

STATE FINANCES: A STUDY OF BUDGETS OF 2005-06¹

Overview

The State Governments presented their budgets for 2005-06² in an environment marked by a growing recognition of the desirability for fiscal correction and consolidation and progressive implementation of fiscal and institutional reforms by the State Governments. The submission of the Report by the Twelfth Finance Commission (TFC) and general acceptance of its recommendations by the Government of India was a major development, which would form the basis of fiscal federal relations over the five years period beginning 2005-06. Implementation of the Value Added Tax (VAT) by a majority of States with effect from April 1, 2005 was a landmark development in respect of tax reform at the State level in India. In their budgets for 2005-06 many State Governments have envisaged carrying forward the process of fiscal correction and consolidation through the enactment of Fiscal Responsibility Legislation (FRL). Other policy initiatives included introduction of new taxes and modification of the existing ones, expenditure rationalisation, institutional reforms and introduction of the new pension scheme based on defined contributions. On its part, the Central Government has taken several initiatives to facilitate and strengthen this reform process. As the banker and debt manager to the State Governments, the Reserve Bank of India (RBI) has also been sensitising the State Governments on various fiscal matters. With a view to providing guidance to the States for enacting FRL, the Reserve Bank had

constituted a Technical Group in October 2003 to frame a Model FRL at the State level.

Structural infirmities in State finances were evident during the late 1990s as reflected in the persistent expansion in revenue deficit (RD) and gross fiscal deficit (GFD), large accumulation of debt and growing debt service burden, rising share of committed but non-developmental expenditure, declining share of social sector expenditure, low and declining non-tax revenues and increasing contingent liabilities. Following policy initiatives there has been improvement in the consolidated fiscal position of the States since 2000-01. All major deficit indicators, as ratios to Gross Domestic Product (GDP), witnessed a declining trend over the period 2000-01 to 2002-03. However, some signs of transitory deterioration was recorded in 2003-04, largely due to issue of power bonds by the State Governments to Central Public Sector Undertakings under the one-time settlement scheme for dues of the State Electricity Boards. The fiscal position in 2004-05 revised estimates, however, improved in terms of key deficit indicators.

The budget estimates for 2005-06 reflect strong commitments by the State Governments to reduce the existing fiscal imbalances through a sharp correction in the level of RD and GFD by 44.0 per cent and 11.0 per cent, respectively, over the previous year. The RD and GFD as ratio to GDP have been envisaged to be reduced by 0.7 and 0.8

1 Prepared in the Division of State and Local Finances (DSLFF) of the Department of Economic Analysis and Policy (DEAP), with the support of the Regional Offices.

2 An analysis of the consolidated fiscal position of State Governments based on the State budgets of 28 States (2 of which were *Vote-on Account*) for 2005-06 has been published in the Reserve Bank of India Annual Report, 2004-05. This Study covers 29 State budgets with one being *Vote-on-Account*. It provides further details on the consolidated fiscal position as also a State-wise analysis covering budgetary data as well as additional information obtained from the State Governments and the Government of India. The data pertaining to the Capital account including public account items have been provided on a gross basis, which were hitherto given on a net basis. Furthermore, the appendices were forwarded to the respective State Governments for their confirmation and modifications suggested till mid-December, 2005 were incorporated.

percentage points, respectively, during 2005-06 from the level of 1.4 per cent and 4.0 per cent, respectively, during the previous year. The primary revenue balance would also show improvement with a surplus estimated at 2.0 per cent of GDP during 2005-06. At this level, it is budgeted to account for nearly three-fourth of interest payments in 2005-06 as compared with around half of the interest payments in the previous year. The fiscal corrections in the revenue account in 2005-06 is sought to be achieved primarily through containment of non-interest revenue expenditure, which as ratio to GDP, is budgeted to decline by 0.6 percentage points over the previous year. The developmental expenditure has been estimated to grow at a low pace of 3.0 per cent in contrast to the high growth of non-developmental expenditure at 9.2 per cent. Within developmental expenditure, the expenditure on economic services is projected to decline by 3.0 per cent over the year. Capital outlay, however, has been budgeted to grow by 12.5 per cent during 2005-06. There has been low utilisation of Ways and Means (WMA) and Overdraft (OD) during the year. On the other hand, the surplus cash balances with the State Governments surged during the year as evident from their investment in 14-Day Intermediate Treasury Bills. These indicate improvement in cash and liquidity management of the State Governments.

The fiscal correction envisaged in 2005-06 is not uniform across the States. There are a few States, which have estimated an increase in RD (5 States) and GFD (11 States) in 2005-06 Budget Estimates (BE) over 2004-05 Revised Estimates (RE), while only a few States would account for the major part of the overall correction. It may be highlighted that Maharashtra has envisaged major correction of fiscal deficit in its Budget for 2005-06 and would contribute about 50 per cent and 70 per cent of reduction in the levels of RD and GFD, respectively, of all States combined together. Thus, the envisaged consolidated fiscal correction of the State Governments would, to a large extent, depend upon the budgetary outcome of the Government of

Maharashtra for 2005-06. The likely outturn of 2005-06 budget estimates arrived at in terms of a technical exercise would indicate that the RD-GDP ratio would be placed higher at 1.1 per cent than the budgeted level of 0.7 per cent. Similarly, the GFD-GDP ratio would be placed at 3.7 per cent, which is close to the level in the previous year (4.0 per cent), against the budgeted level of 3.2 per cent.

The Report of TFC tabled in Parliament in February 2005 contains the blueprint of fiscal federalism over the medium term *i.e.*, 2005-06 to 2009-10. Higher devolution and transfer than in the past has been considered so as to reverse the decline in the volume of transfers relative to GDP and to ensure minimum vertical imbalance (between Centre and States) while correcting the existing horizontal imbalance (among the States). TFC's recommendation of debt relief through rescheduling and debt write-offs would have salutary impact on reduction of debt burden of the State Governments. Debt relief to States is conditional upon the enactment of FRL prescribing specific annual targets with a view to eliminating the RD by 2008-09 and reduction of GFD-Gross State Domestic Product (GSDP) ratio to 3.0 per cent by 2009-10 through a fiscal restructuring path. TFC's recommendation for phasing out Plan loans from the Centre to States would have implications for borrowings by the State Governments. To address various issues related to future market borrowings of the States, the Government of India has constituted a Technical Group (Chairperson: Smt. Shyamala Gopinath, Deputy Governor, RBI). The Group is constituted with representatives from the Government of India, the Reserve Bank and selected State Governments.

For fiscal correction to translate into durable fiscal consolidation, a few issues need to be addressed. First, the State Budgets have envisaged sharp correction in the key deficit indicators in 2005-06, particularly, in the revenue account with bulk of the fiscal correction accounted for by a few major States. However, given the past track record of

weak fiscal marksmanship of the State Governments, such high level of corrections within a span of one year appears to be difficult. To be effective, the States may consider following a gradual and steady approach as specified in the TFC's restructuring scheme. Second, following a holistic approach, which is also specified in the TFC's restructuring scheme, the path for fiscal correction and consolidation of the State Governments needs to emphasise revenue augmentation, compression and rationalisation of expenditure and containment of debt within sustainable limits. Third, making the process of fiscal correction a binding force through FRL is expected to augment fiscal discipline and provide a more realistic correction path. Fourth, in the process of correction, capital expenditure and spending on social services should not suffer by falling below some critical threshold levels.

Prudent fiscal management suggests that the path to durable fiscal consolidation most importantly lies through fiscal empowerment *i.e.*, by expanding the scope and size of revenue flows into the budget. A fiscal strategy based on revenue maximisation would also provide the necessary flexibility to shift the pattern of expenditure and redirect them productively. On the other hand, fiscal adjustments based predominantly on expenditure reduction involve welfare losses and risk the danger of triggering a downturn of overall economic activity. In this context of fiscal empowerment of the States, augmenting resource mobilisation from non-tax revenues through appropriate user charges, cost recovery from social and economic services and restructuring of State Public Sector Undertakings (PSUs) have to be given due importance.

It is widely recognised that the level of social sector expenditure has important implications for long-term prospects of the economy, with bulk of the responsibilities pertaining to public expenditure on social services including education and health

placed in the domain of State Governments. Moreover, the States provide most of the infrastructure services except for telecommunications, civil aviation, railways and major ports and maintain law and order. Therefore, the ability of the States to spend on social services has important implications for social development³. Strengthened policy measures and improvement in health, education and other aspects of rural development in the States will contribute greatly to the overall improvement in human development in the country.

One important issue on State finances pertains to sustainability of debt, which embodies concern about the ability of the State Governments to service their debt obligations. Over the years, large revenue deficits have led to large fiscal deficits and spiraling debt resulting in the emergence of a vicious cycle of deficit, debt and debt service payments for most of the State Governments. Recognising the magnitude of the problem, several national level agencies such as Comptroller and Auditor General of India (CAG), Finance Commissions and the Reserve Bank have repeatedly stressed the need to address the underlying issues related to debt sustainability. In this context, TFC had emphasised the need for imposing a hard budget constraint and suggested that the overall borrowing programme of a State should be within a prescribed limit, determined annually, taking into account borrowings from all sources. A Study⁴ on debt sustainability undertaken in the Reserve Bank emphasised the measures of expenditure compression, improvement in own revenue collection effort and several institutional changes to contain the problem of State level debt in India.

