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PUBLIC FINANCE

The Budget for 1999-2000 was framed in the context of continuing global economic turbulence, fiscal slippage in 1998-99, weak performance of industrial and export sectors, and imposition of economic sanctions after the Pokhran nuclear tests. The constellation of adverse factors strained central government finances during 1998-99. Gross fiscal deficit (GFD) as a proportion of GDP for 1998-99 which was placed at 4.5 per cent as per the revised estimates now stands at 5 per cent on the basis of provisional[1] un-audited figures.

2.2 The fiscal slippage in 1998-99 set in motion a medium term strategy for restoring the fiscal health. The Budget for 1999-2000 envisages a fiscal deficit target at 4.1 per cent of the GDP. A new accounting framework has been effected in respect of small savings and its sharing between the Centre and the States (Box 2.1).

2.3 The Budget for 1999-2000 charts out a path of fiscal correction over a medium term with a view to eliminate the revenue deficit and reduce the fiscal deficit to below 2 per cent of GDP in four years. The Budget has outlined a six fold strategy encompassing (i) medium term process of revenue and fiscal deficit reduction, along the lines indicated in the Ninth Plan (ii) reform of indirect taxes (iii) deepening and widening of economic reforms in all major sectors (iv) safeguarding the economy from external shocks (v) strengthening the knowledge based industries and (vi) revitalising and redirecting public programmes for human development. Besides, the Budget speech has acknowledged the very high growth in non-development expenditure as a major hurdle in expenditure management and has taken some initiatives to curb the growth of non-developmental expenditure in particular.

2.4 The 1999-2000 Budget undertook a major overhaul of indirect taxes by reducing the multiplicity of rates, rationalising the rate structure and drastically curtailing the scope for discretion by abolishing the power to grant ad-hoc duty exemptions. It reduced number of duty rates for excise from 11 to 3. The cap on MODVAT credit of 95 per cent of the admissible amount was lifted and restored to 100 per cent. The Budget has also to a large extent fulfilled the government’s intention to ensure convergence towards a central rate of 16 per cent, a merit rate of 8 per cent and a demerit rate of 24 per cent. Further, Budget also indicated government's intention to move towards a single rate and a full-fledged VAT in the medium term. On the customs side, a modest reduction in peak protective customs tariff from 45 per cent to 40 per cent was effected. This was accompanied by reduction in the number of ad-valorem basic custom duty rates from seven to five. To reduce dispersion and provide some minimal protection to the domestic industry, a basic duty of 5 per cent was imposed on a number of commodities which earlier enjoyed duty exemption. To mitigate the impact of the incidence of 5 per cent duty, these were exempted from the 4 per cent special additional duty. A uniform

[1]Since February, 1999, Government has been making available provisional actual (un-audited) monthly data on the internet on Union Government Accounts. Where possible, these more recent estimates of fiscal aggregates have been used in place of revised estimates for 1998-99 in this chapter.

BOX 2.1

New System of Accounting for Small Savings in the Budget

- The Budget for 1999-2000 made a change in the system of accounting of loans to States & Union Territories (UTs) with legislature against net small savings collections w.e.f. 1.4.99. The change over was effected in the interest of transparency and viability of the small savings schemes and in deference to a suggestion made in the Inter-State Council in December 1998 on delinking the small savings from Central Government's fiscal deficit concerns. A committee set up under the chairmanship of Shri R.V. Gupta, former Deputy Governor, Reserve Bank of India, examined the modalities of transfer of small savings to an outside organisation. After examining the issue, the committee recommended for establishment of "National Small Savings Fund (NSSF)" in the Public Account of India to account for all the transactions relating to small savings.
- The amount (75 per cent States' share now has been enhanced to 80 per cent from 15-1-2000) released to State and UT Governments out of net Small Savings & PPF collections w.e.f. 1.4. 1999 would be treated as investment in the Special Securities of the respective State Governments and booked under "Investments of NSSF ". Further, interest at the rate of 12.5 per cent would be payable from 15-1-2000 and these securities would be redeemed from the sixth year over a period of 20 years. The remaining part (25 per cent) of net small savings and PPF collections (Centre's Share) would be treated as investment in the Special Securities of the Central Government. Similarly, the outstanding balances at the close of the last financial year (1998-99) under various small savings schemes and PPF would also be treated as investment of NSSF in the Special Securities of Central Government.
- In essence, under the new accounting system small savings collections would be credited to NSSF. Similarly all withdrawals of small savings by the depositors would be made out of the accumulation to the Fund. The balance in the NSSF will be invested in Central and State Government securities. The income of the NSSF will consist of the interest earned from the government securities while the servicing cost and the cost of management of small savings will be the expenditure of the Fund. All investments in Central Government securities out of the Fund would form a part of Central Government internal debt from 1999-2000.The investment of the net collections in 1999-2000 in Central and State Governments' securities is budgeted at Rs.8000 crore and Rs.25000 crore respectively. Due to this change in the accounting practice, non plan expenditure of the Centre is budgeted to be lower by Rs.25000 crore which consequently leads to reduction in the Gross Fiscal Deficit (GFD) by a similar amount. The table below gives GFD as percentage of GDP (new series base 1993-94) under old and new accounting framework.

