CHAPTER IV

REASSESSMENT OF THE FORECAST OF THE CENTRAL GOVERNMENT

4.1 According to our terms of reference, we have to adopt a normative approach in assessing the receipts and expenditure on revenue account of the Centre and in doing so, keep in view its special requirements such as defence, security, debt servicing and other committed expenditure or liabilities. In making our recommendations we are required to keep in view the objective of not only balancing the revenue receipts and expenditure but also generating surpluses for capital investment.

4.2 We had requested the Ministry of Finance to furnish the forecast of receipts and expenditure of the Centre under the revenue account for 1990-95. The forecast sent to us assumed 1989-90 rates of taxation, tariffs, prices, emoluments and an increase of 6 per cent in GDP during 1990-95. As we thought that it would be appropriate to reassess the revenue receipts and expenditure at current rates and prices we sought from the Ministry a revised forecast assuming 6 per cent annual growth in GDP and 5 per cent rise in prices. Based on the revised forecast, we also held discussions with the officials of the Ministry of Finance.

4.3 The forecast received from the Ministry of Finance is summarised below:

(Rs. Crore)

I. Revenue Receipts	**1989-90(BE)**	**1990-95**
1. Tax Revenues	50875	337344
2. Non-tax Revenues	15831	84044
3. Total Revenue Receipts	66706	421388
II. Non-Plan Revenue Expenditure		
1. Interest Payments	17000	151255
2. Major Subsidies	7472	58433
3. Other non-Plan Expenditure	23070	165306
4. Total non-Plan Expenditure	47542	374994

4.4 The details of the forecast contain some very disturbing features. After excluding Railways, Postal and Telecommunication Services, the non-Plan revenue expenditure in 1989-90 (BE) is about 71 per cent of the total revenue receipts. As per the forecast, in 1994-95, the expenditure will rise to nearly 97 per cent of total revenue receipts. The percentage of expenditure other than major subsidies and interest payments goes up from about 35 per cent of revenue receipts in 1989-90 to nearly 40 per cent in 1994-95. Major subsidies which account for about 11 per cent in 1989-90 will be nearly 15 per cent of all revenue receipts by 1994-95. But the biggest increase is in interest payments. From the level of Rs. 17,000 crore in 1989-90, it will increase to nearly Rs. 42,200 crore in 1994-95. That will be 42 per cent of all revenue receipts in 1994-95 against 25 per cent in 1989-90. By 1994-95 interest payments will be about 125 per cent of the total proceeds from Union Excise Duties. In 1989-90, it is 75 per cent of excise revenue. As a result of this increasing imbalance between revenue receipts and non-Plan revenue expenditure as per the forecast, the Central Government will have to borrow not only for meeting its own Plan revenue expenditure and Plan grants to States but also for giving statutory grants to States under Article 275 of the Constitution. In fact, according to the forecast, total non-Plan revenue surplus available in 1994-95 will be less than the States' share of the mandatorily shareable Income Tax receipts at current levels.

4.5 We have also attempted a preliminary exercise to assess the likely overall revenue deficit of the Centre based on the forecast and assuming the Finance Commission transfers to States, Plan grants and Central Plan on revenue account broadly at current levels. The revenue deficit for each of the years from 1990-91 to 1994-95 emerges as follows:

(Rs. Crore)

1989-90(BE)	**1990-91**	**1991-92**	**1992-93**	**1993-94**	**1994-95**
(-)7,012	(-)14,500	(-)17,700	(-)21,700	(-)27,600	(-)33,900

4.6 It is obvious that with this order of revenue deficit in the Central Budget, the entire system of budgeting and financial management of the Central Government would face a crisis situation during the Eighth Plan period. It is equally clear that such a trend is totally inconsistent with the objective of balancing the revenue account of the Central Government. In our discussions with the officials of the Ministry of Finance we raised this basic issue. Their response, broadly stated, was that the projections were based on existing rates of taxation, current levels of expenditure commitments and assuming continuation of the current policy positions. They agreed that the non-Plan surplus should be significantly positive and added that the Centre had already taken certain measures in this direction. The budget of 1989-90 reflected lower revenue deficit as well as lower growth rates of consumption expenditure of the Central Government. They also stated that any guidelines the Commission might outline would be helpful to them in improving the position further.