In recent years, there has been a substantial increase in the resource gap of the States largely reflecting structural infirmities as reflected in a sharp increase in their GFD. In the context of the high level of fiscal deficit and debt a critical issue

³ Mohan, Rakesh (2005): "Human Development and State Finances", RBI Bulletin, December, pp.1123 – 1129,

⁴ Rajaraman, I., S. Bhide and R.K. Pattnaik (2005), "A Study of Debt Sustainability at State Level in India", RBI, Mumbai.

that has come to the forefront is the imposition of certain restrictions under Article 293 of the Indian Constitution on the borrowings by State Governments. Under Article 293, the States are not allowed to borrow directly from external sources and require the Centre's permission to raise loans domestically as long as, they are indebted to the Centre or have taken guarantees from the Centre in respect of loans raised by the States. It may be indicated that in practice the borrowings under Public Accounts are not subject to Article 293 as these funds do not belong to the State and are raised by the State as a banker. Historically, items under Article 293 dominated financing of GFD of the State Governments: in particular, the component of loans from the Centre, the largest amongst Article 293 items of borrowings of States, accounted for the bulk. However, with introduction of National Small Saving Fund (NSSF) and consequent change in accounting, its share declined from 1999-2000. In the recent period, Securities issued to NSSF have emerged as the dominating component of GFD financing for the States. As a consequence, the financing pattern of GFD reveals that the share of borrowings under Article 293 has fallen to 33.4 per cent of GFD in 2004-05 from an annual average of 59.5 per cent during 1995-2000. There is, therefore, a concern that notwithstanding explicit and implicit restrictions under Article 293 with regard to borrowings by the States, the provision in practice has not been strictly adhered to. In this backdrop, there is a view that Article 293 restrictions could be extended to encompass all borrowings that finance GFD keeping in view the increasing concerns over States' debt sustainability. One option could be that a global cap on borrowed resources could be fixed rather than separate caps for each individual instrument.

Among the financing of GFD, the Securities issued to NSSF have emerged as the dominant component, constituting over two-third of GFD in the recent period. This is an exogenous source of financing GFD for the States as determination of

the quantum and cost of these borrowings are not under their purview. Given the higher cost of small savings than the market borrowings at present, at least in respect of those States who receive over-subscription in tap issues and a finer spread at the auctions, a few States have put forth their preferences for market borrowings over NSSF. In the context of borrowings from NSSF *versus* market borrowings, there are trade-offs between the current lower interest rates of market borrowings and longer maturity and stability of NSSF. Given the trade-offs, one option could be extending the States freedom to exercise the choice of borrowing instruments *viz.*, NSSF *versus* market borrowings based on the relative advantage for respective States. While the better creditworthy States may prefer market borrowings on account of its perceived lower interest cost, others may prefer the small savings route on account of their relative certainty and stability. Moreover, if a State does not require excess receipts from NSSF, the Centre may either use the excess amount to finance its own GFD or empower NSSF to lend to other States that do not have resources to match their approved overall borrowing limits. Furthermore, in the context of perceived high cost nature of NSSF, prepayments of loans from NSSF by the State Governments and re-alignment of interest rates on NSSF to market rates can also be explored. One option is to swap the existing high cost debt carrying interest rates over 9.5 per cent with fresh receipts from the NSSF in a phased manner. A second option could be to allow the States to enter the market to raise the required resources for the debt swap. A third option could be to switch to back-to-back repayments as suggested by the Expert Committee to Review the System of Administered Interest Rates and Other Related Issues (Chairman: Dr.Y.V.Reddy) in order to eliminate the maturity mismatches arising out of the maturity structure of small savings schemes and the terms of repayment by the States. A fourth option may be to revert back to the 80:20 formula, which will limit NSSF investment in Special State Government Securities (SSGS) to 80 per cent of

the net collections with the balance to be invested in Central Government securities.

There has been a sharp accumulation of the surplus cash balances of State Governments since the beginning of the fiscal 2005-06. This could be attributed to several factors such as (i) containment of expenditure by the State Governments particularly, non-interest revenue expenditure and stagnant capital outlay, (ii) higher Central transfers in the light of TFC recommendations and higher economic growth, (iii) buoyant receipts under various small savings schemes, (iv) completion of Debt Swap Scheme (DSS) and (v) better liquidity management by the States. States invest their temporary surplus cash balances in 14-Day Intermediate Treasury Bills with current rate of return of 5.0 per cent. The States earn a negative spread on the reverse flow of resources from the Centre since the surpluses are funded by the borrowings mobilised at a significantly higher cost. In view of the above, if the States perceive their surplus cash balances to be of enduring nature, appropriate options may be given for deployment of such balances.

The borrowing requirements of the State Governments have made the State Governments raise loans from banks and financial institutions, *inter alia*, LIC, GIC, NABARD, NCDC, HUDCO and REC. The interest rates and other terms of conditions on such loans negotiated between State Governments and the lending institutions, may depend upon the creditworthiness and fiscal soundness of individual State Governments, repayment track record of the State Governments and honouring of guaranteed obligations. The information obtained from a few State Governments reveals the high cost nature of this category of debt on which interest rate varies in the range of 8 to 24 per cent, reflecting significantly high risk premia. This brings into picture the case of the debt-swap for prepayment of these high cost loans. It may be noted that the Union Budget 2004-05 had proposed extending the facility of debt-swap by allowing

States to raise fresh loans and repay their old high-cost loans to NABARD and some other agencies. Consideration may also be given to allow the State Governments to prepay on a voluntary basis the balance high cost loans. In this context, however, it is emphasised that any additional market borrowings to meet such prepayments over and above the level projected by the Reserve Bank would have implications for monetary management. Moreover, this could also exert pressure on debt management on account of lack of investors' appetite for State Development Loans (SDLs).

With reference to Central Plan Assistance (CPA) from the Planning Commission, TFC has recommended for doing away with Plan loans and extending entire plan assistance in the form of grants only. Furthermore, TFC recommended for allowing the States to decide whether to borrow from the market or from the Centre, thus eliminating the process of on-lending. However, if fiscally weaker States are unable to raise funds from the market, TFC recommended that the Centre could borrow for on-lending to such States and charge a rate of interest aligned to the marginal cost of its borrowings. The recommendations of the TFC on doing away with the loan portion of the CPA and discontinuation of Central intermediation have significant implications for the future market borrowings of State Governments. Assuming all other sources of financing GFD remaining unchanged, the short fall due to elimination of Central Plan loans is expected to be compensated by increase in the market borrowings. By resorting to market borrowings, the State Governments would be exposed to market discipline. It is important to note that the quantum of market borrowings by the State Governments in the future has to be consistent with the GFD envisaged in their FRLs and would also critically depend upon the other sources of borrowings in the Consolidated Fund and the Public Account. The immediate concern of the various stake holders associated with market borrowings of the States is regarding the ability of the States

to raise additional resources directly from the market over and above their normal open market borrowings for the current year. Such concern emanated from the experience during 2003-04 and 2004-05, when the open market borrowing programme of the State Governments had received lukewarm response from investors, reflecting in part, their excess holdings of Government securities for the purpose of maintenance of statutory liquidity ratio (SLR) with the banking system, the increasing availability of alternative avenues for lending as economic activity gathered momentum and apprehensions regarding the quality of fiscal and economic performance of the State Governments.

Apart from the borrowings routed through the budget, State Governments have often resorted to off-budget borrowings. States have taken recourse to borrowings through public sector enterprises (PSEs) under their control, enabling them to float bonds against State Government guarantees. Other special purpose vehicles mainly for infrastructure financing have also come into the picture. Although contingent liabilities do not form a part of the debt of States, in the event of default by the borrowing entities, the States will be required to meet the debt service obligations. In this connection, it is noteworthy that the FRLs enacted by many State Governments already contain provisions relating to a cap on the debt-GSDP ratios as also on the guarantees. Thus, progressive enactment of FRL by the State Governments is likely to invoke discipline with regard to guarantees.

The persistent expansion of GFD over the years led to large accumulation of debt by the State Governments. Interest payment as a ratio of revenue receipts peaked at about 26 per cent in 2003-04, bringing the issue of sustainability of debt at the State level to the fore. Given the fact that there is no consistent time series data on outstanding liabilities of the State Governments, an attempt has been made to develop a new data series. Related matters have been discussed in the

form of a special theme in this Study (Section VI). Broadly, in recent years the share of loans from the Centre in the outstanding debt of the State Governments, has been witnessing sharp declines accompanied by upsurge in loans from NSSF and market loans.

In sum, the fiscal position of the State Governments during 2005-06 would to a large extent, be shaped by the recommendations of the TFC, implementation of VAT by majority of States and progressive enactment of FRL by the State Governments. There are some important issues, which need to be addressed by the State Governments in the context of fiscal correction and consolidation. The process of fiscal correction should be durable and sustainable. As recommended by TFC, the State Governments may consider following a holistic approach to fiscal restructuring emphasising revenue augmentation, compression and rationalisation of expenditure and containment of debt at sustainable levels. In this context, it is important to recognise that adequate investment in economic infrastructure and spending on social services by State Governments are essential. With the State Governments facing resource gaps, a desirable path to fiscal correction lies through fiscal empowerment *i.e.*, by expanding the scope and size of revenue flows into the budget. In view of the above, augmenting resource mobilisation from non-tax revenue through appropriate user charges, cost recovery from social and economic services and restructuring of State PSUs assume importance. Furthermore, the State Governments may consider a prudent public expenditure strategy by arresting the rising share of non-plan non-developmental expenditure. In order to be able to borrow from the market in an environment of market discipline, it is essential that the State Governments may consider to improve their financial position.