Fiscal Deficit As Per Old and New Definition

(As per cent of GDP)

Fiscal Deficit	1990-91	1994-95	1995-96	1996-97	1997-98	1998-99	1999-2000#
Old (inclusive of State's share of small savings)	8.3	5.7	5.1	4.9	5.9	6.4**	5.4
New (exclusive of State's share of small savings)	7.0	4.8	4.3	4.1	4.9	5.0**	4.1
Centre & State Combined*	10.0	6.9	6.4	6.2	7.1	8.5	7.6

* For the years 1994-95 to 1999-2000, RBI Annual Report 1998-99; for the year 1990-91 the ratio to GDP has been worked out using old series (Base 1980-81) of National Account Satistices.

**On the basis of provisional un-audited figures. # B.E.

Note: 1. Ratios to GDP at current market prices for the year 1990-91 use old series (Base 1980-81) and from 1994-95 onwards use new series (Base 1993-94) of National Accounts Statistics released by the Central Statistical Organisation (CSO).

2. The ratios to GDP at current market prices for 1999-2000 are based on CSO's Advance Estimates.

- Although the different accounting treatment of small savings reduces the Central Government GFD, it has no effect on the combined GFD deficit of the Centre and States. Earlier any computation of the consolidated deficit of the Centre and the States had to net out this inter governmental flow, so that the consolidated deficit was less than the sum of its parts.
- It may also be noted that the small savings transactions under the new dispensation will reflect the treasury banking nature of these operations. These flows to a large extent are determined by public preferences, and relative attractiveness of these instruments.

surcharge at the rate of 10 per cent of basic duty was imposed on all commodities excluding crude oil and petroleum products, items attracting 40 per cent rate of basic duty, certain GATT bound items and gold and silver. The Budget also signaled government's intention to phase down customs duty structure to Asian levels in five years.

2.5 On the direct tax front, the Budget retained the basic tax rates for personal and corporate taxes, widened the tax base, offered new incentives for housing construction sector, infrastructure and capital markets and strengthened enforcement through tapping of high value transactions. The period for availing benefits under section 80 IA was made uniform

at 15 years across the infrastructure and core sectors. The Budget also accorded ten year tax holiday for industries in North-Eastern region to promote industrialisation. To promote housing construction activities, it unfolded a package of comprehensive fiscal incentives. With a view to encourage small investors and invigorate capital markets, all income from UTI and other Mutual Funds received in the hands of the investors were fully exempted from income tax. However, income distributed by Mutual Funds where the equity investment is less than 50 per cent was subjected to 10 per cent dividend tax.

2.6 The Budget provides a multi-pronged programme to revitalise and strengthen the rural economy in particular. Recognising the critical role of rural infrastructure, the Budget has enhanced the corpus for Rural Infrastructure Development Fund V to Rs.3500 with extended repayment period of seven years and wider coverage. Other major initiative outlined in the Budget for the benefit of the rural economy include, *inter alia,* setting up of a National Watershed Development Fund, encouraging better management of irrigation assets through larger provision of financial assistance to States that rationalise their water rates and rationalising the existing rural employment schemes with a view to enhancing their effectiveness. Budget also unveiled a National Human Development Initiative with emphasis on access of vulnerable groups to food, health care, education, employment and shelter.