4.7 It is against this background that we have reassessed the Centre's forecast. We are of the definite view that the forecast supplies vivid and unassailable justification to the contention that a determined effort is essential which cannot brook any delay whatsoever. While we do not want to set too optimistic goals in revenue collection or expenditure control, in revising the forecast we do assume on the part of the Central Government a reasonable degree of effort involving some not-too-soft options. If this were not to be done, the Commission could well terminate its labours without analysing the forecast at all and conclude that Central Government finances have moved beyond the possibility of corrective action. Such a conclusion is certainly not warranted. It is clear that the Central Government is keen to start a process of stabilisation of the budget, particularly the revenue account, as is evident from the budget estimates of 1989-90. As pointed out by the officials of the Ministry of Finance during the discussions, the trend of increasing revenue deficits has been reversed. We urge that this effort should continue and in our reassessment of the Centre's forecast we propose to indicate the dimensions of improvement reasonably attainable.

4.8 The objective criteria constituting our approach in assessing the Centre's revenue receipts and non-Plan revenue expenditure are the following:

(i) The Centre should set an example to the States;

(ii) The Centre should improve on its own past performance;

(iii) The price rise assumed (5 per cent) should be fully captured in tax buoyancy;

(iv) The real growth rate of GDP assumed (6 per cent) should be reflected fully in the tax yield;

(v) The Centre should move towards the objective of eliminating revenue deficit. The tax revenue yield should reflect some further increase resulting from better efficiency in taxation policy and administration;

(vi) General items of non-tax revenue receipts should, at least partly, reflect general price rise which increases the cost of services rendered;

(vii) Increase in non-Plan revenue expenditure consequent on general price rise should be marginally below the rate of price rise;

(viii) The real increase (over and above the effect of price rise) in non-Plan expenditure should be less than the rate of growth in GDP. This would imply an overall nominal rate of increase (real increase plus price rise effect) of non-Plan revenue expenditure of around 9 per cent per annum; and

(ix) Within that level of overall rate of increase, the higher growth needs of interest payments and other unavoidable expenditure should be accommodated by downward adjustment of rates of increase in other items of non-Plan revenue expenditure.

Our re-assessment of the forecast presented by the Ministry of Finance has been made applying these criteria and adjusting their effect in respect of each major item keeping also in view the other relevant factors germane to the issues.

Tax Revenue

4.9 The revised forecast of the Ministry of Finance assumes different growth rates for the Central taxes: 10.5 per cent and 10 per cent for Income Tax and Corporation Tax, respectively, (after adjusting for surcharges levied in 1989-90), 8.3 per cent for Union Excise Duties, 12 per cent for Customs Duties and 4.8 per cent for other taxes. The overall growth rate of tax revenues as given in the forecast is roughly 10 per cent. As against this, the long-term trend growth rates for the period 1974-75 to 1989-90(BE) are 10.19 per cent for Income Tax, 12.88 per cent for Corporation Tax, 13.39 per cent for Union Excise Duties and 20.42 per cent for Customs Duties. The overall growth rate of tax revenues comes to 14.64 per cent. However, we are not adopting those rates in our projections as the price rise and rate of growth of GDP assumed by us are different from those observed during the past. In our reassessment, the overall growth rate of tax revenue works out to 12.8 per cent per annum for the period 1990-91 to 1994-95. The total tax revenue receipts for the five - year period estimated by us aggregate to Rs. 3,70,014 crore, as against the estimate of Rs. 3,37,344 crore supplied by the Ministry of Finance.

4.10 The gross receipts of Income Tax and Corporation Tax have been assessed at Rs. 28,508 crore and Rs. 33,836 crore, respectively, as compared to Rs. 27,359 crore and Rs. 30,191 crore in the forecast. Our reassessment of the Excise Duty collection is Rs. 1,61,526 crore against a forecast of Rs.1,45,103 crore. The amounts transferred to the States from Income Tax and Union Excise Duties depend upon realised collections from these taxes. If these taxes are projected at high rates, which might not be realised, it would adversely affect the revenue deficit States. We have kept this in view in our reassessment of these two taxes. The reassessed figure of Customs Duties comes to Rs. 1,36,674 crore against the forecast of Rs. 1,27,221 crore.