The remainder of the present Study is organised as follows. Section I summarises the policy initiatives including the major

recommendations of TFC. Section II provides an analysis of the consolidated fiscal position of the State Governments for the years 2003-04 (Accounts), 2004-05 (Revised Estimates) and 2005-06 (Budget Estimates). Section III discusses the State-wise fiscal scenario. This is based on an analysis of thirteen fiscal indicators classified broadly into (i) resource gap; (ii) revenue performance and (iii) pattern of expenditure. The analysis of fiscal indicators is undertaken separately for Special and Non-Special Category States. Section IV discusses implications of TFC's recommendations for State finances. The issues and perspectives in State Government finances are covered in Section V. Section VI analyses debt position of the State Governments based on a new data series as a special theme. Section VII contains the concluding observations. The Appendix Tables (1-21) provide data on major fiscal indicators at consolidated level. The Statements (1-43) provide State-wise data in respect of major fiscal parameters. State-wise detailed data on revenue receipts, revenue expenditure, capital receipts and capital expenditure are set out in Appendices I, II, III and IV, respectively.

I. POLICY INITIATIVES

Structural weaknesses in the finances of the State Governments as reflected in the persistent expansion of key deficit indicators (*viz.*, RD and GFD), large accumulation of debt, mounting debt-servicing burden, rising share of committed but non-developmental expenditure, declining social sector expenditure, low and declining non-tax revenues and increasing contingent liabilities were clearly evident during the late 1990s. These developments warranted fiscal correction and consolidation. Recognising this, a number of State Governments had initiated an array of self-imposed reform initiatives. On its part, the Central Government had also taken several initiatives to facilitate and

strengthen this reform process. As the banker and debt manager to the State Governments, the Reserve Bank of India (RBI) has also been sensitising the State Governments on various fiscal matters⁵. Some moderation in fiscal imbalances of State Governments has been visible in the recent years. The continuation of the process of fiscal correction and consolidation was clearly evident from the policy initiatives announced in the current fiscal year 2005-06⁶. The reform process in the State finances was given a further boost by the recommendations of the TFC with provisions for enhanced devolution and transfer of resources from the Centre to the States in the form of share in Central taxes and grants and benefits of debt relief linked to fiscal discipline.

This Section briefly summarises the schemes and initiatives of the State Governments, Central Government and the Reserve Bank pertaining to State finances. Furthermore, major recommendations of the TFC, which are expected to have implications for State finances during 2005-06 to 2009-10, have also been briefly discussed.

I.A. Policy Initiatives of State Governments

One of the landmark policy initiatives pursued by the State Governments during 2005-06 has been the implementation of VAT in place of Sales Tax. Apart from this, many State Governments in their budgets for 2005-06 have envisaged carrying forward the process of fiscal correction and consolidation through the enactment of FRL. The other policy initiatives included introduction of new taxes and modification of the existing ones, expenditure rationalisation, institutional reforms and introduction of new pension scheme based on defined contributions. The State-wise details of these initiatives are set out in *Annex 1* and a brief summary of the same is provided below.

⁵ The bi-annual Conference of the State Finance Secretaries that has been held since 1997 provides a common platform for a consensus approach to issues.

⁶ This document has been enumerating policy initiatives of the State Governments based on the State Budget documents since 1995-96.

I.A.(i) Revenue Augmentation

As many as 23 State Governments (including Jharkhand) have shifted to the VAT regime while the rest are yet to decide on the matter (Table I).

Many State Governments have proposed new taxes (*viz.*, road tax, special entry tax and luxury tax) in their Budgets for 2005-06 while some States have suggested modifications in the existing tax rates for additional resource mobilisation. Haryana has set up a Committee to look into the avenues for mobilisation of additional resources. The State of Nagaland has proposed to set up a Special Purpose Vehicle (SPV) for raising resources for critical infrastructure requirements.

Low level of non-tax revenue has been an area of concern for State finances. Recognising this, several State Governments *viz.*, Karnataka, Himachal Pradesh, Jammu & Kashmir, Mizoram and Sikkim have proposed to raise water or irrigation charges, recognising the rationale for augmentation of non-tax revenues.

I.A.(ii) Expenditure Management

Most of the State Governments have taken initiatives towards rationalisation of expenditures. Measures towards containment of committed revenue expenditure included introduction of new

pension schemes based on defined contribution system by the States (Chhattisgarh, Jharkhand and Madhya Pradesh)⁷. The State of Nagaland has proposed to set up a Pension Fund Authority to manage pension funds. Several States (*viz.*, Assam, Haryana, Orissa, Sikkim, Tripura, Uttar Pradesh and West Bengal) have proposed a few schemes and policy measures aimed at generating employment avenues. The States of Assam, Himachal Pradesh, Karnataka and Nagaland have set up Committees/ Commissions to advise State Governments on various fiscal matters or monitor expenditures.

I.A.(iii) Institutional Measures

One important institutional reform of the State Governments during the fiscal year 2005-06 relates to the progressive enactment of FRL. Realising the need for fiscal discipline based on rule based policy, five major States namely, Karnataka, Kerala, Tamil Nadu, Punjab and Uttar Pradesh have already enacted FRLs prior to 2005-06. The TFC had incentivised statutory backing to fiscal reforms through enabling legislations by linking it to debt relief benefits. The financial year 2005-06 witnessed enactment of FRLs by a number of State Governments. As per latest information available, 16 States (including the above 5 States) have enacted FRLs, while many others are in the process of doing so (*Annex 2*). Other important institutional measures included proposals to restructure the State Electricity Board in Maharashtra, constitution of the Third Finance Commission and a Public Tariff Commission in Himachal Pradesh, a Tax Reform Commission in Assam and setting up of an Investment Commission in Punjab. States like Rajasthan, Uttaranchal and Tamil Nadu intend to set up bodies for development of roads whereas Nagaland will set up a pricing tribunal for determining costs/prices of goods and services delivered to the people. Furthermore, the States of Madhya Pradesh and Tripura have proposed to set up Guarantee Redemption Funds.

Table I : Implementation of VAT at the State Level

States	No. of States	Date of Implementation
1	2	3
Haryana	1	April 1, 2003
Andhra Pradesh, West Bengal, Kerala, Karnataka, Orissa, NCT Delhi, Tripura, Bihar, Arunachal Pradesh, Sikkim, Punjab, Goa, Mizoram, Nagaland, Jammu & Kashmir, Manipur, Maharashtra, Himachal Pradesh	18	April 1, 2005
Assam, Meghalaya	2	May 1, 2005
Uttaranchal	1	October 1, 2005
Jharkhand	1	Announced to implement from January 1, 2006
Uttar Pradesh, Tamil Nadu, Rajasthan, Gujarat, Chhattisgarh, Madhya Pradesh	6	Not yet decided

⁷ Other States that have also introduced the new pension scheme till now are Andhra Pradesh, Assam, Gujarat, Goa, Himachal Pradesh, Manipur, Rajasthan, Tamil Nadu and Uttar Pradesh.

I.A.(iv) Other Measures

In their Budget 2005-06, the States of Andhra Pradesh, Punjab, Rajasthan, Jammu & Kashmir, Mizoram and Tamil Nadu have proposed to improve urban infrastructure while Gujarat has created an Urban Infrastructure Fund. The States of Haryana, Jharkhand and Karnataka have proposed to set up special economic/export promotion zones while Uttar Pradesh and Haryana have emphasised on gender budgeting. Several States such as Assam, Sikkim, Himachal Pradesh, Punjab and Uttaranchal have initiated measures towards fiscal empowerment of local bodies.

I. B. Initiatives of the Government of India

Having accepted most of the recommendations of the TFC, the Union Budget 2005-06 has made provisions for higher devolution of funds through share in Central taxes and grants to the State Governments with an increase of about 32 per cent. In view of the recommendation of the TFC to do away with the Central Plan loans to the States, the Government of India has constituted a Technical Group (Chairperson: Smt. Shyamala Gopinath) to work out the modalities for smooth transition to the new regime for States' market borrowings.

The Union Budget 2005-06 emphasises the development of the North-Eastern region and specifies that all Ministries and Departments are required to allocate at least 10 per cent of their plan budget for schemes and programmes in the North-Eastern Region. The Union Budget 2005-06 further outlines the National Urban Renewal Mission for upgradation of urban facilities to satisfactory standards of seven mega cities and several other cities/towns. Furthermore, a Backward Regions Grant Fund is also being established which will benefit 170 identified districts but resources will be conditional on proper empowerment of *Panchayati Raj* Institutions. Further, Special Plan assistance for Jammu and Kashmir has been provided in addition to the normal State Plan under a recently

approved Reconstruction Plan. The Union Budget also emphasised several schemes such as the National Rural Health Mission, Employment Generation Scheme, *Sarva Shiksha Abhiyan* and rural electrification, which would benefit States.

I. C. Reserve Bank's Initiatives

As the banker and debt manager to the State Governments, the Reserve Bank has been sensitising the State Governments on various issues pertaining to State finances. The bi-annual State Finance Secretaries Conference organised by the RBI since 1997 provides a common platform to evolve a consensual approach on all relevant issues. The major outcomes of this endeavour include formulation of the Model Fiscal Responsibility Legislation, constitution of Guarantee Redemption Fund (GRF) and Consolidated Sinking Fund (CSF).

To facilitate adoption of a rule-based fiscal programme at the State level, the Reserve Bank had constituted a Group in October 2003, with representatives from several State Governments and Government of India to frame a Model Fiscal Responsibility Bill. The Report of the Group was submitted in January 2005. As decided in the Conference of State Finance Secretaries held in August 2004, the Report of the Group has been placed in the Reserve Bank's website and also published in the March 2005 issue of RBI Bulletin (Box 1).

