

CHAPTER 5

BUDGETARY TRENDS AND FISCAL POLICY

5.1 With the price level showing a declining trend under the impact of the various anti-inflationary measures taken since July, 1974, the fiscal policy as unfolded in the Budget for 1975-76 laid greater emphasis on accelerating the rate of growth of the economy, which had been none too satisfactory in the last four years. The over-all strategy evolved to achieve this objective was to step-up the public sector plan outlay, particularly in the core sectors such as agriculture, irrigation, fertilisers, power, coal, petroleum and shipping and transport and to stimulate domestic savings and channelise these to investment in the desired fields through an appropriate mix of incentives. At the same time, inasmuch as the inflationary potential in the economy had by no means worn out completely, fiscal discipline as an integral part of demand management had to be continued so that the desired stimulus to growth could be provided within a frame-work of stable prices.

Budgetary Developments during 1974-75

5.2 During 1974-75, there was a substantial mobilisation of additional resources amounting to Rs. 1048 crores by the Central and State Governments so as to finance governmental outlays in a non-inflationary manner. However, the gap between current revenues of the Central and State Governments and total public sector outlays widened from Rs. 3589 crores in the budget estimates to Rs. 4123 crores in the revised estimates. Whereas non-development outlays increased from Rs. 5617 crores in the Budget estimates to Rs. 6321 crores in the revised estimates due to larger food and fertiliser subsidies, additional dearness allowance to employees, increase in defence expenditure mainly due to revision in pay scales and allowances, drought and flood relief expenditures and increase in railway deficit, there was also considerable step-up in development expenditures through increased assistance given to core public sector enterprises and outlay on

food and fertiliser imports. While anticipated increases in tax collections over the budget estimates did help to narrow the gap, the sharp increase in outlays outpaced the improvement in revenues.

5.3 In the revised estimates for 1974-75 whereas domestic capital receipts at Rs. 2564 crores were very nearly the same as in the budget estimates, external assistance was higher by Rs. 130 crores, leaving a gap of Rs. 542 crores to be covered by short-term borrowing. According to the provisional data available, the actual budgetary deficit* of the Central and State Governments for the year 1974-75, has been placed at Rs. 691 crores. However, in the absence of details of actual receipts and expenditure it is not possible to account for the increase in the actual deficit over the revised estimates.

5.4 A broad measure of the fiscal impact of the budget, i.e., a measure of the net direct impact on the demand for domestic goods and imports, is given by the net increase in Government's total indebtedness to the Reserve Bank of India adjusted by changes in domestic cash balances†; for the short-term economic impact of Government expenditure financed by borrowing does not depend upon the term of the debt. This fiscal deficit for 1974-75 was Rs. 654 crores, i.e., Rs. 121 crores lower than that in 1973-74 at Rs. 775 crores. On this basis, the budget for 1974-75 could be said to have exerted a less expansionary influence as compared to the budget operations in the previous year. It is also noteworthy that the Reserve Bank of India was a net seller of long-dated Government securities during 1974-75. This reflected the increased demand for Government securities from the rest of the domestic sectors (institutional investors and commercial banks) and partly neutralized the expansionary impact emanating from the short-term borrowing by the Government from the Reserve Bank of India.

* Budgetary deficit as per accounts referred to in the Economic Survey comprises the Centre's deficit as measured by net increases in the holding of treasury bills by the RBI and variation in cash balances, and States' deficit as measured by ways and means advances (net) from the RBI and variation in their cash balances. The Centre's deficit so defined is a measure of the net variation in the Central Government's short-term indebtedness to the RBI and differs from the concept in the budget documents according to which the budgetary deficit equals net increase in floating debt (i.e. net sale of Treasury Bills not only to RBI but also to all other parties such as State Governments, commercial banks, etc.) and variation in cash balances.

† While budgetary deficit is derived from budget data, the fiscal deficit, corresponding to the Planning Commission's definition of deficit financing³ has to be worked out from monetary data. This may introduce a slight discrepancy because of the fact that the final accounts of the Government are closed about three weeks after the end of the fiscal year, whereas monetary accounts represent the position as at the end of the fiscal year.

5.5 As stated above, the fiscal deficit indicates the direct impact on total demand. However, it is found that a substantial part of this deficit reflected purchases abroad of food and fertilisers. To this extent, the impact of the deficit was on balance of payments rather than on GNP or demand for domestic goods.

Central and State Government Budgets for 1975-76

5.6 Since the anti-inflationary measures of 1974-75 succeeded in arresting price inflation, the emphasis in the budgetary policy for 1975-76 shifted to providing the much needed stimulus to savings and investment for faster growth of the economy.

