Tax measures

a) Direct taxes

2.12 In order to provide medium term-stability and predictability, Budget 2006-07 kept the tax rates moderate and stable, and no change in the rates of personal income tax or corporate income tax was proposed. No new taxes were imposed. However, for equity, there were marginal revisions in certain tax rates. The rate under Minimum Alternate Tax (MAT) was increased from 7.5 per cent of book profits to 10 per cent. Long-term capital gains arising out of securities and subject to Securities Transaction Tax were also included in calculating book profits. MAT-paying companies were allowed the credit for MAT over seven years instead of the five years allowed earlier. Adjustment of MAT credit was also allowed while calculating interest liability. Major initiatives in the field of direct taxes, particularly personal income tax, had been initiated in 2005-06 itself. These included having, through a general rebate on savings in any approved instrument up to Rs.1 lakh, neutrality of taxes between forms of savings. Budget for 2005-06 had also introduced two new taxes: a fringe benefit tax targeted at those benefits enjoyed collectively by the employees and not attributable to individual employees, which are to be taxed in the hands of employer;

and a tax on banking cash transactions (withdrawals) over a certain threshold in a single day. In Budget 2006-07, some of the concerns/anomalies in these taxes were addressed (Box 2.1).

b) Indirect taxes

2.13 As part of continuous process of bringing about a moderate, rational and simplified tax structure and to align them with ASEAN levels as per pre-announced commitments, the peak rate of customs duty on non-agricultural products was reduced from 15 per cent to 12.5 per cent in 2006-07 with a few exceptions (Box 2.2). Commodity taxes have been important

Box 2.1 : Budget 2006-07 - Rationalisation of Direct Taxes

- In order to tax unaccounted money being contributed to charitable and religious organizations by way of anonymous donations, such donations brought to tax at the rate of 30 per cent in the hands of certain charitable and religious organizations in certain cases. Wholly religious organizations have been kept out of the purview of this provision.
- Section 10(23G) of the Income Tax Act exempted certain income of an infrastructure capital fund/ company/co-operative bank from investments made on or after June 1, 1998, in any enterprise or undertaking engaged in infrastructure projects or other eligible business. The section omitted so as to make income from existing as well as future investments in infrastructure projects taxable.
- Exemption available to any income of a notified Investor Protection Fund restricted to any income by way of contributions received from recognized stock exchanges and the members thereof.
- Exemption provided to any specified income arising to a notified non-profit body or authority established, constituted or appointed under a treaty or agreement entered into by the Central Government with two or more countries or a convention signed by the Central Government.
- To plug revenue leakages, interest not treated as actual payment not to be allowed as deduction in the computation of income of a business concern.
- The provisions of Section 54EC of the Income-tax Act amended so as to restrict the benefit of tax exemption in respect of long-term capital gains invested in the notified bonds of National Highways Authority of India (NHAI) and Rural Electrification Corporation Limited (REC).
- In Budget 2005-06, the provisions relating to savings were recast. However, fixed deposits in banks were not included as one of the avenues of savings in terms of Section 80C. Considering the demand fixed deposits in scheduled banks for a term of not less than five years were included in Section 80C of the Income Tax Act, 2006. Further, the limit of Rs. 10,000 in respect of contribution to certain pension funds in Section 80CCC was removed, subject to the overall ceiling of Rs. 1,00,000 as prescribed under section 80CCE.
- Primary Agricultural Credit Societies (PACS) and Primary Cooperative Agricultural and Rural Development Banks (PCARDB) continue to be exempt from tax under Section 80P of the Income Tax Act, while other cooperatives were brought under tax net.
- Income Tax Act amended to provide for compulsory obtaining of the permanent account number (PAN) before entering into prescribed transactions, and also to allot PAN suo moto in certain cases.
- As a procedural simplification, annexure-less return forms introduced so that returns could be furnished electronically. New return forms made compulsory for corporate taxpayers.
- The rates of STT been increased by 25 per cent in respect of all transactions chargeable to STT.
- Rationalisation of provisions of FBT done by making the following changes:
  - Valuation of the fringe benefit arising from 'tour and travel' reduced to 5 per cent from 20 per cent;
  - Valuation of the fringe benefit arising from 'hospitality' and 'use of hotel boarding and lodging facilities', in the case of airline companies and shipping industry, reduced to 5 per cent from 20 per cent;
  - Exclusion of the expenses on free samples of medicines and of medical equipment distributed to doctors;
  - Exclusion of the expenses incurred on brand ambassador and celebrity endorsement; and
  - Contribution by an employer to an approved superannuation fund in excess of Rs. 1,00,000 per year for an employee to attract the provisions of FBT.

instruments for management of prices, neutralising the disadvantages to domestic industry because of domestic taxes, removing anomalies in duty structure and strengthening competitiveness of domestic industry. Extension of countervailing duties (CVD) on all imported goods; reduction in duty of metals and other intermediate products; and withdrawal of exemptions to lend simplicity to the tax laws, were some of the important measures taken in Budget 2006-07. The structural shift of the taxes in favour of direct taxes was in line with the policy of removal of price distortions.

2.14 The current year has been characterised by inflationary pressures, initially upon, primary articles and fuels, but subsequently also on manufactured products. The moderation in inflation in the fuel group, with a reduction in international oil prices, from 7-9 per cent up to September 2, 2006 to 3.7 per cent in January 2007, was more than neutralised by the acceleration in inflation in primary articles and manufactured products. Along with the administrative measures, fiscal measures to combat inflation have included duty reduction in some of the items under heavy inflationary pressures. Customs duty of wheat and pulses were reduced to zero in June 2006. Duty on edible oils, particularly the palm group of oils was reduced by 10 percentage points each in August 2006 and January 2007. Duty on portland cement and metals was also reduced in January 2007.

2.15 Performance of revenues from excise duty, which had been quite disappointing with growth of such revenues declining steadily from 13.4 per cent in 2002-03 to 10.3 per cent and 9.2 per cent in the two subsequent years, revived somewhat to 12.8 per cent in 2005-06. Among others, three factors, which have had - and continue to have - a major bearing on excise duty collection, are: area-based excise duty exemptions, small-scale industries' (SSI) excise duty exemption scheme, and the low rates on selected products. Budget 2006-07, while projecting a modest growth in excise duty revenues of 6.3 per cent, took some important steps in redressing these root causes (Boxes 2.3 and 2.4)

Tax expenditure

2.16 Tax expenditure in 2006-07 is estimated at Rs. 1,00,147 crore. Such exemptions and incentives distort resource allocation and stunt productivity. They also result in multiplicity of rates, legal complexities, classification disputes, litigation, higher cost of tax compliance and administration. Such exemptions have been justified in the past for promoting balanced regional growth; dispersal of industries; neutralization of disadvantages on account of scale of operation and location; and incentives to priority sectors including infrastructure. Furthermore, tax exemptions often create pressure groups for their perpetuation, and rent seeking can be avoided only by subjecting such exemptions to a sunset clause.