In order to sensitise State Governments about the adverse impact of the increasing volume of guarantees, the Reserve bank has constituted a Standing Committee to collect and monitor information on State Government guaranteed advances and bonds from the investors' side on a periodic basis. The Reserve Bank has issued revised prudential norms as per which, for the year ending March 31, 2005 (March 31, 2006), State Government guaranteed advances and investment in State Government guaranteed securities would attract asset classification and provisioning norms, if interest and/or principal or any other amount due

Box 1

Report of the Group on Model Fiscal Responsibility Legislation at State Level - Summary

The Group on Model Fiscal Responsibility Legislation at State Level viewed that the model bill would provide guidance to the States for enacting their fiscal responsibility legislations with reference to certain benchmarks. According to the Model, the FRL Bill of a State Government will contain the following, apart from titles, definitions and explanations:

1. Fiscal Management Objectives:

- Taking appropriate measures to eliminate revenue deficit and thereafter build up revenue surplus and contain fiscal deficit at a sustainable level.
- Pursue policies to raise non-tax revenue with due regard to cost recovery and equity.
- Lay down norms for prioritisation of capital expenditure and pursue expenditure policies that would provide impetus for economic growth, poverty reduction and improvement in human welfare.

2. Fiscal Management Principles:

- Transparency
- Responsibility and Integrity
- Efficiency
- Stability and Predictability
- Fairness

3. Fiscal Policy Statements to be laid before the Legislature:

- (a) The Macroeconomic Framework Statement: This Statement shall contain an overview of the State's Economy, an analysis of growth and sectoral composition of GSDP, an assessment related to State Government finances and future prospects.
- (b) The Medium Term Fiscal Policy Statement shall contain the three year rolling targets of RD to Total Revenue Receipts (TRR), GFD as a percentage of GSDP and total outstanding liabilities as percentage of GSDP. The Statement shall include the various assumptions behind the fiscal indicators and an assessment of sustainability relating to:
 - (i) the balance between revenue receipts and revenue expenditure;
 - (ii) the use of capital receipts including borrowings for generating productive assets;
 - (iii) the estimated yearly pension liabilities worked out on actuarial basis for the next ten years.

(c) Fiscal Policy Strategy Statement:

The Fiscal Policy Strategy Statement shall contain, *inter alia*, the following:

- (i) Fiscal policies of the State Government for the ensuing year relating to taxation, expenditure, borrowings and other liabilities, lending, investments, contingent liabilities, user charges on public goods/ utilities and description of other activities such as guarantees and activities of State Level PSUs.
- (ii) Strategic priorities of the State Government in the fiscal area for the ensuing year.
- (iii) The key fiscal measures and the rationale for any major deviation in fiscal measures pertaining to taxation, subsidy, expenditure, borrowings and user charges.
- (iv) Evaluation of current policies of the State Government *vis-à-vis* the fiscal management principles.

The Fiscal Policy Strategy Statement would have nine Disclosure Statements regarding select Indicators of Fiscal Situation, Components of State Government liability and interest cost of borrowings, Consolidated Sinking Fund, Guarantees given by the State Government, Outstanding risk-weighted guarantees, Guarantee Redemption, Assets, Revenue demands raised but not realised and Outstanding miscellaneous liabilities.

4. Fiscal Targets

The State Government may prescribe such targets as may be deemed necessary for giving effect to fiscal management objectives. These may include the followings:

- (a) Reduction and elimination of revenue deficit.
- (b) Reduction of GFD/GSDP ratio
- (c) Reduction of outstanding liabilities/GSDP ratio
- (d) Limiting the incremental risk weighted guarantees as ratio to TRR and/or GSDP.

The RD and GFD targets will have exclusion clauses on grounds of unforeseen demands on the finances of the State Government arising out of internal disturbance or natural calamity or such other exceptional grounds as the State Government may specify.

In addition, the Model Bill specifies about measures for fiscal transparency, measures to enforce compliance, power to make rules, which shall be laid before the House or Houses of the legislature. The State Government may set up an appropriate agency independent of the Government to carry out the periodic review for the compliance of the provisions of the Act in the manner as may be prescribed under the rules framed under the Act.

to the bank remains overdue for more than 180 days (90 days).

Furthermore, an Advisory Committee to review the WMA Scheme was constituted in May 2005 (Chairman: Shri M. P. Bezbaruah). The Report of the

Advisory Committee has been submitted recently, which would be discussed with the State Governments.

I. D. Major Recommendations of TFC⁸

Major recommendations of TFC having significant implications for the State finances are

⁸ The Summary of recommendations of the TFC and the Action Taken Report by the Government of India has been published in the March 2005 issue of RBI Bulletin.

broadly in terms of fiscal transfers from the Centre to States, debt relief benefits for the States and doing away with Central Plan loans to the States.

I.D.(i) Sharing of Union Tax Revenues

In the scheme of fiscal transfers, TFC recommended an increase in the share of States in the divisible pool of taxes to 30.5 per cent as compared to a share of 29.5 per cent during Eleventh Finance Commission (EFC) period. The indicative benchmark for overall transfers to States is to be fixed at 38 per cent of the Centre's gross revenue receipts, as compared with 37.5 per cent recommended by the EFC (2000-01 to 2004-05).

I.D.(ii) Grants-in-aid to States

The system of imposing a 70:30 ratio between loans and grants for extending Plan assistance to non-Special Category States (10:90 in the case of Special Category States) should be done away with. The Centre should confine itself to extending Plan grants to the States and leave it to the States to decide how much they wish to borrow and from whom (*i.e.* Centre or the market). The Central Government should not act as an intermediary for future lending and allow the States to approach the market directly. If some fiscally weak States are unable to raise funds from the market, the Centre could borrow for the purpose of on-lending to such States, but the interest rates should remain aligned to the marginal cost of borrowing for the Centre.

Total grants to the States recommended by the TFC is placed at Rs.1,42,640 crore which is 143 per cent higher than that of Rs.58,587 crore recommended by the EFC. The TFC has also recommended grants for health, education and heritage conservation as well as for the maintenance of roads and bridges, public buildings and forests, amounting to Rs.37,684 crore for the period 2005-10. These grants for education, health and maintenance of roads and buildings are provided as an additionality, over and above the normal expenditure by the States in these sectors.

These grants are required to be utilised only for the respective sectors (non-Plan).

I.D.(iii) Calamity Relief

The scheme of Calamity Relief Fund (CRF) has been recommended to be continued in its present form with contributions from the Centre and the States in the ratio of 75:25. The size of the CRF has been enhanced from Rs.11,008 crore in the EFC period to Rs.21,333 crore under the TFC allocation. The Centre's contribution increases from Rs.8,256 crore during the EFC period to Rs.16,000 crore under the TFC. The definition of natural calamity has been widened to include landslides, avalanches, cloud bursts and pest attacks. According to the TFC, provision for disaster preparedness and mitigation shall be part of State Plans and will not be part of calamity relief.

I.D.(iv) Local Bodies

In order to provide an impetus to the decentralisation process, the TFC has recommended a sum of Rs.25,000 crore as grants-in-aid for the period 2005-10 as compared with Rs.10,000 crore recommended by the EFC to augment the consolidated fund of the States to supplement the resources of the municipalities and the *panchayats*. The amount will be divided between the *panchayats* and the municipalities in the ratio of 80:20. These grants are directed primarily for the assets and operation and maintenance relating to water supply and sanitation in respect of *panchayats* and sewerage and solid waste management in case of urban local bodies. TFC has further recommended that the Central Government should not impose any condition other than those prescribed by TFC for release of these grants.

I.D.(v) Debt Relief

A two-pronged approach to debt relief was adopted by the TFC *viz.*, (i) a general scheme of debt relief applicable to all States and (ii) a write-

off scheme linked to fiscal performance with a view to providing an incentive for achievement of revenue balance by 2008-09. Loans given to States from NSSF have been excluded from the scope of debt relief. Under the general scheme of debt relief, all Central loans to the States contracted till March 31, 2004 and outstanding on March 31, 2005 (amounting to Rs.1,28,795 crore) have been consolidated and the interest rate thereon has been fixed at 7.5 per cent along with a uniform tenor of 20 years. This will be subject to the State enacting FRL. The debt relief during the award period for all States works out to Rs.21,276 crore in interest payments and Rs.11,929 crore in repayments. Under the debt write-off scheme, repayments due from 2005-06 to 2009-10 on Central loans contracted upto March 31, 2004 and recommended to be consolidated and rescheduled as above, will be eligible for write-off subject to the quantum of write-off of repayment being linked to the absolute amount by which the revenue deficit is reduced in each successive year during the award period and fiscal deficit of the State being contained at the level of 2004-05. The enactment of FRL would be a necessary precondition for availing the debt relief under this scheme also, with the benefit accruing prospectively.

I.D.(vi) Fiscal Reform Facility

With the recommendation of debt relief in place, the TFC does not recommend continuation of the Fiscal Reform Facility over the period 2005-10.

I.D.(vii) External Assistance

TFC recommends that external assistance may be transferred to States on the same terms and conditions as attached to such assistance by external funding agencies, thereby making Government of India a financial intermediary without any gain or loss. The external assistance passed to States should be managed through a separate fund in the public account.

I.D.(viii) Sinking Fund

TFC has recommended that all States should set up sinking funds for amortisation of all loans including loans from banks, liabilities on account of NSSF, etc.