5.7 Such a stimulus could come only if the public sector investment in sectors of high priority itself was stepped up significantly. Accordingly, the Annual Plan outlay was increased from Rs. 4844 crores in 1974-75 to Rs. 5978 crores in 1975-76 which represents an increase of 23.4 per cent over the previous year's plan outlay. Of the total plan outlay, the allocation included in the Central Budget for 1975-76 amounted to Rs. 3612 crores. Out of this amount, Rs. 1054 crores were earmarked for assistance to States and for the Plans of Union Territories, leaving Rs. 2558 crores for the Central sector plan. Together with the extra budgetary resources representing gross surpluses of public sector undertakings and their borrowings, the Central Plan outlay for 1975-76 aggregated Rs. 3154 crores.

5.8 The combined budgeted outlays for 1975-76 of the Centre, States and the Union Territories, including the outlay from extra budgetary resources of public sector undertakings, amounted to Rs. 16840

crores, representing an increase of Rs. 1155 crores, or 7.4 per cent over the revised estimates of 1974-75. Development outlays (which include plan and non-plan outlays under development heads) accounted for Rs. 9959 crores forming 59.1 per cent of the total outlays; thus non-development outlays were to account for only 40.9 per cent of the total. Current revenues at Rs. 12776 crores were estimated to show an increase of 10.5 per cent, of which tax revenue was estimated at Rs. 9926 crores. Tax revenues including additional tax impositions were expected to increase by Rs. 1037 crores or by 11.7 per cent over the revised estimates of 1974-75. Non-tax revenues inclusive of new measures taken in 1975-76 were estimated at Rs. 2850 crores. The gap between current revenues and total outlays estimated at Rs. 4064 crores was proposed to be covered by domestic capital receipts to the extent of Rs. 2891 crores and foreign assistance of Rs. 861 crores leaving a deficit of Rs. 312 crores to be financed by short-term borrowings. In the following sections the budgetary operations of the Central and State Governments have been dealt with separately.

Central Government Budget for 1975-76

5.9 The Central budget for 1975-76 provided for a total outlay of Rs. 11450 crores; with the estimated tax revenues, including accruals from fresh tax proposals, at Rs. 5436 crores, non-tax revenue of Rs. 2372 crores and internal and external borrowings of Rs. 3395 crores (of which borrowings from external sources amounted to Rs. 861 crores) the estimated deficit in 1975-76 was Rs. 247 crores. Of the budgeted outlays, development outlays amounted to Rs. 5883 crores and non-development outlays Rs. 5567 crores,

TABLE 5.1
Budgetary Transactions of the Central and State Governments@

	1973-74 (Accounts)	1974-75		1975-76 (BE)
		(BE)	(RE)	
I. Total outlay	12252	14196	15685	16840
(a) Developmental	6864	8579	9364†	9959
(b) Non-Developmental	5388††	5617	6321	6881
II. Current Revenues	8986	10607	11562	12776
of which: Tax revenue	7389	8013	8889	9926
III. Gap (I-II)	3266	3589	4123	4064
Financed by:				
(i) Domestic capital receipts	2231	2561	2564	2891
(ii) Draft on foreign savings	492	887	1017	861
(iii) Budgetary deficit	543	141	542	312
			(691)@@	

@ As per the budgets presented to the Parliament and to the State legislatures respectively.

† Excludes notional entry of Rs. 39 crores on account of conversion of loan capital into equity capital in respect of public undertakings.

†† Excludes contingency fund transactions of the Central and State Governments Rs. (—) 8 crores.

@@ As per accounts.

representing 51.4 per cent and 48.6 per cent respectively of the total. While developmental outlay increased by Rs. 338 crores, or 6.1 per cent, non-developmental outlay increased by Rs. 387 crores, or 7.5 per cent. Subsequent to the presentation of the Central Budget, supplementary demands for grants involving a net outlay of Rs. 260 crores were authorised by Parliament in July, 1975, of which Rs. 74 crores were for assistance to public sector undertakings under the Central Plan and Rs. 75 crores for advance plan assistance to the States for investment in core sectors of irrigation and power. Later in the year further advance plan assistance of about Rs. 85 crores for accelerating the progress on selected irrigation and power projects and about Rs. 37 crores towards expenditures of a development nature necessitated by natural calamities have been allocated to the States. In January, 1976 a Second supplementary demands for grants was authorised by Parliament involving a net expenditure of Rs. 274 crores of which Rs. 26 crores were on plan account. A sizeable part of this additional expenditure was on account of the five instalments of additional dearness allowance sanctioned to Central Government employees in September, 1975*.

