to yield the desired results.

Of course, such a step requires budget to be more of a collaborative exercise between Central ministries and governments at state-level and based on rigorous analysis that ensures coherence and coordination in policy formulation and its implementation. There have been some measures taken in this direction in the past few years, some were mentioned briefly in the preceding sections; however a significant amount of work in this context remains to be addressed.

There are three levels at which the Union Budget and the Finance Minister's budget speech can be useful in bringing about greater policy coherence and encourage spatial diffusion of reforms. These relate to the coordination between the Central ministries and the Union Finance Ministry, between Union Finance Ministry (and Central ministries) and the State Governments and between the Union Government (Union Finance Ministry) and the global economy. Each of these levels of engagement and the scope for further improvement in the context of budget preparation is addressed in the following paragraphs.

Central Ministries and the Union Finance Ministry

The coordination required between the Central ministries and the Union Finance Ministry, in the context of the budget is not confined only to the inter-ministerial allocations for plan and non-plan resources, but it also covers (with the Department of Expenditure) pre-sanction appraisal of major schemes/projects (on both plan and non-plan side), the overall expenditure management, preparation of the Central Government Accounts, financial aspects of Central Government, human resource management and monitoring of public expenditure outcomes. Sector specific policy initiatives are largely the mandate of the concerned subject ministry and are generally discussed and coordinated with the Ministry of Finance only if there are financial and macroeconomic implications, or there are cross-sectoral implications.

Based on the approved Five Year Plans, the progress in the implementation of ongoing schemes and the overall resource availability, the Planning Commission is responsible for presenting a coherent and coordinated annual allocation of plan resources for inclusion in the budget.

However, policy measures and regulatory issues which are resource-neutral, or have no additional resource implications tend to be overlooked in discussions leading up to the finalisation of annual plans, the budget and the speech of the Finance Minister. Sometimes such policy measures do get announced in the Finance Minister's budget speech for the sake of introducing novelty (or even political considerations), but in the absence of a clear strategy and operational details they fail to produce the desired impact among the stakeholders and in the relevant markets. In fact, the Finance Minister's budget speech and other policy events like the independence day address of the Prime Minister and the annual address of the President to the Parliament have all routinely suffered in the past from this 'announcement effect', or the 'credibility-gap', where the announcements made are either not followed-up or are implemented only with considerable delay. This compromises the potential policy impact, encourages uncertainty and creates scope for lobbing by those who stand to lose from the implementation of such announcements/decisions. By anchoring the policy announcements/measures in the Union Budget and in the Finance Minister's budget speech, even when there are no explicit fiscal implications, would help in leveraging, as well as incentivising an improved pace in the implementation of policy reforms. There are a few institutional arrangements that could help in this regards.

First, a dedicated capacity should be created in the Finance Ministry, preferably in the office of the Finance Minister (which is independent of routine administrative responsibilities), to identify, analyse, and flag resource neutral policies and regulatory reforms. This should be pursued on a continuing basis for being taken up with the concerned ministries and stakeholders sufficiently in time for a meaningful integration in the budget proposals. A similar capacity should be available in the Planning Commission to dovetail such policy measures with the annual (plan) budget of the concerned ministry. This has been occasionally tried out in the past, however only as an individual's initiative and not as an institutionalised practice. *Secondly,* at an administrative level, there is need to energise an underutilised institutional facility of the office of Economic Advisers in the Central ministries. Following the arrangement that the Department of Expenditure has with the office of the Financial Advisers in each Central

ministry/department, the Chief Economic Adviser in the Department of Economic Affairs should put in place an annual cycle of consultations with the Economic Advisers of Central ministries, with a view to identify policy reforms and place them in the appropriate administrative context. *Thirdly*, to complement this suggested practice at a political level, the Finance Minister could also take thematically organised meetings (viz. social sectors, infrastructure sectors, issue of strategic national interest) with the relevant Central Ministers to improve cross-sectoral synergies in policy reforms and create the required political thrust for a multi-sectoral stake in the implementation of reforms.