Non-Tax Revenue

4.11 Non-tax revenues mainly comprise receipts from interest on loans advanced by the Central Government, dividends and profits from the public sector enterprises, fees and other receipts on account of services rendered by the government and its agencies and other transactions of a commercial nature.

4.12 The Ministry of Finance has estimated the interest receipts at Rs. 52,457 crore whereas our reassessment is Rs. 57,214 crore. This is after providing for a 7.5 per cent rate of return on the loans outstanding with the non-financial public sector enterprises as against 7 per cent adopted in our first report. Our projection of interest receipts is based on an annual growth rate of 12 per cent over the 1989-90 budget estimates. As the cost of borrowing is going up, there should be corresponding improvement in interest receipts.

4.13 Dividends from public sector undertakings have been projected by assuming a normative rate of return of 6 per cent on investments in those undertakings. The outstanding investments during the forecast period have been projected at a rate of 5 per cent per annum. Dividends from other investments are assumed to increase at 5 per cent over 1989-90(BE). On this basis, we reassessed dividend receipts at Rs. 13,257 crore as compared to Rs. 7,626 crore in the forecast. The budget estimate of dividends for 1989-90 shows that the government is aware of the need for and the possibility of increasing its receipts under this head. We urge that this trend may be maintained and improved upon. Government budget should receive as dividends or contribution a reasonable share of public sector profits, a major part of which is the result of either the government policy of administered prices or the near monopoly status of these public sector enterprises. If that is ensured, dividend receipts as assessed by us can be substantially realised even starting from the current level of profit earned by public sector enterprises.

4.14 Other non-tax receipts have been projected by assuming an annual growth rate of 6 per cent applied to 1989-90 (BE) of Rs. 4,354 crore.

4.15 In all, the estimate of Rs. 84,044 crore of total non-tax receipts given in the forecast by the Ministry of Finance has been reassessed at Rs. 96,488 crore.

4.16 On this basis the total revenue receipts of the Central Government during the period 1990-95 have been reassessed by us at Rs. 4,66,502 crore. This is against the estimate of Rs. 4,21,388 crore given in the forecast of the Ministry of Finance.

Revenue Expenditure

4.17 The forecast of the Ministry of Finance assumes a growth rate of non-Plan revenue expenditure of 18.41 per cent for 1990-91 over 1989-90. Growth rates ranging from 13.79 per cent to 15.71 per cent have been assumed for the rest of the years. This is against the long-term growth rate of 17.04 per cent observed during the period 1974-75 to 1989-90. If the revenue account of the Central budget is ever to be balanced at all, the real effort should come by way of effective control of non-Plan expenditure. We feel that, in this context, at least during the transitional period of reversing the trend of increasing revenue deficits, the Ministry of Finance should effectively resist the increasing demands for items like staff sanctions, subsidies, and housekeeping expenses. The fact that this can be done is evident in the budget estimates of 1989-90. The overall growth in non-Plan revenue expenditure in 1989-90(BE) over 1988-89(RE) is only 10.56 per cent. Our reassessment of non-Plan revenue expenditure for 1990-95 gives a 9.75 per cent growth rate (assuming a price rise of 5 per cent) which implies only a reasonable acceleration of the process of correction attempted in the 1989-90 budget estimates. The growth rates adopted by us in respect of major items of revenue expenditure may be viewed in this background.

4.18 The Central Government's forecast of non-Plan revenue expenditure on defence was based on annual growth rates ranging from 10.17 per cent to 10.22 per cent. We have made our projections on a uniform annual step-up of 10 per cent over 1989-90(BE).

