Chapter 1

UNION GOVERNMENT FINANCES – AN OVERVIEW

The high degree of optimism on growth prospects, which characterized the beginning of the Eleventh Plan period, had to be moderated due to certain unexpected factors viz. the sudden onset of global recession, booming international commodity prices, severe drought in India and consequent high inflationary trends. To minimize the impact of the recessionary trends on the economy, the Government introduced various fiscal policy measures, which controlled the downward spiral at the inevitable cost of higher revenue and fiscal deficits. The current year (2009-10) was characterized by recovery in the manufacturing sector, increase in private investment, higher tax collection and higher capital expenditure and a fall in the quantum of revenue and fiscal deficit when compared to the previous year. Several of the targets recommended by the XII Finance Commission to be achieved by the end of the award period, viz. 2009-10, could not be achieved and a re-assessment of targets in the light of these adverse circumstances had to be made.

1.1 The annual accounts of Union Government presented to the Parliament consist of Finance Accounts and Appropriation Accounts. Finance Accounts depict the statements of receipts into and payments from the Consolidated Fund, Contingency Fund and Public Account, while Appropriation Accounts depict the budget provision, expenditure and the resultant excess/savings under each grant/appropriation.

Box 1.1 : Union Government funds and the Public Account

Consolidated Fund

All revenues received by the Union government, all loans raised by issue of treasury bills, internal and external loans and all moneys received by the Government in repayment of loans shall form one consolidated fund entitled the "Consolidated Fund of India" established under Article 266 (1) of the Constitution of India.

Contingency Fund

The Contingency Fund of India established under Article 267 (1) of the Constitution is in the nature of an imprest placed at the disposal of the President to enable him to make advances to meet urgent unforeseen expenditure, pending authorisation by the Parliament. Approval of the legislature for such expenditure and for withdrawal of an equivalent amount from the Consolidated Fund is subsequently obtained, whereupon the advances from the Contingency Fund are recouped to the Fund.

Public Account

Besides the normal receipts and expenditure of Government which relate to the Consolidated Fund, certain other transactions enter Government Accounts, in respect of which Government acts more as a banker. Transactions relating to provident funds, small savings, other deposits, etc., are a few examples. The public moneys thus received are kept in the Public Account set up under Article 266(2) of the Constitution and the connected disbursements are also made there from.

1.2 This chapter provides a broad perspective of the finances of the Union Government during 2009-10 and analyses critical changes in the major fiscal aggregates during the first three years of the XI Plan in comparison with the X Plan. **Table 1.1** summarises the position of the finances of the Union Government, covering its receipts, disbursements, deficits and borrowings (need and its accommodation) in the current year (2009-10).

Table 1.1 Summary of the current year's operations

(₹in crore)

Receipts		Derived Parameters	Disbursements	
Consolidated Fund of India (CFI)				
Revenue Receipts	704523 (653847)	**Revenue Deficit 352956** (356377)	Revenue Expenditure	1057479 (1010224)
Miscellaneous Capital Receipts	24581 (566)		Capital Expenditure	100686 (77556)
Recovery of Loans	12733 (13509)		Loans and Advances	16115 (14586)
Total Non-Debt Receipts	741837 (667922)	**Fiscal Deficit 432443** (434444)	Total Expenditure	1174280 (1102366)
Public Debt	3405327 (2395765)		Public Debt	3085792 (2164560)
Total CFI	4147164 (3063687)	**Deficit in CFI 112908** (203239)	Total CFI	4260072 (3266926)
Contingency Fund				
Receipts	0		Appropriation	0
Public Account				
Small savings	378377 (357343)		Small savings	342105 (269605)
Reserves & Sinking Fund	101420 (100966)		Reserves & Sinking Fund	114998 (121565)
Deposits	102198 (74084)		Deposits	97849 (61590)
Advances	64855 (41981)		Advances	64006 (47331)
Suspense account	9247 (8654)		Suspense account	12022 (11240)
Remittances	4304 (1450)		Remittances	1153 (4285)
Total Public Account	660401 (584478)	**Surplus in Public Account 28268** (68862)	Total Public Account	632133 (515616)
Opening Cash	95256 (229633)	**Decrease in Cash 84640** (134377)	Closing Cash	10616 (95256)
Public Account Surplus (Demand)		28268	Deficit in (CFI) – Decrease in Cash	
Incremental Liabilities (Supply)		346578	Surplus of (Debt+ Small Savings+ RF+ Deposits)	
Incremental Liabilities (Demand)		346578	Fiscal Deficit (-) Decrease in Cash (+) Net Disbursement of (Advances+ Suspense+ Remittances)	