Union Finance Ministry and State Governments

The Department of Expenditure in the Ministry of Finance is responsible for handling bulk of the Central budgetary resources transferred to the State Governments. It is also responsible for implementing the recommendations of the Finance Commission, which lays down the framework for Central-State financial relations. This places the Ministry of Finance in a unique position to use its interface with the State Governments to encourage spatial diffusion of economic reforms, including by extending the necessary technical cooperation in building relevant analytical and monitoring capacity at the state-level. The globalisation of India and an improved integration of the domestic market (including through the soon to be implemented GST reforms), makes it a policy imperative to improve governance and create a conducive environment for economic growth at the state and sub-state levels. Potentially, the budget offers a modality to encourage and anchor this process. It appears that there have been no major initiatives to use this channel (perhaps other than performance based allocation of some plan funds to the States as mentioned earlier) despite several related recommendations made in the past by the Finance Commissions and other bodies. There are several steps that could be taken in this context.

First, there is a case for (it has also been recommended by the 13th Finance Commission) creating or suitably strengthening the existing State finances division in the Department of Expenditure with analytical capacity to provide policy advise on matters pertaining to inter-governmental financial

relations and fiscal policy practice at state and sub-state levels. The advisories to the State Governments have to go well beyond accounting directives, for example, on ways and means advances or on maintaining cash balances etc. and relate to issues of economic reforms, including public service provisioning, maintenance and pricing, and investment climate at the state level. The said division would need to work in close collaboration with the Department of Economic Affairs. *Secondly,* there is scope to improve some kind of contiguity through appropriate manpower planning, between different tiers of governance, centre, state and sub-state (local government level) levels, for improving the formulation of plans and economic policy coherence and the implementation thereof. This may require the use of a dedicated cadre of officers who are well versed with the economic policy formulation, monitoring, implementation and evaluation with a view to create and strengthen the desired capacity at the state and sub-state levels. The said cadre of officers would need to have expertise in macroeconomic and fiscal policy issues as required for managing an integrated domestic market and a globalized economy. *Thirdly*, with the policy content of the Union Budget becoming increasingly relevant for State and sub-state level developments (viz. through Central Government tax policies and the conditional transfer of CSS plan resources), there is a case for institutionalising the practice of consultation with the State Finance Ministers as a part of the Union Finance Minister's pre-budget consultations, as indicated earlier. In fact, a council of State Chief Ministers is also embedded in the proposed GST implementation framework, which could well be the body to engage with the Finance Minister on policy issues in the context of budget preparation.

Union Government (Finance Ministry) and Global Economy

In a globalizing world, the challenges and opportunities of development, in general, and that of sustaining high growth over an extended period of time, in particular, have become more complex. No country is insulated from developments in other countries. The developments in the Indian economy over the last few years, when it was buffeted by multiple shocks from its external sector, reinforce this understanding. First, there was a surge in capital inflows, which peaked in the last quarter of 2007-08. This was followed by an inflationary explosion in global commodity prices, which

began even before the first challenge had ebbed and hit the economy with great force in the middle of 2008. It pushed the headline (Whole Sale Price Index) inflation in India to nearly 13 per cent, way above the historical and politically sensitive tolerance (upper) band of 5 to 6 per cent per annum. There was barely any time to deal with this problem before the third challenge, the global financial meltdown and collapse of international trade, hit the world with severity. The contagion effect of the crisis that originated in the US economy affected the financial sectors of other developed and emerging economies. However, the resulting economic slowdown and recession in major developed economies adversely impacted growth in all parts of the world. India was also impacted.

The crisis revealed critical gaps in international policy making and regulation, in risk management and international development cooperation. It raised questions on the international decision making process and accountability, which has a direct bearing on the global economic environment for the developing countries. At the domestic level, it highlighted the importance of continuous tracking of national and international developments for a timely, sequenced and calibrated policy response to prevent volatility in various markets, while sustaining growth momentum of the economy. Indeed, it necessitated, within a matter of months, a complete reversal in the direction of fiscal and monetary policy in the country. More importantly, it highlighted the need for pursuing reforms, including in the financial sector, to make the economy more competitive and the economic regulatory and oversight system more efficient and sensitive to new developments.

With the advantage of hindsight and the recent data on performance of the economy, it could be argued that despite some ambiguities arising from the rapid changes in global situation, the short-term challenges emanating from these external shocks, as well as the medium term concern of reverting to the high growth path may have been largely met. This includes issues such as the trade-off between inflation and growth, the use of monetary policy versus use of fiscal policy, their relative effectiveness and the coordination between the two. The latter includes the tension between short- and long-term fiscal policy objectives, the immediate longer term imperatives of monetary

policy and the policy and institutional reforms necessary for restoring high growth. The budget as the principal fiscal policy instrument played a defining role in addressing these macroeconomic concerns by anchoring a coherent and coordinated policy response that went well beyond the ambits of fiscal policy.