4.19 The Ministry of Finance has placed the estimate of interest payments at Rs. 1,51,255 crore. This is an item of expenditure for which we consider that stringent norms should be applied if a dent is to be made in the Centre's revenue deficit. If an annual step-up of 10 per cent is allowed over the 1989-90 budget estimates of total capital expenditure adjusted for recovery of loans (the approximate borrowing requirements), with the rate of interest of 10 per cent per annum going up by 0.25 per cent annually, the total interest outgo on the additional borrowing requirements during the period 1990-95 works out to Rs. 32,400 crore. If interest outgo on account of annual revenue deficits estimated by us during the forecast period and on the outstanding interest-bearing liabilities at the end of 1989-90 is added, the burden of total interest payments in five years comes to Rs. 1,22,500 crore. After reassessment we have provided an amount of Rs. 1,23,880 crore towards interest payments assuming an annual growth rate of 12 per cent on the base level estimate of Rs. 19,500 crore in 1990-91 [the 1989-90 (BE) stands at Rs. 17,000 crore]. We are confident that the provision made by us is adequate to meet the normal budgetary support to the Central Plan, besides ensuring reasonable levels of disbursement of Plan loans to States. We will revert to this aspect later in the report.

4.20 The Ministry of Finance has placed the total estimate of expenditure on subsidies on food, fertilisers and exports at Rs. 58,433 crore. The Ministry's forecast does not indicate the details of expenditure on other subsidies. The Ministry's estimates for the major subsidies are based on different growth rates; 4.55 per cent to 6.39 per cent for food, 4.10 per cent to 27.44 per cent for fertilisers and 25 per cent for exports. We are quite conscious that the expenditure on subsidies is an important component of Central Government's non-Plan revenue expenditure and we have to be careful in making the provisions under this head. While the legitimate expenditure needs under this head must be met, one has to be careful that the tendency to overspend is contained. This is essential to curtail the revenue deficit. In this background we have applied a uniform annual growth rate of 8 per cent in calculating the amount of subsidies for 1990-95. We are of the opinion that the expenditure on subsidies should be contained within the overall ceiling growth rate of 8 per cent.

4.21 As the subsidy commitment on fertilizers is growing fast, we feel that the retention pricing scheme as well as its working should be subjected to a close scrutiny. As they rely substantially on subsidies from the general taxpayers, the fertiliser companies have a responsibility to manage their operations and finances with optimum efficiency and economy. We wonder whether the government is able to ensure that no part of the subsidy goes to finance extravagance and inefficiency. To ensure this, it is necessary that the retention price should be based more on norms rather than the present combination of norms and actuals, particularly when certain items constituting the retention price are outside governmental control. Another area for review is the cost of inputs, such as gas, high speed diesel oil. There does not seem to be justification for adding to the fertilizer subsidies and generating increased surpluses for certain public sector units which have the benefit of administered prices substantially above economic prices.

4.22 We have provided for an annual growth rate of 7 per cent for other non-Plan revenue expenditure. The total non-Plan expenditure including this item but excluding interest and major subsidies has been reassessed by us at Rs. 1,46,013 crore as against Rs. 1,65,306 crore in the forecast. In our projections we have not included provision for assistance on account of natural calamities to the States [Rs. 200 crore in 1989-90 (BE)] as we are dealing with this issue separately. We have not provided for committed expenditure on Plan schemes as explained earlier in Chapter III.

4.23 On the basis of the foregoing assessment, the total non-Plan revenue expenditure of the Central Government during 1990-95 reassessed by us is placed at Rs. 3,17,231 crore. This is against Rs. 3,74,994 crore in the forecast of the Union Government. Thus we are allowing non-Plan revenue expenditure at the level of about 85 per cent of what the Ministry of Finance has indicated in its forecast. On the side of revenue receipts our assessment raises the Ministry's estimate by only 10.7 per cent. We have deliberately moderated our reassessment of the Centre's forecast. This is because we know that the initial stages of correcting a trend that has been in vogue for a long time will be extremely difficult and we do not want to set too high a target for that effort. We, therefore, expect that the Central Government would be able to achieve the reasonable target of Rs. 1,49,271 crore of non-Plan pre-devolution revenue surplus for the Eighth Plan period. A summary of our reassesment of the Central Government's forecast is given in Annexure IV.1.