2.17 Based on a comprehensive review of the tax exemptions, 8 such exemptions in customs duties, 68 in central excise duties and 6 in service taxes were withdrawn in Budget 2006-07. Simultaneously, on the direct tax side, tax benefits available to certain cooperative banks and for income from investment in infrastructure and certain other eligible businesses were also withdrawn. Further, the Department of Revenue has posted on its website select tax exemptions/incentives currently available for eliciting the views of the stakeholders and to generate an informed debate regarding their continuance.

Service tax - a promising source of revenue

2.18 The gradual expansion of the service tax, introduced in 1994-95 to redress the asymmetric and distortionary treatment of goods and services in the tax regime, has been a buoyant source of revenue in recent years. The number of services liable for taxation was raised from 3 in 1994-95 to 6 in 1996-97, and then gradually to 99 in 2006-

Box 2.2 : Budget 2006-07 - Rationalisation of Basic Customs Duties

- The peak rate of duty on non-agricultural products reduced from 15 per cent to 12.5 per cent. Ad-valorem component of duty on textiles fabrics and garments also reduced to 12.5 per cent.
- Budget 2005-06 had introduced special additional duty of customs at 4 per cent to partly make up for the corresponding domestic levies and to start with, this duty had been imposed on ITA (Information Technology Agreement)-bound items and on specified inputs/raw materials used for manufacture of electronics/information technology items. Budget 2006-07 extended this duty to all imported goods, with a few exceptions.
- Duty reduced from 10 per cent to 7.5 per cent on primary and semi-finished forms of metals, viz., alloy steel, aluminium, copper, zinc, ashes and residues of copper and zinc, tin, base metals of Chapter 81 (such as tungsten, magnesium, cobalt, and titanium).
- Duty on ores and concentrates reduced from 5 per cent to 2 per cent.
- Duty on mineral products, except for marble, granite, asbestos and cement reduced from 15 per cent to 5 per cent.
- Duty on refractories and raw materials for refractories reduced from 10 per cent to 7.5 per cent.
- Duty reduced from 15 per cent to 10 per cent on halogens, sulphur, carbon, hydrogen, and methanol; and from 10 per cent to 5 per cent on organic chemicals. Duty on polymers of ethylene (LDPE, LLDPE, HDPE, LHDPE, LMDPE), polymers and copolymers of propylene, polymers and copolymers of styrene and polymers of vinyl chloride and ethyl vinyl acetate duty on catalyst reduced from 10 per cent to 5 per cent. Duty on styrene, ethylene dichloride and vinyl chloride monomer reduced from 5 per cent to 2 per cent. Duty on naphtha for manufacture of specified polymers reduced from 5 per cent to nil.
- Duty increased from 30 per cent to 60 per cent on honey and from 30 per cent to 80 per cent on vanaspati, bakery shortening, inter-esterified, elaidinised fats, margarine and similar boiled, oxidized, dehydrated, sulphurised, blown, polymerized or modified preparations of edible grade.
- Duty reduced from 15 per cent to 10 per cent on man made fibers, filament yearns, spun yearns, specified textile machinery and parts for manufacture of such machinery and also on textile intermediates. Duty on paraxylene has been reduced from 5 per cent to 2 per cent.
- Duty on set top boxes unified at nil basic customs duty plus 16 per cent CVD plus 4 per cent special additional duty of customs.
- Duty reduced from 10 per cent to 5 per cent on naphtha and petroleum coke. Duty on natural gas, including propane and butanes, unified at 5 per cent.
- Duty on 14 specified anti-cancer, 10 specified anti-AIDS and four other specified drugs with bulk drugs for their manufacture, and two specified diagnostic kits and one equipment, reduced to 5 per cent with nil CVD.
- Duty on vinyl acetate monomer; butyl rubber; metallurgical grade silicon; borax/boric acid; potassium chloride reduced from 15 per cent to 10 per cent.
- Duty on non-edible grade oils having free fatty acid content of 20 per cent or above, and used for manufacture of soaps, industrial fatty acids and fatty alcohols reduced from 15 per cent to 12.5 per cent, and on crude glycerine from 30 per cent to 12.5 per cent.
- Duty on cullet (broken glass); parts of pens; phenol/acetone, for manufacture of bisphenol-A; packaging machinery reduced from 15 per cent to 5 per cent. Duty on bisphenol-A and epichlorohydrin for manufacture of epoxy resins reduced from 10 per cent to 5 per cent.
- Duty reduced from 5 per cent to nil on parts of hearing aids.

Withdrawal Of Exemptions

- Duty exemptions/concessions withdrawn on following items: saddle tree; parts of outboard motors imported by specified agencies; spare parts of maintenance of textile machinery; video cassettes and video tapes; food products (excluding alcoholic preparations) imported by hotels/tourism industry in terms of licenses issued under 1997-2002 Exim Policy; plant, machinery, equipment imported for setting up of Currency Note/ Bank Note Press.
- Exemption from CVD withdrawn on specified goods for setting up of a unit with an investment of Rs.5 crore or more for manufacture of capital goods.

Box 2.3 : Budegt 2006-07 – Rationalisation of Central Excise Duties

A. Relief Measures:

I. Duty on aerated waters; petrol cars with length not exceeding four meters and engine capacity not exceeding 1200 cc; diesel cars with length not exceeding four meters and engine capacity not exceeding 1500 cc reduced from 24 per cent to 16 per cent.

II. Duty on heat-resistant latex rubber thread; LPG gas stoves of value exceeding Rs. 2,000 per unit; compact fluorescent lamps; footwear of retail sale price between Rs. 250 and Rs. 750 per pair reduced from 16 per cent to 8 per cent.

III. Paddy de-husking rice rubber rolls; nuclear-grade sodium produced by Heavy Water Board for supply to Kalapakkam Nuclear Power Plant; drawing inks; quebracho and chestnut extract; gold concentrate for refining exempted from duty.

IV. Duty on specified printing, writing and packing paper reduced from 16 per cent to 12 per cent.

B. Imposition and increase:

I. Duty of 8 per cent with CENVAT credit imposed on goggles; articles of wood, registers; accounts books, receipt books, letter pads, memorandum pads, dairies, binders, folders, file covers, etc (excluding note books and exercise books); paper labels; paper pulp moulded trays; articles of mica; goods containing at least 25 per cent by weight of fly ash/phosphor-gypsum; roofing tiles; raw, tanned or dressed fur skins; portable receivers for calling, alerting and paging; henna powder which is not mixed with any other ingredient; 100 per cent wood-free plain or pre-laminated particle or fibreboard made from sugarcane bagasse or other agro-waste; parts of walking-sticks, seat-sticks, whips, riding-crops and the like; parts of drawing and mathematical instruments; and frames and mountings for spectacles, goggles or the like having value below Rs. 500 per piece.