As the economy emerges from the economic slowdown, though the revival of growth in the developed world is still uncertain, the cycle seems to be playing all over again. There is a surge again in capital inflows, which is threatening an already tricky situation where the Rupee is appreciating and domestic inflation is ruling above the trend rate and food inflation has been in double digits now for a significant period of time. It is time again for the fiscal policy to work in tandem with the monetary authority to ensure macroeconomic stability and sustain high growth. Recent experience has shown that the situation can be managed; however, there are lessons to be learnt form the past developments.

A globalized Indian economy has to be prepared to face more frequent episodes of external economic impulses that could threaten its short and medium-term policy objectives. It calls for strengthening the analytical and monitoring capacity for domestic and international economic developments in the Ministry of Finance. There are some specific measures that need to be taken in this context. *First*, there is an urgent need to setup a division dedicated to tracking international developments and creating regional / country desks especially for areas of India's economic and strategic interests. This capacity could be created in the Department of Economic Affairs to support a more coordinated and coherent policy response which is anchored in a longer term strategic perspective. *Secondly*, as Indian economy emerges and takes its place in the global arena, it is time for the Finance Minister to give appropriate importance to global developments and concerns in his budget speech. While the domestic concerns will continue to be the principal focus of the fiscal and macroeconomic policy, as reflected in the Union Budget, these concerns will have to be seen against the larger global backdrop and addressed accordingly. *Thirdly*, there are some critical global issues, such as global warming, physical environment and the availability of natural resources that have a profound consequence for the domestic development

strategy. These issues need to be reflected in the planning process and in the management of India's public finances. More specifically, they need to be addressed in the context of the inter-governmental fiscal arrangements, both at the domestic level and in the context of regional neighbourhoods (South Asia). Appropriate tax and expenditure policies need to be devised for enhancing the supply of environmental public goods, for managing the supply of natural resources and for promoting positive environmental externalities to benefit the nation as a whole.[31]

Finally, there is an issue that goes beyond the focus of this paper on budgetary developments, but relates to capacity of the Union Government to work with the global actors and the world economy. The emergence of G20 as the premier international forum for promoting financial stability and sustainable economic growth in the world, with India as an important player of the grouping, necessitates creation and development of an appropriate institutional capacity in the Finance Ministry to service the country's position at the forum. By virtue of being among the larger and fast growing economies in the world, India would command a certain importance and would be a critical player in addressing the common global challenges before the G20 forum. However, beyond the personal goodwill and professional standing of the current leadership, which has been instrumental in opening the doors for India to this 'high table', there is an urgent need for a significant up-grading in India's analytical inputs that go into the G20 discussions. It would lend weight to her voice and be taken seriously in the global decision making process. There is a need also for the continued strengthening of India's economy to build on her credibility in economic policy management. This cannot be achieved by following a business as usual approach in setting up the national secretariat for the G20.

Each of these three levels of engagement for the Union Finance Ministry and the issues they raise have a direct bearing on the conduct of fiscal policy and hence on the budgetary developments in the country. Some of these are well recognised and as a matter of routine institutional practice, are being addressed, but there are other issues, some that have been highlighted here, which need better understanding and a clearer focus in the context of the budget preparation.

VI. Conclusions

The paper undertakes an assessment of the changing scope and the evolving content of the Union Budget and related processes in recent years. It argues that the Union Budget and the Finance Minister's budget speech is not merely a fiscal policy tool, but it also serves other interrelated objectives. These include the use of the budget as an accountability tool, as a planning tool to operationalise a multi-year plan perspective and as an anchorage for policy coherence and coordination. Based on the analysis, the paper identifies several fiscal policy measures and improvements in the underlying budget processes with a view to improve coherence and effectiveness of public policies.

Fiscal policy plays a dual role as a short-term counter-cyclical tool and as an instrument to maintain macroeconomic stability and promote growth over the medium term. This becomes all the more important because of the reality of business cycles in an era of globalization. In order to balance these two objectives two key aspects of fiscal policy need to be addressed and strengthened. The first relates to restructuring of the tax and expenditure policy to strengthen the "automatic stabilizers". To a considerable extent these would get addressed with the implementation of the proposed DTC and GST. Some measures identified in the paper could also help in this regard. The other relates to the issue of improving fiscal transparency, which was addressed in the FRBMA, 2003 and needs to be taken forward as the Central Government works on the FRBM-II.