I.D.(ix) Guarantee Redemption Fund

In order to provide for sudden discharge of the States' obligations on guarantees, TFC has recommended that all States should set up guarantee redemption funds through earmarked guarantee fees.

The policy initiatives adopted in recent years have resulted in some improvement in fiscal position of the State Governments. It may, however, be added that such improvement is not across the board for all States. In the backdrop of the fiscal initiatives, the subsequent Section would discuss the consolidated fiscal position of the States for the years 2003-04 (Accounts), 2004-05 (RE) and 2005-06 (BE).

II. CONSOLIDATED FISCAL POSITION OF STATE GOVERNMENTS

As alluded to earlier, the impact of policy initiatives of the State Governments was reflected in the improvement of the consolidated fiscal position of the States since 2000-01. All the major deficit indicators, as ratios to GDP, witnessed a decline over the period 2000-01 to 2002-03. However, some signs of transitory deterioration was recorded in 2003-04 largely due to issue of power bonds by the State Governments to Central Public Sector Undertakings under the one time settlement scheme for dues of the State Electricity Board. Against this backdrop, the following discussion highlights the fiscal position of the State Governments in terms of their accounts of 2003-04, 2004-05 (RE) and 2005-06 (BE).

II. A. Accounts : 2003-04

II. A.(i) Fiscal Position in 2003-04 (Accounts vis-à-vis Revised Estimates)

Fiscal correction and consolidation of the State Government finances was evident when the

revised estimates of 2003-04 were translated into accounts (Table II). Resource gap in terms of RD and GFD witnessed a decline of Rs.10,981 crore (0.4 per cent of GDP) and Rs.17,940 crore (or 0.6 per cent of GDP), respectively between 2003-04 (RE) and 2003-04 (Accounts). Reflecting this, the ratio of primary deficit (PD) to GDP registered a reduction by 0.6 percentage points from 2.1 per cent to 1.5 per cent between the revised estimates and accounts (Appendix Tables 1-2).

The correction in the revenue account between 2003-04 (RE) and 2003-04 (Accounts)

Table II: Variation in Major Items - 2003-04 (Accounts) over 2003-04 (RE)

(Rs. crore)

Item	2003-04 (RE)	2003-04	Variation (3 over 2)	Contribution * (per cent)
1	2	3	4	5
I. Revenue Receipts (i+ii)	329,927	316,535	-13,392	100.0
(i) Tax Revenue (a+b)	228,103	226,999	-1,104	8.2
(a) Own Tax Revenue	162,806	159,921	-2,885	21.5
of which				
Sales Tax	98,378	97,590	-788	5.9
(b) Share in Central Tax	65,297	67,079	1,782	-13.3
(ii) Non-Tax Revenue	101,824	89,536	-12,288	91.8
(a) States' Own Non-Taxes	40,940	38,189	-2,751	20.5
(b) Grants from Centre	60,884	51,348	-9,536	71.2
II. Revenue Expenditure	402,053	377,681	-24,372	100.0
of which				
Developmental Expenditure	220,671	204,631	-16,040	65.8
Non-Developmental Expenditure	174,068	166,150	-7,918	32.5
of which				
Interest Payments	83,967	81,763	-2,204	9.0
Pensions	35,279	33,028	-2,251	9.2
Administrative Services	30,303	28,847	-1,456	6.0
III. Revenue Deficit (II-I)	72,126	61,145	-10,981	
	2.6	2.2	-0.4	
IV. Capital Outlay	61,501	52,426	-9,075	100.0
of which				
Social Services	11,389	9,573	-1,816	20.0
Economic Services	47,604	40,810	-6,794	74.9
V. Net Lending	7,383	9,499	2,116	
VI. Gross Fiscal Deficit	141,010	123,070	-17,940	
	5.1 (4.0)	4.5 (3.4)	-0.6	

RE: Revised Estimates * : Denotes percentage share in relevant total

Note : Figures in italics are as percentages to GDP. Figures in italicised brackets are net of power bonds. During 2003-04 twenty six State Governments issued power bonds amounting to Rs. 28,984 crore.

Source : Budget Documents of State Governments.

is largely due to compression of revenue expenditure by Rs.24,372 crore (or 0.9 per cent of GDP). The revenue receipts particularly own non-tax revenue and grants from the Centre showed a decline. The developmental expenditure in revenue account declined substantially by Rs.16,040 crore (or 0.6 per cent of GDP) contributing 65.8 per cent of fall in revenue expenditure (Appendix Tables 3-4).

Apart from the reduction in RD as discussed above, there was a decline in capital outlay. Consequently, as mentioned earlier, GFD showed a decline of 0.6 per cent of GDP. Economic services and social services accounted for 74.9 per cent and 20.0 per cent of fall in 'capital outlay', respectively. Thus, overall correction in GFD was due to compression of developmental expenditure (includes expenditure on revenue and capital accounts and loans and advances extended by the States) by Rs.21,609 crore (or 0.8 per cent of GDP) (Appendix Tables 5-6 and 11-16).

II.A.(ii) Fiscal Position: Accounts 2003-04 vis-a-vis the Trend

A comparison of fiscal performance of the States in 2003-04 with that of the trend of the recent past indicated that, the imbalance in the revenue account continued as compared with the late 1990s, but witnessed an improvement over the period 2000-03. On the receipt side, notwithstanding increase in own tax revenue over time, own revenue experienced a setback due to falling own non-tax revenue. In revenue expenditure of States, non-developmental expenditure registered an upward trend led by committed expenditures such as interest payments and pensions, while developmental expenditure witnessed deceleration. Capital outlay as a ratio of GDP has recorded improvement over the past trend. The fiscal performance of the States in 2003-04 vis-a-vis the trends since the early 1990s is set out in Table III.

Table III: Trends in Major Fiscal Indicators

(As percentage to GDP)

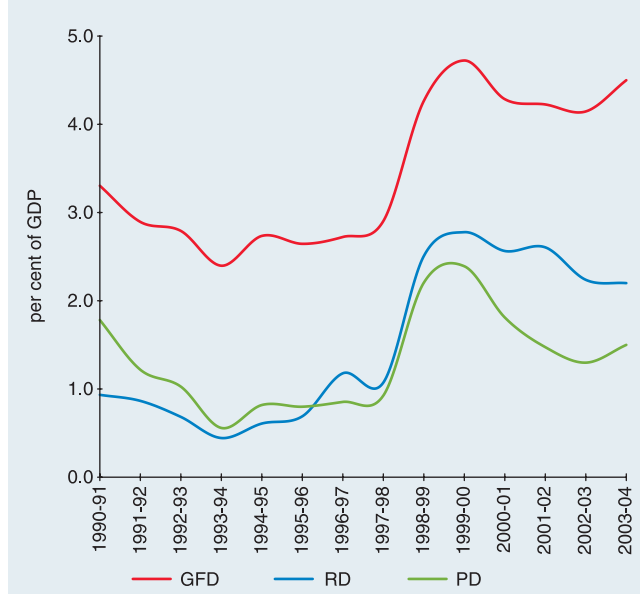
Item	1990-95 (Average)	1995-00 (Average)	2000-03 (Average)	2003-04
1	2	3	4	5
I. Revenue Receipts (i+ii)	12.1	10.9	11.3	11.5
(i) Tax Revenue (a+b)	8.0	7.7	8.0	8.2
(a) Own Tax Revenue	5.4	5.3	5.7	5.8
of which				
Sales Tax	3.2	3.1	3.46	3.54
(b) Share in Central Tax	2.6	2.4	2.3	2.4
(ii) Non-Tax Revenue	4.1	3.2	3.3	3.2
(a) States' Own				
Non-Tax Revenue	1.8	1.6	1.5	1.4
(b) Grants from Centre	2.3	1.6	1.9	1.9
II. Revenue Expenditure	12.8	12.6	13.8	13.7
of which				
Developmental Expenditure	8.4	7.6	7.7	7.4
Non-Developmental				
Expenditure	4.3	4.8	5.9	6.0
of which				
Interest Payments	1.7	2.0	2.7	3.0
Pensions	0.60	0.85	1.24	1.20
Administrative Services	1.21	1.14	1.17	1.05
III. Capital Outlay	1.6	1.4	1.5	1.9
of which				
Social Services	0.23	0.23	0.28	0.35
Economic Services	1.30	1.12	1.12	1.50
IV. Net Lending	0.6	0.4	0.3	0.3
Major Deficit Indicators				
I. Gross Fiscal Deficit	2.8	3.5	4.2	4.5 (3.4)
II. Revenue Deficit	0.7	1.6	2.5	2.2
III. Primary Deficit	1.1	1.4	1.5	1.5

Note : Figure in bracket is net of power bonds. During 2003-04 twenty six State Governments issued power bonds amounting to Rs.28,984 crore under the one-time settlement scheme.

Source : Same as Table II.

It may be noted that the ratio of RD to GDP in 2003-04 is higher than the average ratio in the second half of the 1990s, but it is lower by 0.3 percentage points from the average ratio during 2000-03 (Chart 1). However, resource gap in terms of GFD as percentage of GDP at 4.5 per cent in 2003-04, was one percentage point higher than the average GFD-GDP ratio during 1995-00. It is also marginally higher to the average GFD-GDP ratio of 4.2 per cent during 2000-03. However, it is important to note that there was a surge in the amount of GFD in 2003-04 due to issuing of power bonds under the one-time settlement scheme for dues of the SEBs by the State Governments. Net of power bonds, the ratio of GFD to GDP would be placed at 3.4 per cent in 2003-04 (Accounts).