5.10 Excluding post-budget concessions, the yield from additional tax proposals made in the Central Budget for 1975-76 was estimated at Rs. 217.3 crores (excluding States' share), of which Rs. 173.3 crores were to accrue from union excise duties and Rs. 34.1 crores from countervailing customs duties mainly on non-ferrous metals like copper and zinc. A notable feature in the excise levies was the imposition of a general levy of one per cent *ad valorem* duty covering all goods produced for sale or other commercial purpose not specified in the Central Excise Tariff with exemption for a few items. The major objectives in imposing excise duties were to exercise an over-all restraint on private demand, to ensure utilisation of scarce material more economically and efficiently and to make consumption of luxury goods more costly.

5.11 In the field of direct taxes, there were two major changes. First, the rate of income tax on the first Rs. two lakhs of income of closely-held industrial companies was raised from 55 per cent to 60 per cent where the taxable income exceeds Rs. 2 lakhs. Second, it was provided that only 85 per cent of interest paid on public deposits by non-banking non-financial institutions could be deducted as cost from taxable income. In the case of the former, the intention was

to follow in the case of closely-held industrial companies the same pattern of rate structure as obtaining in the case of widely-held companies. As regards the latter, the objective was to discourage the companies from attracting deposits from the public by offering higher rates of interest than those offered by the commercial banks so that the priorities laid down for credit planning do not get distorted. These measures together were to yield a revenue of Rs. 10.50 crores in the current year.

5.12 The main thrust of the Central Budget for 1975-76, as stated earlier, was to stimulate the growth of prospect for the economy through providing incentives for savings and investment. The details of these have been outlined in the "Current Economic Situation : A Review" presented to Parliament in July, 1975.

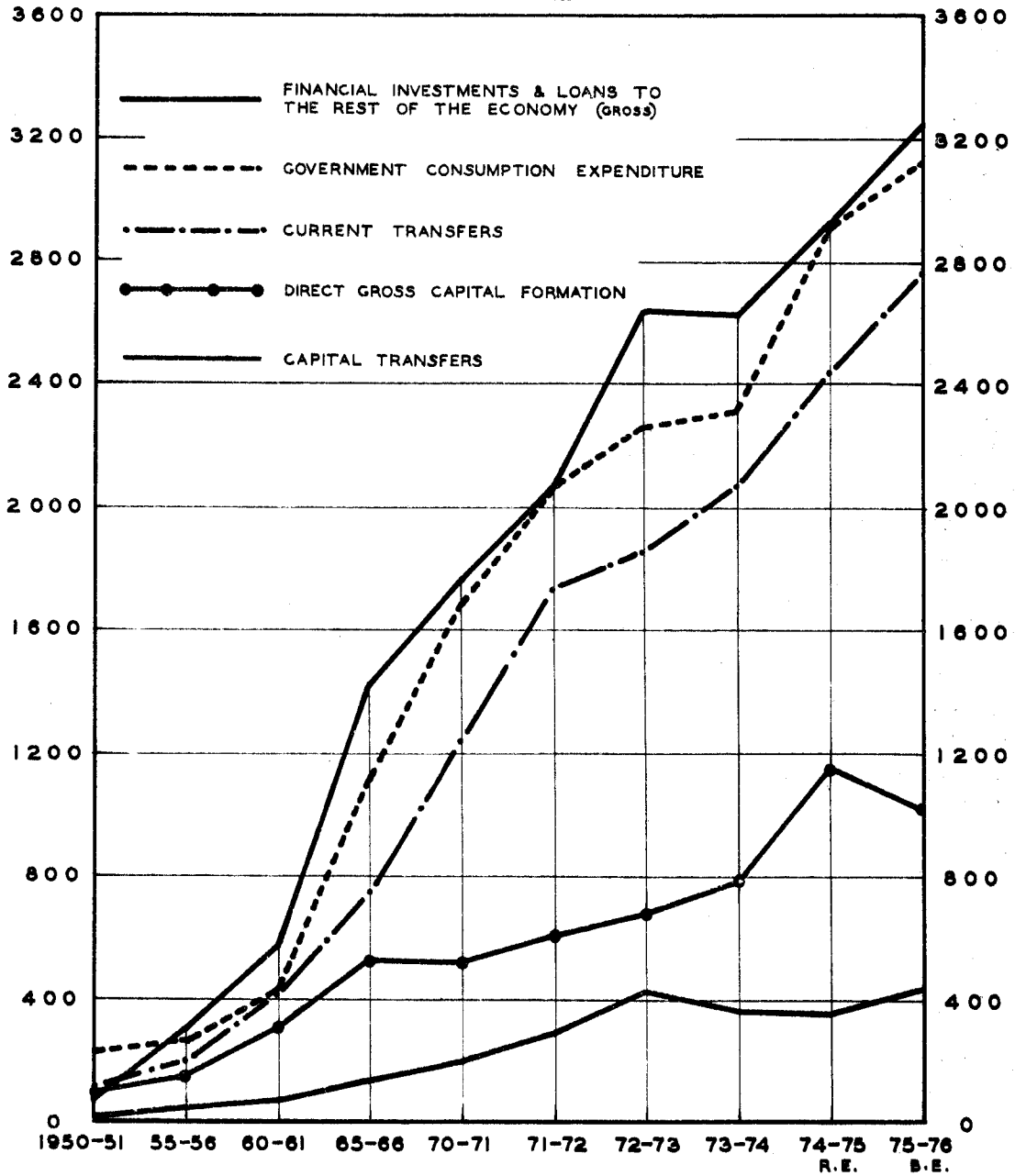
5.13 An event of considerable importance on the tax legislation side was the enactment of the Taxation Laws (Amendment) Act, 1975 in pursuance of the recommendations of the Wanchoo Committee. The main purpose of the Act was to fight and curb tax evasion, to check avoidance of tax through various legal devices, including the formation of trusts and diversion of income or wealth to members of a family unit. A scheme for voluntary disclosure of hidden income and wealth was promulgated through a Presidential Ordinance on October 8, 1975 under which persons with unaccounted income and wealth were given an opportunity to disclose their black money before the end of December, 1975. Regardless of the number of years over which it remained undisclosed, the amount disclosed would be taxed as a single block.