The analysis on tax policy highlights that even as one awaits the implementation of the DTC and the proposed GST in the near future, the Central Government needs to urgently take steps to curtail existing tax concessions and tax exemptions and bring them in line with the proposed exempted lists of items under the GST. This would go a long way in bringing down the Central revenue deficit at a faster pace than anticipated in the Medium Term Fiscal Policy Statement 2010-11 and bring it in line with the fiscal roadmap suggested by the 13th FC. The analysis on expenditure policy emphasises the need to curtail revenue expenditure and effect changes in the composition of public expenditure. It suggests steps in the short

term that could help in this regard, while maintaining the medium to long-term perspective on running a supportive tax and expenditure policy for macroeconomic stability and growth. The analysis also identifies some of the institutional reforms to improve the efficiency of government expenditure.

The paper argues that the budget and its related documentation have to support *ex ante* and *ex poste* accountability of government activity. It identifies several measures and emphasises the need to build capacity for budget analysis among the political parties and civil society organisations with a view to strengthen the oversight of public bodies. The role of the budget as a planning tool depends on the effectiveness of the planning process in the country. To the extent there are weaknesses in the annual planning cycles, there would be weaknesses in the preparation and implementation of the budget. At the same time, improvement in the budget formulation and its implementation would have beneficial consequences for the planning process in the country. The paper reiterates some of the well known conceptual and methodological weaknesses in the planning process and makes a case for addressing them in time for the formulation of the next (twelfth) five year plan. The use of budget as a tool for anchoring policy coherence and spatial diffusion of reforms is perhaps the least recognised of its roles. The paper identifies a considerable scope in improving the budget processes and further develop its content, with a view to improve policy coherence and in speeding up implementation of reforms at different tiers of governance in the country.

Endnotes

[1] In a parliamentary democracy, the legislative approval of the budget (the finance bill) is vital for the survival and continuation of an elected government in power. Thus, the budget is a political tool that can be used by the opposition party to bring down the government if it does not enjoy the majority in the legislature.

[2] These principles have been identified as being important to the notion of good governance. They are also related in the literature to the human rights principles or cross cutting human rights norms and are seen as being vital to the conduct of public policy for human development, human freedom and human well being (see Malhotra 2006).

[3] It could be argued that the deficit figures by not taking into account the issue of oil bonds or 'below the line budget items' may have understated the extent of 'real' subsidy and hence government spending and deficits in some of the years. This practice of issuing bonds for funding certain subsidies was dispensed with from the fiscal 2010-11.

[4] It has been argued that fiscal stimulus when so measured tends to overstate the fiscal expansion undertaken purely in response to the economic slowdown, as it also includes public expenditure already committed and factored in the budget estimates for 2008-09. Thus, farmers loan waiver in 2008, or the implementation of the Sixth Central Pay Commission award were expenditures that were committed prior to the onset of economic slowdown. However, one tends to overlook that even these committed expenditures are a function of the government revenue, which dipped considerably in the slowdown years. The fact that these committed expenditures were nevertheless undertaken (leading to a higher fiscal deficit) makes it logical to include them in estimating the magnitude of fiscal stimulus.

[5] See Virmani and Malhotra (2010) and Economic Survey 2009-10 (chapter 1).

[6] Virmani and Malhotra (2010) show that the statistically significant structural break in 2003-04 resulted in the trend GDP growth rate improving by 3 percentage points to over 8.6 per cent per annum, while the step up in trend growth rate in 1980-81 was only 2 percentage points to 5.6 per cent per annum over the preceding period (1951-52 to 1979-80) when trend growth rate was 3.6 per cent per annum.

[7] See the Report of the 13th FC 2010-2015, December 2009.

[8] Medium Term Fiscal Policy Statement, Union Budget Documents 2010-11.

[9] The first quarter (April-June) 2010-11 estimates of GDP growth at 8.8 per cent puts the economy well on the path to record 8.5+/- 0.25 per cent GDP growth for 2010-11 as forecasted in Economic Survey 2009-10 chapter 1.