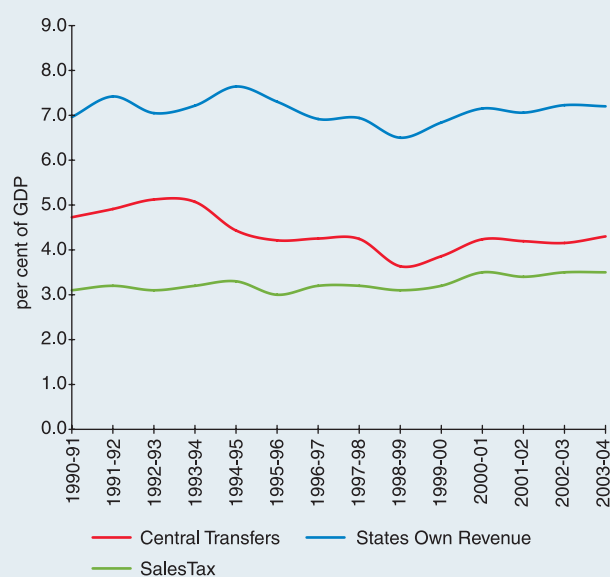
Chart 1: Trends in Deficit Indicators



In the revenue account, revenue receipts as a percentage of GDP increased to 11.5 per cent in 2003-04 from the average of 10.9 per cent during 1995-00, while it was still lower as compared to the average ratio of 12.1 per cent during 1990-95. On the other hand, revenue expenditure as a percentage of GDP in 2003-04 was close to 1 percentage point higher than the average in the 1990s.

The ratio of tax revenue to GDP remained around 8 per cent during the entire period 1990-2004, while the ratio of non-tax revenue to GDP declined by close to 1 percentage point from the average of 4.1 per cent during 1990-95 to 3.2 per cent during 2003-04. State's own tax-revenue as a ratio to GDP showed a gradual rise from the average level of 5.3 per cent during 1995-00 to 5.8 per cent in 2003-04. Amongst the components of non-tax revenue, gradual deterioration in own non-tax revenue was particularly evident as, in terms of percentage to GDP, it gradually declined from the average of 1.8 per cent during 1990-95 to 1.4 per cent in 2003-04. Grants from the Centre as a ratio to GDP during 2003-04 at 1.9 per cent was higher than the average level of 1.6 per cent during 1995-00 (Chart 2).

Chart 2: Trends in Major Components of Revenue Receipts



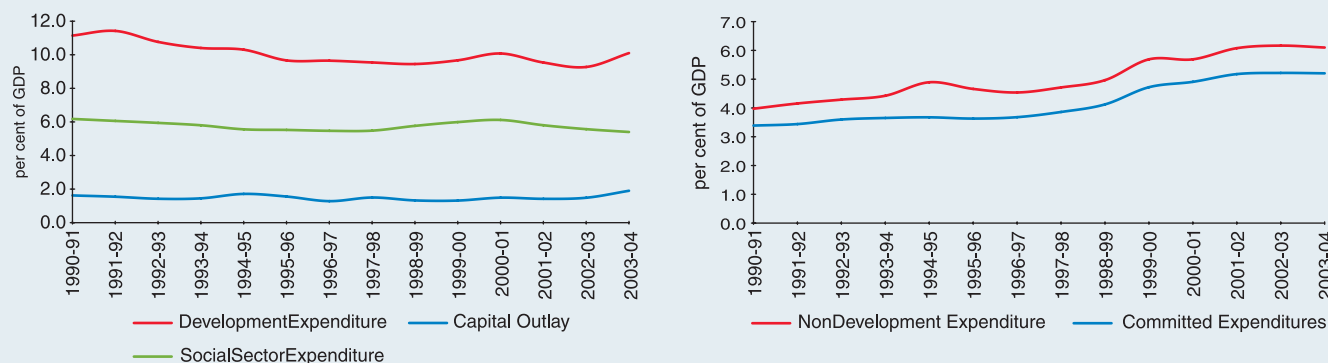
In revenue expenditure, as a percentage of GDP, the non-developmental expenditure gradually increased from the average of 4.3 per cent during 1990-95 to 6.0 per cent in 2003-04 while developmental expenditure exhibited a reverse trend from 8.4 per cent to 7.4 per cent over the same period. Among the components of non-developmental revenue expenditure, as a percentage of GDP, interest payments and pensions at 3.0 per cent and 1.2 per cent, respectively in 2003-04 were close to twice of their respective average ratio during the first half of the 1990s. While capital outlay as a percentage to GDP, showed a rise of 0.4 percentage point in 2003-04,

the net lending remained nearly stagnant as compared to the average level of 2000-03 (Chart 3).

II.B. Revised Estimates: 2004-05

The assessment of the variation in the revised estimates of 2004-05 over those of budget estimates revealed that there was an increase in RD by Rs.1,123 crore in the revised estimates of 2004-05 over the budget estimates due to higher revenue receipts. As a ratio to GDP, RD declined marginally to 1.4 per cent from the level of 1.5 per cent (Table IV). In the revenue account, increase in revenue receipts by Rs.9,858 crore (or 0.3 per cent of GDP) in 2004-05 (RE) over 2004-05 (BE) was more than compensated by increase in revenue expenditure by Rs.8,735 crore (or 0.3 per cent of GDP). Increase in revenue receipts was led by Rs.5,675 crore increase in Central grants and Rs.2,803 crore rise in share in Central taxes. The increase in Central transfers both in the form of share in Central taxes and grants accounted for 86.0 per cent of increase in revenue receipts of the States in 2004-05 (RE) over 2004-05 (BE). On the other hand, increase in revenue expenditure by Rs.8,735 crore in 2004-05 (RE) over 2004-05 (BE) was due to an increase in developmental expenditure by about Rs.14,862 crore (or 0.5 per cent of GDP) as against a decline in non-developmental expenditure by about Rs.6,886 crore (or 0.2 per cent of GDP). In non-developmental revenue expenditure, interest payments declined by about Rs.3,000 crore (or 0.1

Chart 3: Trends in Expenditures of State Governments



Note: Committed Expenditures includes Interest Payment, Pensions and Administrative Services.

Table IV: Variation in Major Items - 2004-05 (RE) over 2004-05 (BE)

(Rs. crore)				
Item	2004-05 (BE)	2004-05 (RE)	Variation (3 over 2)	Contribution * (per cent)
1	2	3	4	5
I. Revenue Receipts (i+ii)	374,581	384,439	9,858	100.0
(i) Tax Revenue (a+b)	263,557	268,170	4,613	46.8
(a) Own Tax Revenue	185,605	187,415	1,810	18.4
of which				
Sales Tax	112,737	115,330	2,593	26.3
(b) Share in Central Tax	77,952	80,755	2,803	28.4
(ii) Non-Tax Revenue	111,024	116,269	5,245	53.2
(a) States' Own				
Non-Taxes	49,612	49,181	-430	-4.4
(b) Grants from Centre	61,413	67,088	5,675	57.6
II. Revenue Expenditure	420,006	428,741	8,735	100.0
of which				
Developmental Expenditure	217,200	232,062	14,862	170.1
Non-Developmental Expenditure	195,595	188,709	-6,886	-78.8
of which				
Interest Payments	90,858	87,899	-2,959	-33.9
Pensions	38,370	38,142	-228	-2.6
Administrative Services	33,394	32,602	-791	-9.1
III. Revenue Deficit (II-I)	45,425	44,302	-1,123	
	1.5	1.4	-0.1	
IV. Capital Outlay	60,828	68,231	7,402	100.0
of which				
Social Services	12,463	12,987	523	7.1
Economic Services	45,208	51,769	6,561	88.6
V. Net Lending	8,394	11,103	2,709	
VI. Gross Fiscal Deficit	114,647	123,635	8,989	
	3.7	4.0	0.3	

RE : Revised Estimates

BE : Budget Estimates

*: Denotes percentage share in relevant total.

Note : Figures in italics are as percentages to GDP.

Source : Same as Table II.

per cent of GDP), largely due to benefits of DSS. Details of DSS are provided in Statement 32.

The revised estimates for 2004-05 marked a deterioration in the GFD as a proportion to GDP, registering an increase by 0.3 percentage points from 3.7 per cent in 2004-05 (BE) to 4.0 per cent in 2004-05 (RE) mostly due to higher provisions in capital outlay and net lending. Enhanced provision for capital outlay was mainly in respect of economic services, which constituted close to 90 per cent of the increase.

II.C. Budget Estimates: 2005-06

The gradual improvement in State finances, in terms of reduction in key deficit indicators, has also been envisaged to continue firmly in the State budgets for 2005-06 (Table V and Chart 4).