5.14 As at the end of December, 1975 the trend in the collection of major Central taxes has been quite encouraging. The provisional data show that collection of these taxes during the first nine months of 1975-76 amounted to 77.2 per cent of full year budget estimates as against 70.1 per cent in the corresponding period of 1974-75. Tax-wise, in relation to full-year budget estimates, Central excise collections have shown a distinct improvement at 76.8 per cent compared with 73.0 per cent last year. Revenue from customs has done even better at 78.9 per cent as against 72.2 per cent during this period last year. An even more encouraging trend is depicted in the collections from income and corporation taxes (excluding collections under the Voluntary Disclosure Scheme), the amount of collections reaching 76.8 per cent of budget estimates whereas last year during this period they had amounted to only 62.4 per cent. Under the Voluntary Disclosure of Income and Wealth

* The total amount involved on account of additional dearness allowance sanctioned to Government employees, including railways and P & T, in September, 1975 is Rs. 285 crores of which Rs. 113 crores are included in the second supplementary demands for grants.

CENTRAL GOVERNMENT EXPENDITURE (ECONOMIC CATEGORIES)

RS. CRORES



MINISTRY OF FINANCE, ECONOMIC DIVISION.

Ordinance, 1975, total amount disclosed has been provisionally placed at Rs. 1578 crores of which incomes disclosed have amounted to Rs. 744 crores and wealth Rs. 834 crores. Income-tax and wealth-tax payable respectively on these disclosed amounts are estimated to be Rs. 241 crores and Rs. 7.7 crores respectively, of which Rs. 159 crores of income-tax and Rs. 4.2 crores of wealth-tax have been already paid. Besides, Rs. 4.9 crores have been invested in specified securities.

5.15 While revised estimates of expenditure are not yet available, in view of the additional expenditure on account of D. A. increases, larger outlay on Central Plan, additional assistance to States for their Plans including specified irrigation and power projects, increased budgetary support to Public Sector Undertakings to fill their resource gaps, the budgetary expenditure is likely to be much higher than that envisaged in the original budget. At the same time it is possible to anticipate some economies in administrative expenditure following the declaration of Emergency. On the receipts side, as stated earlier the Voluntary Disclosure of Income and Wealth scheme has helped to augment revenues. The net market borrowings have also been substantially higher by about Rs. 128 crores than budget estimates and the small savings collections, as of now, are showing an encouraging trend compared to last year. External borrowings and grants taken credit for in the budget might well exceed the earlier estimates on present indications. While it is hazardous to guess the implications of all these

factors for the year-end budgetary deficit, in spite of buoyancy of receipts, the prevailing trend points to an increase in the deficit over that estimated in the original budget.

5.16 The provision for gross fixed capital formation in the Central budget showed an increase of 3.6 per cent in 1975-76 (BE) compared to an increase of 20.4 per cent in the 1974-75 (RE) over 1973-74 (Accounts). Including inventories, however, the gross capital formation would decline in 1975-76 by 11.4 per cent since the inventory build up in 1975-76 is expected to be much lower than in 1974-75 (RE). The Gross capital formation including financial assistance for capital formation in other sectors of the economy in 1975-76 (BE) which has been estimated at Rs. 3932 crores will be financed to the extent of Rs. 1044 crores (26.5 per cent) from gross savings generated by the Central Government and its departmental undertakings, Rs. 1780 crores (45.3 per cent) from savings mobilised from other domestic sectors and Rs. 861 crores (21.9 per cent) from foreign sources leaving a deficit of Rs. 247 crores (6.3 per cent) to be financed from short-term borrowings.