II. Duty of 16 per cent imposed on umbrellas, sun umbrellas and their parts; food preparation intended for free distribution subject to end-use certification (food products, in general, are exempted unconditionally from excise duty); soap manufactured under a scheme for sale of Janata soap; strips and tapes of polypropylene used in the factory of its production in the manufacture of polypropylene ropes; parts and components of motor vehicles transferred to a sister unit for manufacture of goods falling under chapter 87; goods (other than electrical stampings and laminations, bearings and winding wires) supplied for manufacture of PD pumps of handing water; specified goods meant for display in any fair or exhibition in India; parts of table ware, kitchenware and other household articles made of iron & steel, copper, aluminium; railway track machines; sulphur; mixture of graphite and clay for manufacture of pencils and pencil leads; aluminium ferrules for manufacture of pencils; tobacco used for smoking through 'hookah' or 'chilam' and 'gudaku'. Sulphur for fertilizers has been exempted from excise duty.

III. Duty raised from 8 per cent to 16 per cent on mosaic tiles; glassware; lay flat tubing ; and cigarette filter rods. The rate of compounded levy on stainless steel patti/pattas has been increased from Rs. 15000/- per machine to Rs. 30000/- per machine.

C. Miscellaneous:

I. Exemption withdrawn for the unbranded goods like wadding, gauges, protein concentrates, textured protein substances, churan for pan, custard powder, and mineral water.

II. Exemption of goods manufactured without the aid of power removed from items such as essential oils, perfumes and toilet waters, blocks, ceramic tiles, metal containers of iron, steel and aluminium.

III. Exemption available on raw materials for manufacture of rotor blades of wind operated energy generators, extended to all glass fiber items and resin binders.

IV. Generic exemption withdrawn from products of coir industry, cashew industry, tanning industry, oil mill and solvent extraction industry and rice industry.

07. Simultaneously, the rate of tax was raised from 8 per cent to 10 per cent in 2004-05, and further to 12.0 per cent in 2006-07. Revenue from service tax, as the combined outcome of expanding tax net, creeping rate, and buoyant service sector growth, increased rapidly from a paltry Rs. 407 crore in 1994-95 to Rs. 14,200 crore in 2004-05. In 2005-06 (Prov.), service tax revenue was Rs. 23,055 crore (Table 2.4). Budget 2006-07 took some significant steps in rationalising the service tax regime (Box 2.5).

Box 2.4 : Budget 2006-07 – Changes in Commodity-Specific Excise Duties

Food processing:

- Duty reduced from 16 per cent to nil on condensed milk, ice cream, pectic substances, pectinates and pectates, pectin esterase, yeast and pasta.
- Duty reduced from 16 per cent to 8 per cent on ready to eat packaged food, texturised vegetable protein (soya bari), and instant food mixes, namely, pongal mix, vadai mix, pakora mix, payasam mix, gulab jamun mix, rava dosa mix, idli mix, dosai mix, murruku mix and kesari mix.
- Processed meat, fish and poultry products exempted from duty.

Petroleum:

- The general rate of cess applicable on domestic petroleum crude oil under the Oil Industry (Development) Act, 1974 increased from Rs. 1,800 per tonne to Rs. 2,500 per tonne.

Tobacco products:

- Duty rates unified at 66 per cent for all types of Pan Masala.
- Specific rates of excise duty on cigarettes revised.

Textiles:

- Duty on all man-made (like polyester, nylon, viscose and acrylic) fibers and filament yarns reduced from 16 per cent to 8 per cent

Small-scale industries (SSI):

- SSI exemption available to power-driven pumps restricted to only pumps conforming to prescribed BIS Standards.

Information technology:

- Excise duty of 12 per cent and 8 per cent imposed on computers and packaged software on electronic media, respectively.
- Set top boxes not covered under the Information Technology Agreement subjected to 16 per cent duty.
- Storage devices, namely, DVD-drives, flash drives and combo drives, exempted from duty.
- Excise duty on MP3 and MPEG4 players reduced from 16 per cent to 8 per cent

Export-oriented units

- Duty on clearances of goods to Domestic Tariff Area (DTA) from Export Oriented Units (EOU), Software Technology Parks, Electronic Hardware Technology Parks, etc. changed from 50 per cent of aggregate customs duties to 25 per cent of the basic custom duty plus excise duty payable on like goods.

Retail sale price (RSP) based assessment:

- RSP-based assessment extended to parts, components and assemblies for automobiles, plant growth regulators, and toothbrushes.
- Abatement from RSP for levy of excise duty reduced from 45 per cent to 42.5 per cent on aerated waters and 40 per cent to 37 per cent on compact fluorescent lamp, footwear of RSP between Rs. 250 to Rs. 750 per pair, ready to eat packaged food, and instant food mixes.
- Existing rate of abatement of 50 per cent to apply to all varieties of pan masala, which are subject to RSP based assessment.

Expenditure trends

2.19 The NCMP has pledged to raise the level of public spending in education to at least 6 per cent of GDP, and on health to at least 2-3 per cent of GDP in a phased manner. Further, it attaches highest priority to the development and expansion of physical infrastructure like roads, highways, ports, power, railways, water supply, sewage treatment and sanitation through higher public investment, even as the role of the private sector is expanded. This has to be accomplished in an overarching framework of fiscal consolidation. With about 86 per cent of the revenue receipts in 2005-06 appropriated by committed expenditure like interest payments, subsidies, pay, pensions and defence, expenditure reprioritization needs to be calibrated through higher allocation of incremental revenue towards the NCMP objectives.

2.20 FRBMA stipulates that public expenditure must be reoriented for the creation of productive assets. Given the existing classification of expenditure, plan expenditure and capital expenditure are the

Table 2.4 : Service Tax–A Growing Revenue Source					
Year	**No of services**	**Number of assessees**	**Tax rate in per cent**	**Revenue (In rupees crore)**	**Growth in per cent**
1994-95	3	3,943	5.00	407	…
1995-96	3	4,866	5.00	862	111.8
1996-97	6	13,982	5.00	1,059	22.9
1997-98	15	45,991	5.00	1,586	49.8
1998-99	26	107,479	5.00	1,957	23.4
1999-00	26	115,495	5.00	2,128	8.7
2000-01	26	122,326	5.00	2,613	22.8
2001-02	41	187,577	5.00	3,302	26.4
2002-03	52	232,048	5.00	4,122	24.8
2003-04(with effect from May 14, 2003)*	60	403,856	8.00	7,891	91.4
2004-05 (with effect from September 10, 2004)*	75	740,267	10.00	14,200	80.0
2005-06 (Prov.)	84	805,591	10.00	23,055	62.4
2006-07 (BE) (with effect from April 18, 2006)*	99	…	12.00	34,500	49.6

*** The date mentioned in parentheses after 2003-04, 2004-05 and 2006-07 is the date from which the number of services under service tax increased from the previous year.**

Source : Department of Revenue, Ministry of Finance.

closest approximation to expenditure for creation of productive assets. As a proportion of GDP, plan expenditure, after declining from 5.0 per cent in 1990-91 to 3.8 per cent in 1998-99, again started rising to reach 4.5 per cent in 2002-03 before declining to 3.9 per cent in 2005-06. Plan expenditure was budgeted to increase by 20.4 per cent over 2005-06 (BE) to 4.2 per cent of GDP in 2006-07. Non-plan expenditure, after recording a year-on-year growth of 15.6 per cent in each of the two years of 2002-03 and 2003-04, witnessed a moderation in growth in 2004-05 and 2005-06. While non-plan expenditure in fact had declined in 2005-06 (prov.), in 2006-07, an increase of 5.5 per cent in such expenditure was proposed over 2005-06(BE). As a proportion of GDP, non-plan expenditure followed a pattern similar to that of plan expenditure. It fell from 12.3 per cent of GDP in 1990-91 to reach 10.0 per cent in 1996-97. The proportion rose again to reach 11.4 per cent in 2001-02 and further to 12.6 per cent in 2003-04. The proportion, which is expected to have declined to 10.2 per cent of GDP in 2005-06 (prov.), was budgeted at 9.5 per cent of GDP in 2006-07.