II.C.(i) Key Deficit Indicators

It is pertinent to note that RD at 0.7 per cent of GDP is budgeted to decline sharply by around 44.0 per cent (or 0.7 percentage points in terms of GDP) over the level of 2004-05 (RE). Consequent upon the significant reduction in the RD, the GFD-GDP ratio of the States is budgeted to decline by 0.8 percentage points to 3.2 per cent. Reflecting the reduction in RD and GFD, PD relative to GDP is also budgeted to decline by 0.7 percentage points to 0.5 per cent. The primary revenue balance with a surplus of 2.0 per cent of GDP during 2005-06 is budgeted to account for nearly three-fourth of interest payments in 2005-06 as compared with around half of the interest payments in the previous

Table V: Trends in Major Deficit Indicators of State Governments

(Rs. crore)						
Years	Gross Fiscal Deficit		Revenue Deficit		Primary Deficit	
	Primary Revenue Balance (PRB)					
1	2	3	4	5	6	7
1999-00	91,480	(4.7)	53,797	(2.8)	46,309	(2.4)
2000-01	89,532	(4.3)	53,569	(2.6)	37,830	(1.8)
2001-02	95,994	(4.2)	59,188	(2.6)	33,488	(1.5)
2002-03	1,02,123	(4.1)	55,111	(2.2)	31,981	(1.3)
2003-04	1,23,070	(4.5)	61,145	(2.2)	41,306	(1.5)
2004-05(RE)	1,23,635	(4.0)	44,302	(1.4)	35,737	(1.2)
2005-06(BE)	1,10,070	(3.2)	24,770	(0.7)	16,772	(0.5)

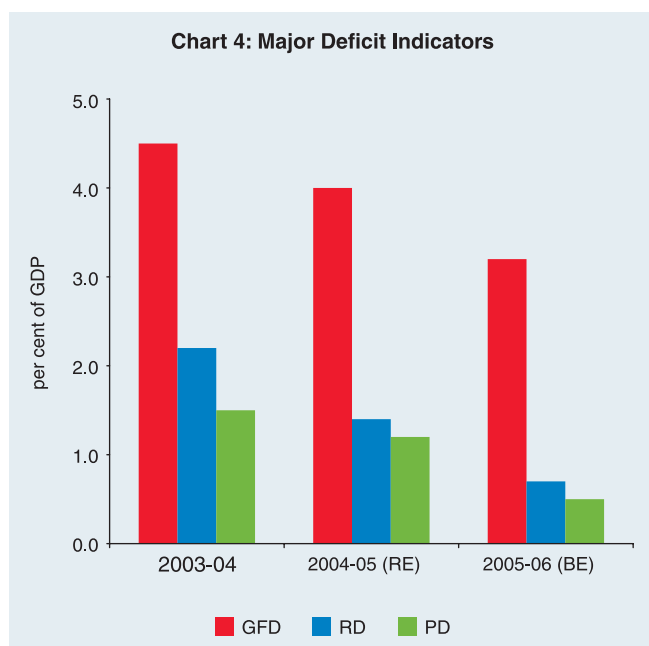
RE: Revised Estimates

BE: Budget Estimates

‘-’ sign in PRB indicates surplus

Note : Figures in brackets are percentages to GDP.

Source : Data on fiscal variables have been compiled from budget documents of State Governments. Source for data on GDP is Central Statistical Organisation (CSO).



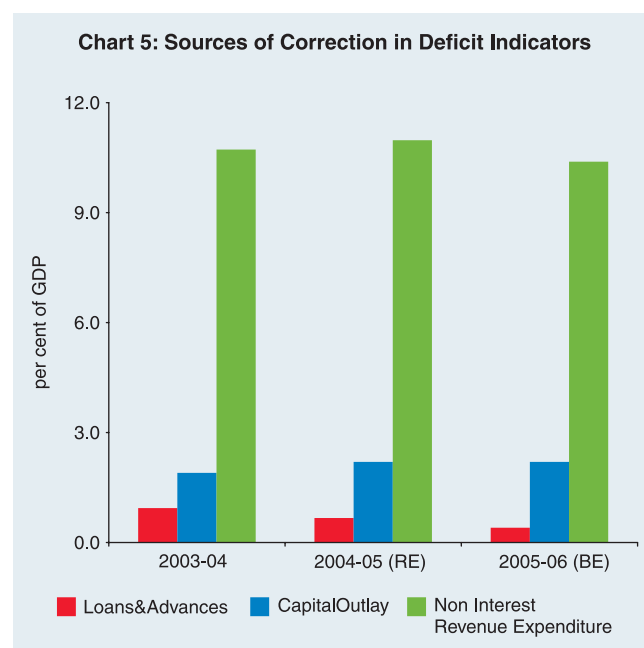
year. It is of interest to note that while 24 States had primary revenue surplus in 2004-05 (RE), there are 27 States, which are estimated to be in surplus in 2005-06.

The fiscal correction in the revenue account in 2005-06 is sought to be achieved primarily through containment of non-interest revenue expenditure, which is budgeted to decline by 0.6 percentage points (as proportion of GDP) over the previous year. The deficit reduction envisaged in the budgets of 2005-06 reflects the commitment of the State Governments to undertake fiscal restructuring in the direction of fiscal correction path as suggested by TFC. The TFC has stipulated enactment of FRL by the State Governments as a precondition for availing the debt-relief scheme recommended by it. Consequently, there is a progressive move by the State Governments to enact FRL. Many States, however, have not taken into account the recommendations of TFC relating to devolution of resources due to transfer and grants as well as phasing out of Plan loans from the Centre, which may alter the budget estimates quite significantly. Implementation of VAT by most of the States with effect from April 1, 2005 would also have implications for revenue mobilisation of States. Phasing out of Loans from the Centre to the States

as recommended by TFC would also have implications for market borrowings of the State Governments.

The reduction in non-interest revenue expenditure of the State Governments coupled with a decline in net lending (by 0.1 percentage point of GDP) and stagnant capital outlay to GDP ratio at 2.2 per cent together are budgeted to contribute to the decline in GFD-GDP ratio by 0.8 percentage points (Chart 5). The reduction in GFD-GDP ratio along with a reduction in interest payments as a ratio of GDP by 0.1 percentage point would contribute towards decline of PD-GDP ratio by 0.7 percentage point.

As explained earlier, the correction in revenue deficit (by Rs.19,531 crore or 0.7 per cent of GDP) envisaged in 2005-06 by the State Governments is budgeted to contain growth of non-interest revenue expenditure to 6.1 per cent from 15.2 per cent growth in 2004-05 (RE). Furthermore, it would be supported by an increase in revenue receipts by 11.9 per cent. The revenue expenditure (net of power sector) is budgeted to decelerate and grow by only 7.3 per cent compared to 17.3 per cent in 2004-05 (RE). As a ratio to GDP, revenue expenditure would decline to 13.1 per cent from



13.8 per cent in the previous year. Excepting for the smaller sectors such as nutrition, agricultural research and education, the deceleration in the revenue expenditure is perceived across all developmental sectors. Non-development expenditure is also poised for a lower growth excepting for administrative and miscellaneous general services. On the other hand, revenue receipts (inclusive of additional resource mobilisation (ARM) net of concessions) would increase by 11.9 per cent largely on account of the increase in sales tax mobilisation by 16.4 per cent, accounting for over 41 per cent of the increase (Statement 31). As a percentage to GDP, revenue receipts, however, would remain at the previous years' level of 12.4 per cent. Current devolution from the Centre (share in central taxes and grants) would account for 45 per cent of the increase in revenue mobilisation (Table VI).

The fiscal correction in 2005-06 as discussed above, however, is not uniform across the States. There are a few States, which have estimated an increase in RD (5 States) and GFD (11 States) in 2005-06 (BE) over 2004-05 (RE), while only a few States would account for the major part of the overall correction. The State-wise analysis of the fiscal correction process during 2005-06 reveals that the non-special category States account for nearly four-fifth of the overall correction⁹ in revenue account. The Government of Maharashtra has budgeted a surplus in its revenue account with a correction of Rs.9,666 crore which is around 63 per cent of overall RD reduction envisaged by the non-special category States.

Furthermore, non-special category States would contribute to around 74 per cent of the overall GFD correction of all States. Among non-special category States, Maharashtra as budgeted would account for about 96 per cent of the overall correction. Thus, the final outcome of fiscal correction of the States in 2005-06 would largely

Table VI: Variation in Major Items - 2005-06 (BE) over 2004-05 (RE)

Item	Variation		Contribution* (per cent)
	Amount (Rs. crore)	Per cent	
1	2	3	4
I. Revenue Receipts	45,830	11.9	100
of which			
Sales Tax	18,879	16.4	41.2
Share in Central Taxes	9,248	11.5	20.2
Grants-in-Aid	11,384	17.0	24.8
II. Revenue Expenditure	26,299	6.1	100
of which			
Education	6,111	8.1	23.2
Power	-3,586	-17.0	-13.6
Interest Payments	5,399	6.1	20.5
Administrative Services	4,752	14.6	18.1
Pension	3,519	9.2	13.4
Miscellaneous General services	4,994	61.0	19.0
Non Interest Revenue Expenditure	20,900	6.1	79.5
III. Capital Receipts	-113,335	-13.5	100
of which			
Market Borrowings (Gross)	-15,645	-42.2	13.8
Special Securities issued to NSSF	-24,333	-29.6	21.5
Recovery of loans	-4,163	-43.1	3.7
Suspense & Miscellaneous	-46,142	-13.0	40.7
Reserve Fund	-1,923	-10.2	1.7
Power Bonds and Other Bonds	-2,320	-100.0	2.0
IV. Capital Expenditure	-102,437	-12.8	100
of which			
Capital Outlay	8,533	12.5	-8.3
Capital Outlay on Urban Development	1,728	99.1	-1.7
Capital Outlay on Irrigation & Flood Control	2,853	13.1	-2.8
Capital Outlay on Energy	-3,232	-34.4	3.2
Transport	3,117	27.4	-3.0
Discharge of Internal Debt	-52,747	-43.4	51.5
Repayments of loans to Centre	-13,305	-49.0	13.0
Loans for Power Projects	-4,815	-42.5	4.7
Suspense & Miscellaneous	-44,091	-12.4	43.0

BE: Budget Estimates RE: Revised Estimates

* : Denotes percentage share in relevant total

Source : Same as Table II.

be dependent on the fiscal performance of Maharashtra (Table VII).