Note: Figures in parenthesis indicate corresponding figures for 2008-09

1.2.1 Current year's operations in the Consolidated Fund

Total receipts in the Consolidated Fund (debt and non-debt) grew by over 35 *per cent* in the current year over the previous year. The year 2009-10 showed a recovery in revenue collection, which grew by nearly 8 *per cent* over the past year (A detailed analysis has been provided in Chapter 3 of this report). The slowdown in the industry and export sector coupled with the measures taken by the Government to reduce taxes and duties[1] meant insignificant growth of less than one *per cent* in net tax revenue receipts in the previous year. Thus, the relatively high growth in net tax revenue receipts in the current year was partly because of the very low revenue collection in the previous year. Miscellaneous capital receipts, which had declined in absolute terms in 2008-09, also showed marked recovery this year, primarily due to disinvestment of government's equity holdings in public sector undertakings (Details are given in Chapter 3 of this Report). As a result, total non-debt receipts, which had shown a negative growth of over four *per cent* in 2008-09, grew by over 11 *per cent* in the current year. There was considerable negative growth in recovery of loans (minus six *per cent*) and significant growth in Public Debt (over 42 *per cent*). On the expenditure side, revenue expenditure grew at a lower rate of nearly five *per cent,* compared to the 37.47 *per cent* growth in 2008-09 over the previous year. Capital expenditure showed a high positive growth of nearly 30 *per cent,* compared to the negative growth of 33.68 *per cent,* witnessed by this head in 2008-09. With the growth in disbursements of loans and advances and repayment of Public Debt being around ten *per cent* and 43 *per cent* respectively, the total disbursements from CFI amounted to ₹ 42,60,072 crore as against receipts in CFI of ₹ 41,47,164 crore, resulting in a deficit in CFI of ₹ 1,12,908 crore, which was around 45 *per cent* lower than the deficit in the CFI in the previous year.

Box 1.2: Managing Funds: Constitutional Provisions

Article 266 (3) of the Constitution of India provides that "No moneys out of the CFI or the Consolidated Fund of State shall be appropriated except in accordance with the law and for the purposes and in the manner provided in the Constitution". This provision, read with Articles 112 and 114, culminate in the Appropriation Act after the Demands for Grants of financial year are voted by the Lok Sabha, and the connected Appropriation Bill is passed by the Parliament and assented to by the President of India. Sections 2 and 3 of the Appropriation Act provide as under:

From out of the CFI, there may be paid and applied sums not exceeding those specified in column 3 of the Schedule amounting in the aggregate towards defraying the several charges which will come in course of payment during the financial year in respect of the services specified in column 2 of the Schedule.

The sums authorized to be paid and applied from and out of the CFI by this Act shall be appropriated for the services and purposes expressed in the Schedule in relation to the said year.

1.2.2 Current year's operations in the Public Account: There was a 13 *per cent* increase in the receipts into Public Account and around 23 *per cent* in the

[1] In 2008-09 budget, a major tax relief was the reduction of CENVAT rate by 2 *percent*age points.

outgo from the Public Account in 2009-10 resulting in a Public Accounts surplus of ₹ 28,268 crore. (An analysis of the receipts in the Public Account for the current year is given in Chapter 3 of this Report).

***1.2.3 Deficits and Cash Balances**:* The current year saw a revenue deficit[2] of ₹ 3,52,956 crore, which was an improvement over the previous year by almost one *per cent*. This amounted to 5.66 *per cent* of GDP as against the FRBM target of 4.8 *per cent* for the year. The fiscal deficit[3] for 2009-10 stood at ₹ 4,32,443 crore, which was also a marginal improvement over the previous year, and amounted to around 7 *per cent* of GDP. This was slightly greater than the FRBM target of 6.8 *per cent* target set out in the MTFPS at the beginning of the year. (A detailed analysis of these imbalances is given in Chapter 5 of this Report).

1.3 Performance in the current year on key financial parameters in comparison to recommendations of the XII Finance Commission

In November, 2004, the XII Finance Commission recommended achievement of certain financial targets by the Union Government. **Table 1.2** compares the actual performance against these targets.