2.21 The Constitution requires revenue and capital expenditures to be shown separately in the budget. Article 112 (2) states: "The estimates of expenditure embodied in the annual financial statement shall show separately - (a) the sums required to meet expenditure described by this Constitution as expenditure charged upon the Consolidated Fund of India; and (b) the sums required to meet other expenditure proposed to be made from the Consolidated fund of India, and shall distinguish expenditure on revenue account from other expenditure." The same provision is repeated under Article 202 under the State Section. The distinction between revenue and capital expenditures not only is a Constitutional requirement but also an essential ingredient for policy formulation and efficient resource allocation. FRBMA 2003 highlights the significance of keeping the revenue expenditure under control and envisages elimination of the revenue deficit by the end of 2008-09.

Box 2.5 : Budget 2006-07 – Service Tax

New Services added

- Service provided by a Registrar to an issue;
- Service provided by Share Transfer Agent;
- Automated Teller Machine operations, maintenance or management;
- Service provided by recovery agent;
- Sale of space or time for advertisement, other than in print media;
- Sponsorship services provided to anybody, corporate or firm, other than sponsorship of sports events;
- Transport of passengers, other than economy class passengers, embarking on international journey by air;
- Transport of goods in containers by rail by any person, other than Government railway;
- Business support services;
- Auctioneers' service, other than auction of property under directions or orders of a court of law or auction by the Central Government;
- Public relation service;
- Ship management service;
- Internet telephony service
- Transport of persons by cruise ship;
- Credit card, debit card, charge card or other payment card related services.

Exemption withdrawn

- In relation to general insurance where -- premium is received from re-insurance, both domestic and overseas, and business for which premium is booked outside India;
- For services, other than accounting, auditing and statutory certification services, provided by practicing chartered accountant, company secretary or cost accountant in her professional capacity;
- For taxable services provided by a Call Centre or a Medical Transcription Centre;
- For services provided in relation to Enterprise Resource Planning (ERP) software system provided by a management consultant in connection with the management of any organization;
- For catering services provided on railway train by an outdoor caterer;
- For catering services provided within the premises of an academic institution or medical establishment by an outdoor caterer.

Exemption granted

- For financial leasing services including equipment leasing and hire-purchase, on that portion of the taxable value comprising of 90 per cent of an amount representing as interest, i.e., the difference between the instalment paid towards repayment of the lease amount and the principal;
- For testing and analysis services provided in relation to water quality testing by Government-owned State and district level laboratories;
- For all taxable services provided by Reserve Bank of India.

2.22 Broadly, revenue expenditure is expenditure incurred for purposes other than creation of assets of the Central Government. In many countries, it is known as current expenditure. Revenue deficit is the difference between revenue expenditure and revenue receipts. Broadly, the revenue deficit indicates the excess of current expenditures over revenues, or dis-savings by the Government, while the fiscal deficit captures the excess of overall expenditure over revenue. Revenue deficit implies an increase in the liabilities of the Central Government without corresponding increase in its assets. The existence of revenue deficit indicates a departure from the observance of the golden rule of public finance whereby all borrowings by the Government is for financing public investment. When the focus is only on reducing the fiscal deficit, the brunt of fiscal correction is often borne by compression in capital expenditure. The change in revenue deficit on the path of fiscal adjustment indicates the quality of fiscal correction, which is as important as the level of fiscal correction itself.

2.23 As a proportion to GDP, capital expenditure declined from 4.4 per cent in 1990-91 to 1.8 per cent in 2005-06 (prov.). It is budgeted at the same level of 1.8 per cent in 2006-07. As a proportion to GDP, revenue expenditure after increasing to 13.8 per cent in 2002-03, declined to 12.3 per cent in 2005-06 (prov.). It is budgeted to decline further to 11.9 per cent in 2006-07. In terms of economic classification, revenue expenditure is composed of pay and allowances; interest payments; grants to the States and Union Territories; subsidies and others.

Interest payments

2.24 Persistent and high deficits seriously impair the counter cyclical ability of fiscal policy, lead to unsustainable debt build-up and adversely affect the composition of expenditure through larger and larger interest outgo. As a proportion of GDP, interest payments after remaining at highs of 4.6 per cent to 4.8 per cent in the four-year period from 1999-2000 to 2002-03, started declining to reach 3.7 per cent in 2005-06(prov.). It is budgeted to decline further to 3.4 per cent of GDP in 2006-07. As a proportion of revenue receipts, the corresponding decline was from a high of 53.4 per cent in 2001-02 to 38.3 per cent in 2005-06, and further to 34.7 per cent in 2006-07(BE). These declining trends, as proportion of both GDP and revenue receipts, was partly on account of the soft interest rate regime in vogue and progressive reduction in the average cost of borrowing (Table 2.5). The average cost of internal borrowing, including those under Market Stabilisation Scheme (MSS), is budgeted at 8.0 per cent in 2006-07. Bringing down the average cost of borrowing and reducing, in general, the interest outgo are critical to fiscal consolidation, growth and macroeconomic stability.

Table 2.5 : Interest on outstanding internal liabilities of Central Government

	Outstanding internal liabilities	Interest on internal liabilities*	Average cost of borrowings (per cent per annum)
	(Rs. crore)		
1990-91	283,033	19,664	8.2
1991-92	317,714	23,892	8.4
1992-93	359,654	27,546	8.7
1993-94	430,623	33,017	9.2
1994-95	487,682	40,034	9.3
1995-96	554,984	45,631	9.4
1996-97	621,438	55,255	10.0
1997-98	722,962	61,527	9.9
1998-99	834,551	73,519	10.2
1999-00	933,000	85,741	10.3
2000-01	1,047,976	94,900	10.2
2001-02	1,196,245	103,175	9.8
2002-03	1,323,704	113,238	9.5
2003-04	1,457,583	116,869	8.8
2004-05	1,603,785	124,126	8.5
2005-06(RE)	1,708,885	126,859	7.9
2006-07(BE)	1,891,346	136,191	8.0

Note : 1. Average cost of borrowing is the percentage of interest payment in year ' t' to outstanding liabilities in year 't-1'.
2. Outstanding internal liabilities exclude NSSF loans to States, with no interest liability on the part of the Centre.