5.17 According to the functional classification, the expenditure on social and economic services which broadly adds up to the developmental outlays is estimated at Rs. 5353 crores and shows an increase of Rs. 441 crores or 9 per cent over 1974-75 (RE) and forms 51 per cent of the total expenditure as against 50 per cent of such expenditure in 1974-75 (RE).

TABLE 5.2
Capital Formation by the Central Government and its financing

	(Rs. crores)		
	1973-74 (Accounts)	1974-75 (RE)	1975-76 (BE)
I. Gross capital formation out of budgetary resources of the Central Government	2665	3579	3932
(i) Gross capital formation by the Central Government	782	1149	1018
(a) Gross fixed capital formation	711	856	887
(b) Increase in inventories	71	293	131
(ii) Financial assistance for capital formation to the rest of the economy	1883	2430	2914
II. Gross savings by the Central Government	585	807	1044*
III. Deficit (I-II)	2080	2772	2888
Financed by:			
IV. Draft on other sectors of the domestic economy	1588	1755	2027
(i) Domestic capital receipts	1165	1130	1780*
(ii) Budgetary deficit	423	625	247
V. Draft on foreign savings	492	1017	861
		(559)†	

* After taking into account the post-budget concessions.

† As per Accounts. Does not include RBI's transactions in long-dated securities.

Note: Gross capital formation in this table includes loans given for capital formation on a gross basis. Consequently domestic capital receipts include loan repayments to the Central Government.

Performance of Central Government Commercial Undertakings

5.18 The performance of Central Public sector undertakings has shown further improvement in 1974-75 with more undertakings joining the list of those giving a good account of themselves. The provisional operating results of 121 running enterprises during 1974-75 have indicated a total pre-tax net profit of Rs. 312 crores, which is more than twice the profit of Rs. 148.7 crores earned by 114 running concerns in 1973-74. While the enterprises making profits numbered 82 and accounted for a net profit of Rs. 451 crores, those incurring losses were 39 and their losses aggregated Rs. 139 crores. The major enterprises making pre-tax profits are Indian Oil Corporation (Rs. 52.14 crores); Oil and Natural Gas Commission (Rs. 50.77 crores); Bharat Heavy Electricals Ltd., (Rs. 48.53 crores); Hindustan Steel Ltd., (Rs. 48.24 crores); Mineral and Metals Trading Corporation (Rs. 44.08 crores); Shipping Corporation of India (Rs. 34.55 crores); State Trading Corporation of India (Rs. 18.61 crores) and Indian Petro-Chemical Corporation (Rs. 8.06 crores). Among those which incurred losses, the more important ones were Coal Mines Authority Ltd., (Rs. 36.11 crores); Bharat Coking Coal Ltd., (Rs. 26.12 crores); Neyveli Lignite Corporation (Rs. 11.77 crores); Bokaro Steel Ltd., (Rs. 11.65 crores); Heavy Engineering Corporation (Rs. 4.38 crores) and Fertilizer and Chemicals (Travancore) Ltd., (Rs. 3.06 crores). It will be seen that a major part of the losses has been sustained by coal enterprises. Coal prices were raised by an average of Rs. 10 per tonne in April, 1974 to meet the increased cost of production resulting from higher emoluments to labour following the decision to raise the minimum wage by about 50 per cent and from absorbing a large number of casual miners in the regular labour force after nationalisation. However, the increase in the price of coal could not fully neutralise the increased cost of production. In respect of other enterprises, the losses incurred are due to under-utilisation of installed and developed capacities and cost escalations.

5.19 The losses incurred by enterprises mentioned above, however, do not include the sick textile mills which have been constituted into 9 subsidiaries of the National Textile Corporation under the provisions of the Sick Textile Undertakings (Nationalisation) Act, 1974. According to the preliminary indications available, these 9 subsidiaries have incurred a net loss of Rs. 34.59 crores in 1974-75.

5.20 It may also be noted that the return on capital employed in the Central Government enterprises

viz., ratio of gross profits after providing for working expenses and depreciation but before deducting interest and tax-liability, shows a marked improvement from 5.2 per cent in 1973-74 to 7.8 per cent in 1974-75. The dividends declared by 33 enterprises in 1974-75 are also higher at Rs. 19.75 crores than Rs. 13.12 crores declared by 34 companies in 1973-74. Gross internal resources comprising retained profits, depreciation and deferred revenue expenditure written off during the year generated by 83 of the enterprises stood at Rs. 545 crores compared to Rs. 387 crores in 1973-74. Notwithstanding the higher utilisation of capacity by all major enterprises, they have been successful in bringing down the level of inventories from 4.3 months' to 4.1 months' cost of production. Considering the power cuts, labour unrest, transport difficulties, shortage of raw materials etc., experienced by the enterprises in 1974-75, this is no small achievement.