[10] The announced dates for the proposed implementation of DTC and the GST have been postponed more than once. As of now, the DTC is expected to be enforced from fiscal 2012-13, but the picture in respect of the GST is not sufficiently clear. See Government of India (2004) for issues and proposals on tax reforms.

[11] The GDP data for Q1 2010-11 and information on the quarterly advance tax receipts for both direct and indirect tax revenues corroborate this.

[12] There have been several initiatives for modernising business processes of tax administration including, through e-filling of returns, e-payment of taxes, issue of refunds through ECS and refund bankers and computerised tax payment reporting system. As these changes take root there will be a positive effect on tax compliance.

[13] There is need to build on the experience of the FRBMA 2003 and learn from the recent lessons on policy imperatives for a growing developing economy in a globalized world. The 13th FC, which was asked to look into the fiscal policy requirements for 2010-11 and in the medium term, recommended a calibrated exit strategy from the expansionary fiscal stance of 2008-09 and 2009-10 as the main agenda of the Central Government. Further, it suggested that the

revenue deficit of the Centre should be progressively reduced and eliminated, followed by emergence of revenue surplus by 2014-15. While recommending a cap on the overall debt of the Government, it suggested a target of 68 per cent of the GDP for the combined debt of the Centre and the States to be achieved by 2014-15. It amounts to a steady reduction in the augmented debt stock of the Centre to 45 per cent of the GDP and that of the States to less than 25 per cent of the GDP by 2014-15. The 13th FC also suggested that the FRBMA-II to specify the nature of shocks that would require a relaxation of targets under the Act.

14 The Central Government started presenting the information on revenue forgone in the Budget documents from 2006-07. Annex 12 of the Receipt Budget which reflects this information also outlines the assumptions and the methodology for estimating tax expenditure.

15 Unlike the disinvestment proceeds which are set aside in a separate National Investment Fund (NIF), there are no restrictions on the use of proceeds from the auction of 3G telecom spectrum to offset revenue expenditure of the government. The income from NIF can be used for meeting public expenditure on specific social sector projects in education, health care and employment and for the capital investment in profitable and revivable public enterprises. However, the Central Government has approved (on 5 November 2009) a one time exemption permitting full utilization of disinvestment proceeds deposited in the National Investment Fund during 2009-10 to 2011-12 for meeting capital expenditure requirements of selected social sector programmes. Thus, the capital component of revenue grants to the State governments for the flagship social sector programmes can be adjusted against disinvestment proceeds under the prevalent accounting arrangements. This would help in bringing down the revenue deficit.

16 With the accommodative monetary policy regime coming to an end in fiscal 2010-11, there has been a rise in policy rates to check strengthening of non-food or core inflation in the economy. This hardening of interest rates and the level of government borrowing envisaged to finance the 2010-11 fiscal deficit, has resulted in a rise in the benchmark-G-Sec yield, which is currently close to 8 per cent. While this has implications for an increase in revenue outflows to service public debt, it lends support to the temporary use of disinvestment proceeds for moderating government borrowing in the second half of 2010-11.

17 With record capital inflows and if one goes by the response to the Coal India IPO in October 2010, which generated in excess of Rs. 2.3 lakh crore (USD 54 billion) as against Government's disinvestment target of Rs 40,000 crore (USD 9 billion for 2010-11) the indications are that the domestic capital market along with FII will easily absorb the equity being offered as a part of the public disinvestment programme and on account of the intended increase in the public float of the listed companies, including public sector undertakings. Indeed, there may be a case here for the Government to fast track its disinvestment programme to take advantage of the current market sentiments.

18 A public good (service) is one where the consumption by the incremental consumer introduces no costs and, at the same time, it is not possible to exclude any potential consumer from benefiting from it.

19 The budget document provides details of expenditure on the major subsidies only, covering food, fertilizer and petroleum products, interest subvention and a few others. There are other expenditures of the Government which are in the nature of transfers to a target population or a region and hence qualify to be categorised as subsidies.

20 An increase in capital spending is not only desirable for sustaining growth (bridging the infrastructure deficit in the country), but it can also help overcome the contractionary implications of fiscal consolidation on the economy. While the FRBMA focus is principally on curtailing revenue expenditure, or rather on ensuring revenue surplus, the Government has the option of increasing its capital spending, to the extent that the increased borrowing and consequent increase in interest payments can be offset by an increase (or potential increase) in revenue receipts.