*** Excludes Rs.313.61crore and Rs. 4079.62 crore towards premium on account of domestic debt buyback scheme and prepayment of external debt for 2002-03 and 2003-04 respectively.**

Source : Budget documents.

Subsidies

2.25 Subsidies are an important fiscal policy tool for correcting market failures, particularly under-consumption of basic essentials such as food. With direct provision by the Centre, major subsidies, mainly on food, fertiliser and petroleum grew from Rs. 40,716 crore in 2002-03 to Rs. 44,220 crore in 2005-06 (prov.), and were budgeted at Rs. 44,792 crore in 2006-07. As a proportion of GDP, subsidies fell from 1.7 per cent in 2002-03 to 1.2 per cent in 2005-06 (prov.) and 1.1 per cent of GDP in 2006-07 (BE). Including the supplementary demand for grants, the expenditure on subsidies is expected to increase by Rs. 5,200 crore in 2006-07. These subsidies, however, do not include the compensation through the issue of special securities to Oil Marketing companies towards the estimated under recoveries on account of domestic LPG and PDS Kerosene and special securities issued to Food Corporation of India for settlement of outstanding dues on account of release of foodgrains under Sampoorna Gramin Rozgar Yojana and National Food for Work Programme.

Supplementary demands for grants

2.26 There were two supplementary demands for grants in 2006-07 for which Parliament gave its approval. The first batch of demands included 42 grants involving a net cash outgo aggregating to Rs. 8,668 crore. Together with the demands for additional expenditure of Rs. 39,201 crore of a technical nature without cash outgo, the gross additional expenditure authorised was Rs. 47,869 crore. The major items involving cash outgo included subsidy on imported urea and on imported decontrolled fertiliser (Rs. 1,500 crore); transfers to State and Union Territory Governments for (i) providing Normal Central Assistance (Rs. 1,000 crore), (ii) providing special Central Assistance (Rs. 500 crore) and (iii) releasing grants-in-aid to States under Additional Central Assistance for Externally Aided Projects (Rs. 3,000 crore). Some major items of expenditure of a technical nature were for transfer of assets of erstwhile Nuclear Power Board to Nuclear Power Corporation of India as investment (Rs. 967 crore) and loan (Rs. 346 crore); writing off of accumulated losses of Indian Bank (Rs. 3,830 crore) and netting of accumulated losses of United Bank of India (Rs. 278 crore) against their equity capital as on March 31, 2006; for compensation through issue of special securities to Oil Marketing Companies towards estimated under recoveries in 2006-07 on account of domestic LPG & PDS Kerosene (Rs. 14,150 crore) and for issue of special securities to Food Corporation of India(FCI) for settlement of outstanding dues on account of release of food grains under Sampoorna Gramin Rozgar Yojana (SGRY) and National Food for Work Programme (NFFWP) till April 30, 2005 (Rs. 16,200 crore).

2.27 The second batch of supplementary demands for grants for 53 items approved by Parliament authorised gross additional expenditure of Rs. 21,824 crore. Net cash outgo involved was Rs. 11,445 crore and the rest were matched by savings or enhanced receipts. The major items of expenditure with cash outgo included subsidies on (i) imported urea, (ii) indigenous decontrolled fertilisers and (iii) imported decontrolled fertilisers (Rs. 2,000 crore); subsidy on nitrogenous fertilisers (Rs. 1,700 crore); interest relief to debt-stressed farmers of Andhra Pradesh, Karnataka, Kerala and Maharashtra (Rs. 1,359 crore); for providing interest subvention on short-term credit to farmers (Rs. 1,000 crore); transfer to State and Union Territory Governments to recoup of the National Calamity Contingency Fund (Rs. 500 crore); and to provide (i) Normal Central Assistance (Rs. 2,100 crore), (ii) Special Central Assistance (Rs. 436 crore) and (iii) National Social Assistance Programme (Rs. 900 crore). The major items of expenditure of a technical nature, that is, without net cash outgo, were transfer to State and Union Territory Governments for write off of loans under Debt Waiver Scheme under the TFC award (Rs 3,857 crore); and for compensation through issue of special securities to the Oil Marketing Companies towards estimated under recoveries in 2006-07 on amount of domestic LPG & PDS Kerosene (Rs 5,000 crore).

Central Plan outlay

2.28 The Budget for 2005-06 had envisaged a Central Plan outlay of Rs. 211,253 crore, the RE for which was placed at Rs. 205,338 crore because of a shortfall under Internal and Extra Budgetary Resources (IEBR) of Central Public Sector Enterprises (CPSEs). The Budget for 2006-07 hiked the Central Plan outlay to Rs. 254,041 crore, up 20.3 per cent from 2005-06 (BE). This outlay is composed of Budget support of Rs. 131,284 crore and IEBR of CPSEs of Rs. 122,757 crore. The IEBR and Budget support in 2006-07(BE) are 21.7 per cent and 18.9 per cent higher than 2005-06(BE). The relative shares of important heads of development are: energy (27.4 per cent); social services (24.9 per cent); transport (19.1 per cent); communication (7.8 per cent); rural development (7.2 per cent); industry and minerals (5.7 per cent); agriculture and allied activities (2.9 per cent); and irrigation and flood control (0.2 per cent).

Central assistance for States and UTs Plans in 2006-07(BE) at Rs. 41,443 crore is up 13.4 per cent from 2005-06 (RE).

Government debt

2.29 As a proportion of GDP, outstanding liabilities (including external debt at historical exchange rate) of the Central Government declined from 55.3 per cent in 1990-91 to reach 49.4 per cent in 1996-97, reflecting the lower fiscal deficit in the intervening years. This trend got reversed subsequently, and such liabilities as a proportion of GDP rose to 63.8 per cent in 2004-05. During the Tenth Five Year Plan, average annual rate of growth of outstanding liabilities at 12.6 per cent was marginally higher than the GDP growth of 12.5 per cent. Compared to 2001-02, the ratio of outstanding liabilities to GDP in 2006-07 (BE), therefore, was higher by 0.4 percentage points. However, with the nominal rate of growth of GDP accelerating to 14.1 per cent and 15.0 per cent in 2005-06 and 2006-07, respectively, a relatively lower growth in outstanding liabilities moderated the ratio in the two recent years at 61.5 per cent in 2005-06 (RE) and 60.3 per cent in 2006-07 (BE) (Table 2.6).