Table 1.2 Summary of Suggested Restructuring of Central Finances (XII Finance Commission)

(per cent of GDP)

Parameter	2004-05	2009-10	Actual performance as per Finance Accounts 2009-10
Gross Tax Revenues	9.96	10.88	10.02
Tax Revenue (Net to Centre)	7.34	7.95	7.38
Non Tax Revenues	2.21	2.25	3.93
Total Revenue Receipts	9.55	10.19	11.31
Interest Payment	4.17	2.85	3.59
Total Revenue Expenditure	12.05	10.26	16.97
Capital Expenditure	2.97	3.47	1.62
Total Expenditure	15.02	13.67	18.85
Revenue Deficit	2.50	0.00	5.66
Fiscal Deficit	4.50	3.00	6.94
Primary Deficit	0.30	0.15	3.35
Interest Payment as a *per cent* of Revenue Receipts	43.69	27.95	31.75
Debt (end of the year adjustment liabilities)	53.00	43.73	50.73

The total revenue receipts as *per cent* of GDP exceeded the target recommended by the XII Finance Commission with non tax revenues showing a sizeable increase from the targeted 2.25 *per cent* of GDP to nearly four *per*

[2] Revenue deficit = Revenue Expenditure – Revenue Receipts
[3] Fiscal Deficit = Total Expenditure – Non-Debt Receipts.

cent of GDP. This was primarily due to a considerable increase in disinvestment receipts (Details are given in Chapter 3 of this report). Total expenditure far exceeded the target recommended by the XII Finance Commission, mainly because revenue expenditure could not be contained due to the fiscal stimulus package and the Pay Commission Award. Interest payments as a percentage of GDP as well of revenue receipts exceeded targets but capital expenditure fell considerably short of the targets visualized by the XII Finance Commission. Revenue deficit, which should have been wiped out, was around six *per cent* and fiscal deficit was more than double what was envisaged by the XII Finance Commission. Debt as a *per cent* of GDP could also not be contained to around 44 *per cent* and was instead much larger at more than 50 *per cent*.

1.4 Inconsistencies between Finance Accounts and Budget documents

To ensure effective Parliamentary financial control, it is imperative that the principles of recognition of expenditure and receipt are consistent in the Budget documents and Finance and Appropriation Accounts. Figures for revenue and fiscal deficits as indicated/derived from the Finance Accounts have, however, continued to be different from those being depicted in the Budget at a Glance and some of the papers accompanying the Budget documents. This difference has been due to inclusion/exclusion of some of the transactions on receipts and expenditure side. While these are indicated in the accompanying documents of Budget papers, it is important to indicate these upfront. **Table 1.3** shows the difference in revenue and fiscal deficit as indicated/derived from the Finance Accounts and as depicted in the Budget at a Glance along with the necessary reconciliation transactions for the first two years of the Eleventh Plan.

Table 1.3: Revenue and Fiscal Deficit as in Finance Accounts and in Budget at a Glance

(₹in crore)

Deficit as per Finance Accounts	**2007-08**	**2008-09**
Revenue Deficit	85435	356377
Fiscal Deficit	164962	434444
Deficit as per Budget at a Glance		
Revenue Deficit	52569	253539
Fiscal Deficit	126912	336992
Difference in the two Figures		
Revenue Deficit	32866	102838*
Fiscal Deficit	38050	97452**
Factors explaining the difference		
Bonds issued to oil companies (Revenue Expenditure)	20554	75942
Securities issued to nationalised banks (Capital Expenditure)	9996	
Securities issued to International Monetary Fund (IMF) omitted per contra from capital expenditure		1444
Securities issued to Asset Management Trust for Stressed Assets Stabilisation Fund (SASF) of Industrial Development Bank of India (IDBI)		1225

(₹in crore)

	2007-08	2008-09
Adjustment of Write off of outstanding loans to state governments against recovery of loans		5671
Issue of Special Bonds to fertilizer companies as compensation towards fertilizer subsidy	7500	20000
Combined Effect	**38050**	**102838*** **

* Revenue Deficit understated by ₹ 1,02,838 crore (₹ 75,942 crore + ₹ 1,225 crore + ₹ 5,671 crore + ₹ 20,000 crore) in 2008-09.

** Fiscal Deficit understated by ₹ 97,386 crore (₹ 75,942 crore + ₹ 1,444 crore + ₹ 20,000 crore) in 2008-09. There is an unreconciled difference of ₹ 66 crore.

***This excludes ₹ 1,444 crore on account of Securities issued to International Monetary Fund (IMF) omitted per contra from capital expenditure.