5.21 On present indications, the Central Government public undertakings are poised for even better results in 1975-76. In real terms the weighted average rate of growth of production in them during April-December, 1975 has registered an increase of 15 per cent over that during the same period last year. In consequence, the provisional operating results during the first half of 1975-76 of major public sector enterprises have exceeded the targets set for them.

5.22 Several unfavourable factors such as a decline in originating freight traffic and passenger traffic, payment of three instalments of additional dearness allowance sanctioned to the employees and escalation in costs of operation resulted in the railways deficit going up in the revised estimates to Rs. 128 crores from Rs. 53 crores in 1974-75 (BE). The railway budget for 1975-76, however, anticipated a surplus of Rs. 23.03 crores after taking credit for Rs. 39 crores of additional yield from an upward revision in tariffs on transporting foodgrains (including pulses), iron ore and manganese ore for export, but did not allow for expenditure on additional dearness allowance which had fallen due. However with the subsequent sanction of five instalments of additional dearness allowance to the railway employees and further increase in operational costs due to the increase in coal prices in the post-budget period, it would appear that the anticipated surplus would be converted into a substantial deficit. Despite some improvement in gross earnings consequent upon an increase in originating freight traffic and passenger traffic during the first half of the current fiscal year, on present indications, it might be difficult for the increased revenues to fully offset additional expenditure arising out of additional dearness allowance payments to railway employees and increase in operating costs.

5.23 The finances of the Department of posts and telegraphs, which were showing a healthy trend until recently have, of late, come under strain due to rising expenses. As a result, the revised estimates for 1974-75 have scaled down the surpluses envisaged in that year's budget estimates from Rs. 64.84 crores to Rs. 24.56 crores. With an additional expenditure of about Rs. 52 crores anticipated for 1975-76 and a normal growth in revenue of about Rs. 42 crores, the surpluses expected for 1975-76 from the posts and telegraphs department was only Rs. 14.52 crores. However, with further increases in working expenses resulting mainly from the increase in additional dearness allowance payments in the post-budget period, the surplus anticipated at the time of the presentation of the budget is unlikely to be realised. Posts and telegraph rates have been raised from 1st March 1976 to cover cost escalations and the revenue impact of these revisions will mainly accrue in the next financial year.

Finances of the State Governments in 1975-76

5.24 In contrast to the slackness shown by most of the State Governments in the mobilisation of additional resources in the Fourth Plan period, their efforts in this direction in the first two years of the Fifth Plan have been commendable. The measures undertaken by them in 1974-75 yielding Rs. 358 crores in that year are expected to yield an additional revenue of Rs. 634.62 crores in 1975-76 and Rs. 703.89 crores in 1976-77. The fresh measures undertaken by them in the current year are estimated to yield Rs. 197.89 crores in 1975-76 and Rs. 308.39 crores in 1976-77. These efforts of the States at additional resource mobilisation augur well for financing their development plans, but having regard to their growing commitments on non-developmental expenditures and the escalations in the costs of irrigation and power projects, the States will have to exercise considerable financial discipline and intensify their efforts at resource mobilisation, if they are to sustain Plan outlays at higher levels in the coming years. Besides, the additional resource mobilisation efforts of the States have still not adequately touched the affluent sections of the farm sector, which has benefited the most from the massive investments in agriculture made under the Plans.

5.25 As a result mainly of the additional resource mobilisation efforts, the combined budgetary deficit of the States in 1974-75 came down to Rs. 30 crores from Rs. 175 crores in 1973-74. Though their combined budgetary deficit for 1975-76, as shown in their budgets, is of the order of Rs. 65 crores, the current indications are that the State budgets taken together might end the year with a surplus consequent upon

the share from increased income tax collections as well as from the share in the income tax collected on the incomes disclosed under the Voluntary Disclosure Scheme.