2.30 The Central Government debt is composed primarily of external and internal debt, which includes market loans (as also treasury bills) and relief/savings bonds and others. The share of debt in total internal liabilities rose from 54.4 per cent in 1990-91 to 66.0 per cent in 2004-05 before marginally declining to 63.5 per cent in 2006-07 (BE). Market borrowings, as a proportion of Government debt, after increasing from 22.4 per cent in 1990-91 to 40.8 per cent in 2003-04, has hovered around 38-39 per cent. The RBI, in consultation with Ministry of Finance, fixes biannual indicative issuance calendar for Government borrowings. The Budget for 2006-07 placed the net market borrowings (dated securities and 364-day Treasury Bills excluding borrowings under MSS) at Rs. 113,778 crore. The banks have been subscribing to Government securities much in excess of their statutory liquidity ratio (SLR) requirement. With the pick up in non-food credit (details in Chapter 3), such investments are placed at 31 per cent of net demand and liabilities of scheduled commercial banks on as on end March 2006.

2.31 Under the golden rule principle, borrowings are resorted to only for the purpose of assets creation. However, with the existence of a revenue deficit all through these years, a significant proportion of liabilities were contracted to meet the current expenditure commitments. Government accounting systems do not provide a comprehensive accounting of its assets, particularly the land, building etc., owned by it. But Government accounts do capture the assets created in the form of capital expenditure and outstanding loans receivable by the Central Government. These two together form the assets of Government created out of its annual fiscal operations. Though the assets, for example, machinery and buildings, are of different vintages, their sum total nonetheless provides an assessment of Government's assets. Total assets as defined above were 55.8 per cent of Government's outstanding liabilities, indicating that cumulatively so far nearly 45 per cent of the outstanding liabilities went to meet the current expenditure of Government.

Economic and functional classification

2.32 The economic and functional classification of the Central Government Budget 2006-07, which reclassifies budgetary transactions in significant economic categories on the lines of national income accounts, places total expenditure at Rs. 563,145 crore, indicating an increase of 10.8 per cent over 2005-06 (RE). Average annual growth of total expenditure during the Tenth Five Year Plan was 9.3 per cent. The total expenditure of Rs. 563,145 crore, excluding an allocable Rs. 4,785 crore, was composed of consumption expenditure of Rs.127,078 (22.6 per cent), current transfers of Rs.337,030 crore (59.8 per cent) and gross capital formation of Rs.94,252 crore (16.7 per cent) (Table 2.7). In terms of functional classification, general services accounted for 24.8 per cent of total expenditure, while social

Table 2.6 : Outstanding liabilities of the Central Government

(end-March)

		1990-91	2001-02	2002-03	2003-04	2004-05	2005-06 (RE)	2006-07 (BE)
					(Rs. crore)			
1.	**Internal liabilities ##**	**283,033**	**1,294,862**	**1,499,589**	**1,690,554**	**1,933,544**	**2,126,995**	**2,396,846**
	a) Internal debt	154,004	913,061	1,020,688	1,141,706	1,275,971	1,355,943	1,522,030
	i) Market borrowings	70,520	516,517	619,105	707,965	758,995	867,368	984,645
	ii) Others	83,484	396,544	401,583	433,741	516,976	488,575	537,385
	b) Other Internal liabilities	129,029	381,801	478,901	548,848	657,573	771,052	874,816
2.	**External debt(outstanding)***	**31,525**	**71,546**	**59,612**	**46,124**	**60,878**	**68,392**	**76,716**
3.	**Total outstanding liabilities (1+2)**	**314,558**	**1,366,408**	**1,559,201**	**1,736,678**	**1,994,422**	**2,195,387**	**2,473,562**
4.	Amount due from Pakistan on account of share of pre-partition debt	300	300	300	300	300	300	300
5.	**Net liabilities (3-4)**	**314,258**	**1,366,108**	**1,558,901**	**1,736,378**	**1,994,122**	**2,195,087**	**2,473,262**
					(As per cent of GDP)			
1.	**Internal liabilities**	**49.8**	**56.8**	**61.0**	**61.1**	**61.8**	**59.6**	**5.85**
	a) Internal debt	27.1	40.0	41.5	41.3	40.8	38.0	37.1
	i) Market borrowings	12.4	22.6	25.2	25.6	24.3	24.3	24.0
	ii) Others	14.7	17.4	16.3	15.7	16.5	13.7	13.1
	b) Other Internal liabilities	22.7	16.7	19.5	19.8	21.0	21.6	21.3
2.	**External debt(outstanding)***	**5.5**	**3.1**	**2.4**	**1.7**	**1.9**	**1.9**	**1.9**
3.	**Total outstanding liabilities**	**55.3**	**59.9**	**63.4**	**62.8**	**63.8**	**61.5**	**60.3**
	Memorandum items							
	(a) External debt@ (Rs.crore)	66,314	199,869	196,043	184,177	191,182	194,078	n.a.
	(as per cent of GDP)	11.7	8.8	8.0	6.7	6.1	5.4	n.a.
	(b) Total outstanding liabilities (adjusted) (Rs.crore)	349,347	1,494,731	1,695,632	1,874,731	2,124,726	2,321,073	n.a.
	(as per cent of GDP)	61.4	65.5	69.0	67.8	68.0	65.1	n.a.
	(c) Internal liabilities(Non-RBI)# (Rs.crore)	208,978	1,142,698	1,337,752	1,529,571	1,771,117	1,964,070	2,234,031
	(as per cent of GDP)	36.7	50.1	54.4	55.3	56.6	55.1	54.5
	(d) Outstanding liabilities (Non-RBI)# (Rs.crore)	275,292	1,342,567	1,533,795	1,713,748	1,962,299	2,158,148	n.a.
	(as per cent of GDP)	48.4	58.9	62.4	62.0	62.8	60.5	n.a.
	(e) Contingent liabilities of Central Government (Rs.crore)	n.a.	95,859	90,617	87,780	107,957	n.a.	n.a.
	(as per cent of GDP)	n.a.	4.2	3.7	3.2	3.5	n.a.	n.a.
	(f) Total assets (Rs crore)	236,740	760,592	840,768	903,558	1,083,422	1,189,340	1,381,289
	(as per cent of GDP)	41.6	33.3	34.2	32.7	34.7	33.3	33.7

n.a. : not available

*** External debt figures represent borrowings by Central Government from external sources and are based upon historical rates of exchange.**

@ Converted at year end exchange rates. For 1990-91,the rates prevailing at the end of March,1991; For 2002-2003,the rates prevailing at the end of March, 2003 and so on.

 # This includes marketable dated securties held by the RBI.

Internal debt includes net borrowing of Rs 64,211crore for 2004-05, Rs 27,230 crore for 2005-06(RE) and Rs 73,230 crore for 2006-07(BE) under Market Stabilisation Scheme.

Note: The ratios to GDP for 2006-07 (BE) are based on CSO's Advance Estimates. GDP at current market prices prior to 1999-2000 based on 1993-94 series and from 1999-2000 based on new 1999-2000 series.

Source: 1. Budget documents. 2. Controller of Aid Accounts and Audit. 3. Reserve Bank of India.

and economic services accounted for 13.2 per cent and 24.4 per cent, respectively, with the balance 37.6 per cent (being in the nature of statutory grants-in-aid to States, non-plan grants, food and other consumer subsidies, etc.) unallocable.