[21] International Budget Partnership which collaborates with civil society around the world to use budget analysis and advocacy as a tool to improve effective governance and reduce poverty. It undertakes an independent periodic survey of budget transparency and accountability around the world called the Open Budget Survey to rank the surveyed countries. As per the 2010 survey, India's open budget index score has improved from 53 in 2006 and 60 in 2008 to 67 in 2010. A higher score on the index indicates more information on public finance being shared with the public, which helps in checking abuse, and inefficient use of public resources. Reference accessed at http://www.internationalbudget.org on October 27, 2010.

[22] A case to point in this context is the implication of the announcement to implement austerity measures in fiscal 2009-10 due to sub-normal South-West monsoons. Though there was significant deficiency and delay in monsoon rainfall, given the huge food buffer stocks and the subsequent good winter (Rabi) crop, the food availability was manageable. The overall agriculture growth for the year 2009-10 declined only marginally. Yet, food inflation continues to be high even after 15 months. The announcement for across-the board austerity measures may have contributed significantly to fuelling inflationary expectations that remain to be fully checked so far.

[23] In recent years, with the constitution of the National Advisory Council the United Progressive Alliance Government, by roping in professional non-governmental expertise to inform and set the agenda on social development in the country, has taken initial steps towards institutionalising such practice in the policy making process in the country.

[24] The Five Year Plan Plans are drafted by the Planning Commission, Government of India in consultation with the Central ministries/departments, State and Union Territory Governments and other stakeholders. These plans are approved by the National Development Council, the apex development policy making body, chaired by the Prime Minister with the Union Cabinet Ministers, Deputy Chairman and Members of the Planning Commission, State Chief Ministers or the Heads of Government of the State and Union Territories as members of the council. The preparation of the Annual Plan and the allocation of Plan funds among the Central ministries/departments and the State/Union Territory Governments is the function of the Planning Commission in consultation with the respective ministries and the State Governments. The Non-Plan funds are managed and allocated by the Ministry of Finance (Department of Expenditure and the Budget Division of the Department of Economic Affairs) in consultation with the Central Ministries and Departments. In addition, the Ministry of Finance is responsible for transferring the non-plan grants and the States share in the Central tax revenues as per the recommendation of the Finance Commission which is a Constitutional body appointed once every five year and determines *inter alia* the distribution of Central tax revenues between the Centre and the States. The Department of Revenue is responsible for the tax policy and the Department of Economic Affairs with the help of the Reserve Bank of India manages the public debt and the borrowing programme of the government. The Union Budget, coordinated by the Department of Economic Affairs, brings the two sides - resource allocation and resource mobilization-together in the Finance Bill (and the related budget documentation) which is approved by Parliament in its Budget session.

[25] The Five Year Plans were also a part of a rolling fifteen year perspective plan for a major part of the planning process as followed in India since its independence, but sometime in the late 1990s the effort to continue that practice seems to have been dispensed with.

[26] In the early 1990s, the Department of Economic Affairs, Ministry of Finance did come out with a medium term fiscal policy statement; however, it was a reflection of intention and not a binding plan of action. It laid down the agenda for fiscal reforms in the early years of the rethinking on economic policy management in India.

[27] For example, some State Governments are motivated to show a higher incidence of poverty in their States as this allows them to claim a higher allocation of Central funds for rural development and poverty alleviation programmes, and under the NCA.

[28] In recent years there has been moderation in this practice, as more stake-holder consultations and better preparatory work is going into the formulation of the flagship development programmes of government.

[29] The Mid-Year Review of the Ninth Five Year Plan had a detailed commentary on this facet of the planning process in India. On a random count it identified over 300 small and major development schemes that have to be reckoned and acted upon by a district level development functionary.

[30] The need to design and implement a scheme to reform these practices, modify the existing code of accounts so as to capture more accurately the nature of public expenditure at the Centre as well as in the States has been recognised by the Planning Commission (Eleventh Plan Document, Vol. 1 page 49, paragraph 3.70). It is to be finalised during the Eleventh Plan and implemented in due course by the Controller General of Accounts. The scheme would include a comprehensive Decision Support System (DSS) and Management Information System (MIS) for monitoring of plan schemes.

[31] The 13th FC has also highlighted some of these concerns in its report.

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