5.26 According to budget estimates for 1975-76 presented to their legislatures, the combined revenue and capital expenditure of the State Governments at Rs. 8115 crores, would increase by 6.4 per cent over 1974-75 (RE). Whereas non-development expenditures at Rs. 2436 crores are up by 10.8 per cent, development expenditures at Rs. 5679 crores have shown a modest rise of 4.7 per cent. The increase in non-developmental expenditures have been due mainly to rise in interest payments and increased outlay on fiscal and administrative services, including pensionary benefits following the revised scales of pay in some States and additional dearness allowance payments. Increases in developmental expenditures are mainly concentrated in the field of agriculture and allied services, power and major irrigation, in keeping with the general objective of strengthening the core sectors of the economy. Thus the step-up in the expenditure on the agricultural sector has been from Rs. 816 crores in 1974-75 (RE) to Rs. 965 crores in 1975-76 (BE); and outlay in the irrigation and power sector, has increased from Rs. 573 crores in 1974-75 (RE) to Rs. 608 crores in 1975-76 (BE). These increases have been marginally offset by declines in other development expenditures and a considerable fall in gross loans disbursed. Considering further the special advance plan assistance given recently to the States for selected irrigation and power projects, development outlay as a whole would be higher than envisaged in their budgets.

5.27 Current revenues of the States and the Union Territories are expected to increase by 8.2 per cent to Rs. 6475 crores in 1975-76 (BE) as against an increase of 14.8 per cent to Rs. 5986 crores in 1974-75 (RE). While total tax revenue is expected to increase from Rs. 3987 crores in 1974-75 (RE) to Rs. 4440 crores in 1975-76 (BE)—an increase of 11.4 per cent—taxes raised by the States (excluding their share in Central Taxes) show a slightly higher rate of growth at 12.9 per cent both because of the full impact of the large additional tax effort resorted to in 1974-75 as well as due to fresh tax effort in the current year. Major State taxes showing substantial increases are land revenue, general sales tax, stamps and registration, taxes on vehicles, entertainment tax, and taxes on goods and passengers, which together account for more than 67 per cent of the total increase of Rs. 453 crores in tax revenues in 1975-76. Non-tax revenues, however, show a decline from Rs. 943 crores in 1974-75 (RE) to Rs. 917 crores in 1975-76 (BE).

5.28 The share of States in the Central taxes, namely, Central excises and income tax, has increased from Rs. 1217 crores in 1974-75 (RE) to Rs. 1315 crores in 1975-76 (BE) representing an increase of 8.1 per cent. While Central grants for plan and non-plan purposes have also shown a rise, the increase has been only of the order of 6 per cent, from Rs. 1056 crores in 1974-75 (RE) to Rs. 1118 crores in 1975-76 (BE). After taking credit for these receipts, the gap to be filled by borrowings has been budgeted at Rs. 1640 crores in 1975-76 (BE) which is almost the same as in 1974-75 (RE). In financing this gap, the States have taken a net credit for loans from the Central Government and market borrowings at Rs. 929 crores. Unfunded debt, loans from funds administered by the Reserve Bank and miscellaneous capital receipts together are expected to bring Rs. 646 crores, leaving a budgetary deficit of Rs. 65 crores to be financed by ways and means advances from the Reserve Bank and drawing down of cash balances.

State Governments' Commercial Undertakings

5.29 Last year's Economic Survey had pointed out that except for forests, mines and minerals, the major commercial undertakings of States like irrigation and electricity continued to incur heavy losses which seriously eroded the resources that the States could make available for investment. Consequently, there has been an increasing reliance by the States on the Centre for expanding investment even in these priority sectors.

5.30 It is a matter of concern that the revenue from irrigation rates levied presently is proving insufficient even to meet the maintenance and operational expenditure on irrigation works. This in effect means that the irrigation sector is being subsidised. Since only about a quarter of the area under crops has been brought under irrigation, any subsidy to irrigation would benefit only a small section of the population and the resulting burden has to be borne by other sectors including farmers without irrigation facilities. The information regarding the present practices of levy of irrigation rates by different States brings out the wide divergence both in the system of levy as well as the rates themselves. It appears that the rates are fixed largely on an *ad hoc* basis resulting in multiplicity of systems. Having regard to these facts, it needs to be emphasised that the State Governments, as an immediate measure, need to increase irrigation water rates for earning adequate revenues to cover the working expenses taking into account all types of irrigation works i.e., major, medium, minor, lift etc. It is with this objective in view that the Central Government, while sanctioning advance plan assistance to the States this year for selected irrigation projects, has stipulated

that the States should take positive steps in this direction. Once this objective is achieved, the State Governments should endeavour to earn progressively increasing returns on the capital invested in these projects.