2.33 The share of wages and salaries within consumption expenditure at 38.6 per cent in 2006-07 (BE) was marginally less than 40.1 per cent in 2005-06(RE). The reclassification shows that share of current grants in total expenditure went up from 19.1 per cent in 2005-06 (RE) to 22.7 per cent in 2006-07 (BE), reflecting the impact of implementation of the TFC award. Dissavings of the Central Government, which grew steadily from Rs. 10,502 crore in 1990-91 to Rs. 81,734 crore in 2002-03, was reduced to Rs. 71,968 crore in 2003-04 and

Table 2.7 : Total expenditure and capital formation by the Central Government and its financing (As per economic and functional classification of the Central Government budget)								
		1990-91	2001-02	2002-03	2003-04	2004-05	2005-06 (RE)	2006-07 (BE)
					(Rs. crore)			
I.	**Total expenditure**	**97,947**	**360,616**	**398,879**	**426,132**	**463,831**	**508,287**	**563,145**
II.	**Gross capital formation out of budgetary resources of Central Government**	**28,032**	**76,888**	**76,782**	**82,561**	**92,855**	**85,551**	**94,252**
	(i) Gross capital formation by the Central Government	8,602	12,634	21,697	23,997	27,396	36,628	38,615
	(ii) Financial assistance for capital formation in the rest of the economy	19,430	64,254	55,085	58,564	65,459	48,923	55,637
III.	**Gross saving of the Central Government**	**-10,502**	**-76,306**	**-81,734**	**-71,968**	**-60,378**	**-63,491**	**-55,277**
IV.	**Gap(II-III)**	**38,534**	**153,194**	**158,516**	**154,529**	**153,233**	**149,042**	**149,529**
	Financed by							
	a. Draft on other sectors of domestic economy	34,768	145,841	168,582	165,858	135,918	138,508	138,588
	(i) Domestic capital receipts	23,421	147,337	166,699	169,800	208,259	123,021	138,588
	(ii) Budgetary deficit/draw down of cash balance	11,347	-1,496	1883	-3,942	-72,341	15,487	0
	b. Draft on foreign savings	3,766	7,353	-10,066	-11,329	17,315	10,534	10,941
					(As per cent of GDP)			
I.	**Total expenditure**	**17.2**	**15.8**	**16.2**	**15.4**	**14.8**	**14.2**	**13.7**
II.	**Gross capital formation out of budgetary resources of Central Government**	**4.9**	**3.4**	**3.1**	**3.0**	**3.0**	**2.4**	**2.3**
	(i) Gross capital formation by the Central Government	1.5	0.6	0.9	0.9	0.9	1.0	0.9
	(ii) Financial assistance for capital formation in the rest of the economy	3.4	2.8	2.2	2.1	2.1	1.4	1.4
III.	**Gross saving of the Central Government**	**-1.8**	**-3.3**	**-3.3**	**-2.6**	**-1.9**	**-1.8**	**-1.3**
IV.	**Gap(II-III)**	**6.8**	**6.7**	**6.4**	**5.6**	**4.9**	**4.2**	**3.6**
	Financed by							
	a. Draft on other sectors of domestic economy	6.1	6.4	6.9	6.0	4.3	3.9	3.4
	(i) Domestic capital receipts	4.1	6.5	6.8	6.1	6.7	3.4	3.4
	(ii) Budgetary deficit/draw down of cash balance	2.0	-0.1	0.1	-0.1	-2.3	0.4	0.0
	b. Draft on foreign savings	0.7	0.3	-0.4	-0.4	0.6	0.3	0.3
					(increase over previous year)			
II.	**Gross capital formation out of budgetary resources of Central Government**	**2.8**	**14.8**	**-0.1**	**7.5**	**12.5**	**-7.9**	**10.2**
	Memorandum items							
					(Rs crore)			
1	Consumption expenditure	22,359	77,324	85,389	87,170	105,692	121,680	127,078
2	Current transfers	45,134	201,188	228,501	248,436	259,529	295,367	337,030
					(As per cent of GDP)			
1	Consumption expenditure	**3.9**	**3.4**	**3.5**	**3.2**	**3.4**	**3.4**	**3.1**
2	Current transfers	**7.9**	**8.8**	**9.3**	**9.0**	**8.3**	**8.3**	**8.2**

Notes:
(i) 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.
(ii) Consumption expenditure is the expenditure on wages & salaries and commodities & services for current use.
(iii) Interest payments, subsidies, pension etc. are treated as current transfers.
(iv) Gross capital formation & total expenditure are exclusive of loans to States'/UTs' against States'/UTs' share in the small savings collection.
(v) The figures of total expenditure of the Central Government as per economic and functional classification do not tally with figures given in the Budget documents. In the economic and functional classification, interest transferred to DCUs, loans written off etc, are excluded from the current account. In the capital account, expenditure financed out of Railways, Posts &Telecommunications' own funds etc, are included.
(vi) The ratios to GDP for 2006-07 (BE) are based on CSO's Advance Estimates. GDP at current market prices prior to 1999-2000 based on 1993-94 series and from 1999-2000 based on new 1999-2000 series.

Source : Ministry of Finance, An Economic and Functional classification of the Central Government Budget-various issues.

further to Rs. 63,491 crore in 2005-06 (RE). It was budgeted to decline further to Rs. 55,277 crore in 2006-07. As a proportion to GDP, total expenditure was budgeted at 13.7 per cent, a secular decline from 17.2 per cent in 1990-91 and 16.2 per cent in 2002-03. All the three components, viz., consumption expenditure, current transfers, and gross capital formation, shared the decline. As a proportion of GDP, dissavings were placed at 1.8 per cent in 2005-06 (RE) and 1.3 per cent in 2006-07 (BE).

2.34 In economic and functional classification, non-monetary transactions are not recorded. The Government Finance Statistics (GFS) Manual 2001 of IMF updates the internationally recognized standards for the compilation of statistics required for fiscal analysis and harmonizes these with other internationally recognized macroeconomic statistical systems to the extent consistent with supporting fiscal analysis. GFS 2001 suggests that flows should be recorded on accrual basis, which means that the flows should be recorded at the time when economic value is created, transformed, exchanged, transferred or extinguished. TFC had recommended adoption of accrual accounting to allow better cost-price calculations, record capital use properly, distinguish between current and capital expenditure, and focus policy attention on financial position. A balance sheet can be more informative than just cash flows or debt. There has been some progress towards migration to accrual-based accounting (Box 2.6).