In 2008-09, the difference in revenue deficit was of the order of ₹ 1,02,838 crore and that in fiscal deficit was ₹ 97,452 crore. This difference was on account of (1) bonds issued to oil companies (₹ 75,942 crore), (2) securities issued to IMF (₹ 1,444 crore), (3) special bonds issued to fertiliser companies as compensation towards fertilizer subsidy (₹ 20,000 crore), (4) write-off of outstanding loans to State Governments against recovery of loans (₹ 5,671 crore) and (5) securities issued to Asset Management Trust for SASF of IDBI (₹ 1,225 crore).

Union Government considers the issuance of these bonds/securities *per se* to be fiscal deficit neutral since they do not involve cash flow and are, therefore, not treated as part of budgetary expenditure/receipts. According to the existing accounting practice, the issuance of oil bonds and other similar bonds is reflected in the Annual Financial Statement (AFS) of the Union Budget under the Public Account and a matching transaction is shown under revenue expenditure for settlement of claims with oil companies/fertiliser companies. These transactions are then netted out of the revenue account of the expenditure budget and the capital account of the receipts budget through the respective reconciliation statements. However, these bonds have fiscal implications as they add to the liability of the Government. Furthermore, as interest payments on such bonds are treated as part of the revenue expenditure, they affect the revenue deficit and, thereby, the fiscal deficit on a continuing basis. The net accretion to Public Account during the year is, thus, utilized as a resource to meet deficits in Consolidated Fund of the Government.

The significant quasi-fiscal transactions to finance recurrent revenue expenditures through *de facto* borrowings not only create apprehensions about the quality of the fiscal consolidation process that is underway but raises the issue of transparency in fiscal operations and inter-generational equity in fiscal management and long term macroeconomic stability. Logically, fiscal deficit calculations presented to the Parliament in 'Budget at a glance' should take into account the net effect of all such items taken to the Public Account. On it being pointed out by CAG that the revenue and gross fiscal deficits were understated to the extent the Government incurred liabilities on account of oil, food and fertiliser bonds, the Union Budget 2008-09 for the first time explicitly reported the off-budget items as below the line items in the 'Budget at a Glance'. The matter was referred by the Government to the Thirteenth Finance Commission. The Thirteenth Finance Commission has indicated that "it is important that contingent liabilities be reported at fully and that adequate provisioning be made for such liabilities". Thirteenth Finance Commission has recommended modification of the fiscal rule that limits government guarantees (Para 9.47 at Page 134 of the Thirteenth Finance Commission 2010-2015 December 2009 Volume1: Report). However, the 13th Finance Commission Report does not explicitly provide any recommendation on the issue of deferred liabilities such as petroleum and fertilizer bonds. Till such liabilities are fully disclosed in the budgeting process of the Union Government, inconsistencies between revenue and fiscal deficits as reported in the Union Budget and as emerged from the audited Finance Accounts need to be appropriately disclosed and correct amount of the revenue and fiscal deficits taking into account all the off-budget liabilities should be reported by the Government in the Union Budget bringing transparency in the operations of these off-budget items.

1.5 Accountability in Public Finance Management

The economy has shown signs of recovery in 2009-10 and there is a need to revert to the fiscal correction path as recommended by the Thirteenth Finance Commission and as emphasized in the budget speech in 2009-10 and 2010-11. High growth target of 9 *per cent* with inclusive development is achievable in the medium term, if there is a concerted effort to rely more on non-debt receipts, improve delivery systems so that financial outcomes translate into physical outcomes within the intended time-frame and ensure transparency and accountability of institutions. Budgeting is a critical component of Public financial management framework. The credibility of the budget, its comprehensiveness and transparency, its link with the stated policy of the government and its predictability directly impacts financial management. At present, budgeting in many departments is done mechanically and there are huge variations between estimates and actual performance. Internal audit systems are not robust and there is a lack of synergy between internal and external audit. In the last decade, we are seeing an increasing trend in the transfer of public funds for expenditure to a wide variety of agencies, including special purpose vehicles, public-private partnerships, societies and NGOs. Many of these bodies do not come within the scope of audit of CAG as defined by the DPC Act. To ensure accountability and obtain required assurance, it is essential that CAG be provided access to records of all agencies receiving public funds. The Act governing the Duties, Powers and Conditions of Service of the CAG requires to be urgently reviewed and amended to ensure that accountability of public expenditure is assured as visualized in the Constitution.