5.31 The working results of State Electricity Boards are in no better position than those of the commercial irrigation projects of the State Governments. Despite the revision in tariff rates by many State Electricity Boards both in 1974-75 and during the current year, the increase in revenues has been barely sufficient to cover the escalation in operational and maintenance costs. In 1974-75 the losses of the State Electricity Boards were around Rs. 175 crores. Their financial results for 1975-76 appear to be no better. Generation of electricity itself was below capacity in 1974-75 due to inadequate inflows into hydel reservoirs following poor rainfall. Generation of thermal power also suffered due to frequent breakdowns following poor maintenance of the plants. While these problems are incidental to electricity generation, the poor financial results of the Electricity Boards are also due to their uneconomic tariff rates and operational inefficiency. Loans advanced by the State Governments to the State Electricity Boards by the end of 1974-75 exceeded Rs. 3500 crores. Besides, State Electricity Boards also borrow directly by issue of bonds and during 1974-75 such borrowings amounted to Rs. 120 crores. The financial position of the State Electricity Boards can be judged from the fact that many of them have been unable to pay full interest on their loans to the State Governments. This has imposed a heavy burden on the State finances which are already under severe strain and has affected further investment in new power projects.

5.32 The reasons for the losses sustained by the Electricity Boards are manifold. Firstly, cost escalations have not been fully neutralised through tariff revisions with the result the large scale users of power such as medium and large scale industries which account for two-thirds of total power consumption are being subsidised. Secondly, there has been a spectacular increase in power consumption in the agricultural sector, but in most of the States agriculture tariff is palpably low and losses currently incurred on rural electrification are thus in the nature of concealed subsidies. Besides, the transmission losses in a number of States continue to be abnormally high. The so-called power losses are reported to be partly due to theft of power by small and big consumers alike. It is for the State Governments to study the various problems confronting the Electricity Boards and take remedial measures to overcome them. In order to raise adequate resources for new power projects and for expansion of

existing ones, there is need to initiate measures so that the Electricity Boards meet the norms adopted by the Sixth Finance Commission and earn an adequate surplus to pay full interest on the loans advanced to them by the States after meeting their operational and depreciation expenses. With the ever growing demand for power it is equally important for the Electricity Boards to move towards the objective of earning adequate return on the capital invested so as to enable them to make further investments in power generation.

5.33 State Governments have also made substantial investment in road transport, particularly passenger transport. Here again, with proper management and appropriate fare structure it should be possible for the State Governments to step up substantially the rates of return being currently earned by them on the investments made in Road Transport Undertakings.

Towards a More Rational Tax Structure

5.34 In the last five years, considerable effort has been made by the Government both at the Centre as well as in the States to raise revenue through taxation. Revenue from taxes levied by the Centre has increased from Rs. 3207 crores in 1970-71 to Rs. 6128 crores in 1974-75* and revenue from State taxes has also increased from Rs. 1545 crores to Rs. 2761 crores during the period. The ratio of taxes to national income is estimated at 14.8 per cent in 1974-75 as against 13.8 per cent in 1970-71. However, in recent years considerable difficulty has been experienced in raising resources through further taxation. One important reason for this outcome has been the sluggishness of the industrial sector which contributes the major share of Government revenue. Another important factor at work has been the lack of adequate elasticity of revenues from major tax sources.

5.35 Taking Central excise which accounts for a major part of the Centre's tax revenue, rough calculations show that over the period 1960-61 to 1973-74, the co-efficient of elasticity of revenue from this source with reference to net national product at current prices (factor cost) was around 0.7**, although, because of additional taxation, the buoyancy of Central excise revenue (that is, the growth of actual revenue relative to NNP) was 1.4. The automatic response of excise taxation to changes in gross value of manufacture and in value added by manufacture is also found to be poor (the elasticity co-efficient being 0.50 and 0.61 respectively). Moreover, since the public sector has emerged as a major consumer of many excisable commodities, the net increase in financial resources corresponding to any given increase in excise taxation has tended to diminish. If therefore, Government revenue from commodity taxation is to keep pace with growth of income without necessitating repeated increase in rates and coverage, measures have to be taken to improve the built-in-elasticity of the excise duties. Besides, the combined operation of Central excise and sales tax has at times led to unintended incidence of taxation on commodities. It is necessary to take a look at the entire structure of indirect taxation in the country so as to avoid or to minimise any undesirable effects on prices and distortions in the allocation of resources.

5.36 As for the direct taxes, while it is desirable to intensify efforts to check evasion, one has to take into account the impact of progressive taxation of income and wealth on the flow of savings and investment in the economy. Given the structure of income and wealth distribution in our country, taxation of income at high rates by itself does not necessarily reduce private consumption. There is need to reform the structure of direct taxation in such a way as to gear it towards promotion of savings and investment without sacrificing the objective of reducing inequalities.

* Provisional data.

**The co-efficient of elasticity of tax revenue is derived by dividing the percentage change in revenue at constant rates of tax by the percentage change in income or other aggregate chosen. By contrast, the buoyancy coefficient is derived by dividing the percentage change in revenue (due both to additional taxation as well as normal growth at constant rates) by the percentage change in income or other aggregates.