Expenditure management

2.35 Public expenditure management is an integral part of the fiscal reforms and Government has been taking a series of initiatives in this regard, like avoiding rush of expenditure through releases in a time sliced manner and simplification of procedures. Recent initiatives include: special drive to bring down outstanding 'unspent balances' and 'utilisation certificates' from States and other implementing agencies; instructions that prohibit relaxation of conditionalities attached to transfer of funds under Plan schemes; revision of General Financial Rules; speeding up the process of transmission of funds and simultaneously facilitating faster feedback on unspent balances through utilization certificates; and

Box 2.6 : Accrual Accounting in Government

Traditionally, India has followed a cash-based system for accounting and financial reporting. A cash-based system is simple, and recognizes a transaction when cash is paid or received. This system of accounting, however, is not the most informative way of presenting government accounts. It is limited in scope because it lacks an adequate framework for accounting for assets and liabilities, depicting consumption of resources and full picture of government's financial position at any point of time. Importantly, capital expenditure under the cash system is brought to account only in the year in which a purchase or disposal of an asset is made. An asset once acquired is expensed in the same year and only progressive figure of expenditure remains in the book of accounts. The present system also fails to reflect accrued liabilities. Because of these weaknesses, the existing accounting system does not capture the long-term impact of the decisions taken and promotes a bias in favour of short-term policies.

Initiatives by the Office of the Comptroller & Auditor General of India:

In July 2004, Office of the Comptroller and Auditor General of India had commissioned a study on Conceptual Framework of Government Accounting System in India under Shri D. N. Ghosh, former Chairman of the State Bank of India and presently with ICRA Advisory Services. The study emphasized that the prevailing cash-based accounting system is deficient on the dimensions of transparency and user-friendliness, and suggested the need for migration to accrual accounting.

Recommendation of the Twelfth Finance Commission (TFC) & Role of Government Accounting Standards Advisory Board (GASAB):

TFC in its Report submitted in November 2004 recommended introduction of accrual accounting in Government. Government has accepted the recommendation in principle and has asked Government Accounting Standards Advisory Board (GASAB) in the office of the Comptroller and Auditor General of India to draw up a roadmap for transition from cash to accrual accounting system and an operational framework for its implementation. Besides the Union, so far, 18 State Governments have also in principle agreed to introduce the accrual accounting system. In line with these expectations, GASAB has deliberated the matter and has also discussed the study by Shri D N Ghosh. It has suggested a roadmap for transition to accrual accounting system. The roadmap spells out the constituent activities and tasks that have to be completed for transition from a cash-based system to accrual-based accounting. Currently, it is finalizing its Report on Operational Framework, which would provide a broad design of accrual accounting system in Government, and be a reference point for financial reporting by Governments to ensure uniformity and comparability in reporting across different Ministries and also the Union and the State Governments.

e-banking scheme for transfer of funds to district level implementation agencies by three Ministries which are big in the social sector, namely, the Ministries of Human Resource Development, Rural Development and Health & Family Welfare. Simultaneously, an institutional mechanism of "outcome" budget which was placed in 2005-06 has been strengthened. Performance audit by the Comptroller & Auditor General of India of selected programmes continued to throw up important lessons for expenditure management (Box 2.7).

Collection rates

2.36 The peak rate of customs duty was brought down progressively from 150 per cent in 1991-92 to 15 per cent in the Budget for 2005-06. As the spread between peak rate and average effective rate of duty was high to begin with, the initial reductions in the former did not have significant adverse impact on revenues. However, with the spread coming down, revenue growth from customs decelerated. Since there were numerous rates and exemptions, the closest approximation to the average effective rates for customs duty for different sectors is given by the relevant collection rates. The collection rate for all commodity groups combined fell from 47 per cent in 1990-91 to 10 per cent in 2005-06 (Prov). There are large variations in the collection rates for various groups. The collection rates for the food products group fluctuated over the years, and after a decline to 19 per cent in 2003-04, climbed up to 32 per cent in 2005-06 (prov.). Apart from the changes in the composition of commodities, increase in collection rate for food products in 2005-06 compared to 2004-05 was because of special additional duties which were imposed to neutralise the disadvantes on account of domestic taxes. In chemicals group, collection rates have declined from an average of 92 per cent in 1990-91 to 20 per cent in 2005-06 (prov.). In metals also, collection rate have come down in the last few years (Table 2.8).

Box 2.7 : Performance Audit

The Comptroller & Auditor General of India (C&AG), during audit of expenditure and revenues of the Government of India, goes beyond the accounting of such transactions and conformity with the laid down procedure, to the underlying wisdom with which the expenditures have been incurred. C&AG recently completed such performance audits on Accelerated Irrigation Benefit Programme (AIBP) and Sarva Siksha Abhiyan (SSA).

Performance review of AIBP during 2003-04 revealed that despite allocating Rs 13,823 crore (including the State's share) in 24 States during 1996-2003, could not achieve the intended objective of accelerating irrigation benefits by ensuring completion of projects over four agricultural seasons. As on March 2003, only 23 of the 172 projects covered under the programme were completed. Irrigation potential created was a mere 28.28 per cent of the target, of which only 11.06 per cent could be utilized. Poor performance was due to inadequate planning and lack of coordination; frequent modification of guidelines; inappropriate selection of projects; ineffective execution and substantial time and cost over-runs; insufficient monitoring, and lack of any meaningful mid-term evaluation for possible mid-course correction.

The performance audit of SSA (2006) revealed that even after four years of the implementation of the scheme and utilization of almost 86 per cent of the funds available with implementing agencies, the revised target to enroll all children in schools, education guarantee scheme, alternate schools, and back to school camps by 2005 was not achieved. As many as 1.36 crore children in the age group of 6-14 years (40 per cent of the total 3.40 crore children out of school) remained out of school. There were delays in the release of funds and substantial gap between planned and actual achievement.

Table 2.8 : Collection rates* for selected import groups

(in per cent)

Sl. No.	Commodity Groups	1990-91	1995-96	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06 (Prov.)
1	Food Products	47	23	31	40	30	19	22	32
2	POL	34	30	16	10	11	11	10	6
3	Chemicals	92	44	38	29	28	24	22	20
4	Man-made fibres	83	36	49	31	31	46	39	34
5	Paper & newsprint	24	8	8	6	7	7	7	9
6	Natural fibres	20	12	18	8	10	13	11	12
7	Metals	95	52	48	36	36	32	26	25
8	Capital goods	60	33	36	28	23	19	16	12
9	Others	20	13	12	9	9	8	6	5
10	Non POL	51	28	23	19	17	14	12	11
11	**Total**	**47**	**29**	**21**	**16**	**15**	**14**	**11**	**10**

* Collection rate is defined as the ratio of realised import revenue (including additional customs duty/countervailing duty (CVD), and special additional duty) to the value of imports of a commodity.

S.No.1 includes cereals, pulses, tea, milk and cream, fruits, vegetables, animal fats and sugar.

S.No. 3 includes chemical elements, compounds, pharmaceuticals, dyeing and colouring materials, plastic and rubber.

S.No. 5 includes pulp and waste paper, newsprint, paperboards and manufactures and printed books.

S.No. 6 includes raw wool and silk.

S.No. 7 includes iron and steel and non-ferrous metals.

S.No. 8 includes non-electronic machinery and project imports, electrical machinery.

Source : Department of Revenue, Ministry of Finance