The decomposition of GFD indicates that the share of the revenue deficit would decline substantially to 22.5 per cent in 2005-06 from 35.8 per cent in the previous year. Small savings (NSSF) and market borrowings of the State

⁹ Overall correction refers to total correction with some States budgeting a decline in RD and GFD while other States have budgeted an increase.

Table VII: State-wise Correction of Revenue Deficit and Gross Fiscal Deficit (2005-06 (BE) over 2004-05 (RE))

(Amount in Rs. crore)

	States	Revenue Deficit		Gross Fiscal Deficit	
		Correction over 2004-05 (RE)	Percentage To Total	Correction over 2004-05 (RE)	Percentage To Total
1		2	3	4	5
A. Special Category					
1	Arunachal Pradesh	-25	0.6	-172	4.8
2	Assam	-1,124	27.5	-1,504	41.8
3	Himachal Pradesh	-964	23.6	-990	27.6
4	Jammu and Kashmir	-540	13.2	258	-7.2
5	Manipur	-495	12.1	-542	15.1
6	Meghalaya	5	-0.1	35	-1.0
7	Mizoram	-98	2.4	-255	7.1
8	Nagaland	-105	2.6	-11	0.3
9	Sikkim	-23	0.6	-112	3.1
10	Tripura	-88	2.1	146	-4.1
11	Uttaranchal	-626	15.3	-446	12.4
	Total (A)	-4,083	100.0	-3,594	100.0
B. Non-Special Category					
1	Andhra Pradesh	-60	0.4	1,673	-16.8
2	Bihar	-479	3.1	-62	0.6
3	Chhattisgarh	-251	1.6	97	-1.0
4	Goa	-34	0.2	64	-0.6
5	Gujarat	-2,660	17.2	-2,761	27.7
6	Haryana	722	-4.7	1,297	-13.0
7	Jharkhand	7	-0.05	230	-2.3
8	Karnataka	-347	2.2	523	-5.2
9	Kerala	-493	3.2	-128	1.3
10	Madhya Pradesh	2,673	-17.3	-1,154	11.6
11	Maharashtra	-9,666	62.6	-9,533	95.6
12	Orissa	-1,111	7.2	-1,356	13.6
13	Punjab	-800	5.2	-383	3.8
14	Rajasthan	-1,125	7.3	-85	0.8
15	Tamil Nadu	-283	1.8	898	-9.0
16	Uttar Pradesh	-1,773	11.5	-154	1.5
17	West Bengal	739	-4.8	1,271	-12.7
18	NCT Delhi	-509	3.3	-409	4.1
	Total (B)	-15,448	100.0	-9,971	100.0

Source : Same as Table II.

Governments though continue to be the major source for GFD financing, are budgeted to finance a lower proportion of the GFD during 2005-06 as compared to 2004-05 (RE). Loans from the Centre are budgeted to finance an increased proportion (15.8 per cent) of the States' borrowings requirements (Table VIII and Appendix Tables 7-9 and Statement 6-11).

II.C.(ii) Revenue Receipts

The revenue receipts are budgeted to increase by 11.9 per cent during 2005-06 as compared with a growth rate of 21.5 per cent in the preceding year. In terms of GDP, however, revenue receipts have been envisaged to remain constant at 12.4 per cent. States' own revenue as a ratio to GDP is estimated to be marginally lower in 2005-06 compared to the previous year while transfers from the Centre are budgeted to remain constant (Table IX).

Amongst the components of revenue receipts, States' own tax revenue as percentage to GDP is expected to show a marginal increase during 2005-

Table VIII: Decomposition and Financing Pattern of Gross Fiscal Deficit - 2004-05 (RE) to 2005-06 (BE)

(per cent)

Item	2004-05 (RE)	2005-06 (BE)
1	2	3
Decomposition (1+2+3)	100.0	100.0
1. Revenue Deficit	35.8	22.5
2. Capital Outlay	55.2	69.7
3. Net Lending	9.0	7.8
Financing (1 to 11)	100.0	100.0
1. Market Borrowings	26.4	14.6
2. Loans from Centre	4.7	15.8
3. Special Securities issued to NSSF/Small Savings	43.4	47.8
4. Loans from LIC, NABARD, NCDC, SBI & Other Banks	2.3	7.3
5. State Provident Fund	7.8	7.2
6. Reserve Funds	5.0	3.8
7. Deposits and Advances	-1.0	-2.5
8. Suspense and Miscellaneous	0.5	-1.3
9. Remittances	-0.8	1.5
10. Increase (+)/Decrease (-) in Cash Balance	-5.5	1.0
11. Others	17.1	4.7

BE: Budget Estimates

RE: Revised Estimates

NSSF: National Small Savings Fund

Notes : (i) Overall surplus/deficit would be matched by increase/decrease in cash balance since 2003-04. This is due to Cash Balance Investment Account now included under 'Suspense and Miscellaneous' while WMA/OD from RBI is included under 'Internal Debt'.
(ii) 'Others' (item '11') includes miscellaneous capital receipts, Contingency Fund, inter-State settlement, WMA/OD from RBI, etc.

Source : Same as Table II.

Table IX: Aggregate Receipts of State Governments

(Rs. crore)

Items	2005-06 (BE)	2004-05 (RE)	2003-04 (Accounts)	2000-03 (Avg.)	1995-00 (Avg.)	1990-95 (Avg.)	Variations (per cent)	
							Col.3/4	Col.2/3
1	2	3	4	5	6	7	8	9
Aggregate Receipts (1+2)	1,155,807 (33.2) <i>16.7</i>	1,223,312 (39.4) <i>19.0</i>	1,330,584 (48.2) <i>19.1</i>	(16.8)	(15.2)	(16.1)	-8.1	-5.5
1. Total revenue receipts (a+b)	430,270 (12.4)	384,439 (12.4)	316,536 (11.5)	(11.3)	(10.9)	(12.1)	21.5	11.9
(a) States own Revenue	261,795 (7.5)	236,596 (7.6)	198,109 (7.2)	(7.2)	(6.9)	(7.3)	19.4	10.7
States own tax	215,243 (6.2)	187,415 (6.0)	159,921 (5.8)	(5.7)	(5.3)	(5.4)	17.2	14.8
States own non tax	46,552 (1.3)	49,181 (1.6)	38,189 (1.4)	(1.5)	(1.6)	(1.8)	28.8	-5.3
(b) Central Transfers	168,475 (4.8)	147,843 (4.8)	118,426 (4.3)	(4.1)	(4.0)	(4.9)	24.8	14.0
Shareable taxes	90,003 (2.6)	80,755 (2.6)	67,079 (2.4)	(2.3)	(2.4)	(2.6)	20.4	11.5
Central Grants	78,472 (2.3)	67,088 (2.2)	51,348 (1.9)	(1.9)	(1.6)	(2.3)	30.7	17.0
2. Capital Receipts (a+b)	725,537 (20.8) <i>4.3</i>	838,873 (27.0) <i>6.6</i>	1,014,048 (36.7) <i>7.6</i>	(5.5)	(4.2)	(4.0)	-17.3	-13.5
(a) Loans from Centre@	31,216 (0.9)	32,940 (1.1)	26,127 (0.9)	(1.0)	(1.0)	(1.2)	26.1	-5.2
(b) Others Capital Receipts	694,321 (19.9)	805,932 (26.0)	987,921 (35.8)	(4.4)	(3.2)	(2.9)	-18.4	-13.8

@ With the change in the system of accounting with effect from 1999-2000, States' share in small savings which was included earlier under loans from Centre is included under internal debt and shown as special securities issued to National Small Saving Fund (NSSF) of the Central Government. The data for the years prior to 1999-2000 as reported in this Table, however, exclude loans against small savings, for the purpose of comparability.

Notes : 1. Figures in brackets are percentages to GDP.

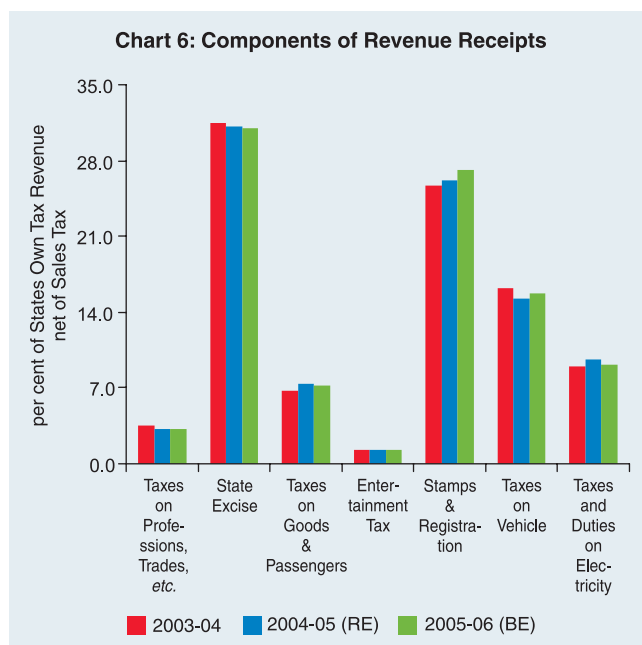
2. Since 2003-04, the data on capital receipts are on a gross basis and therefore, not comparable with that of earlier years. Figures in *italics* are also percentages to GDP and are on a net basis (for items of public account) and given for comparison with earlier years.

Source : Same as Table II.

06. The implementation of the VAT by majority of the State Governments would have an important bearing on the States' own tax revenues during the current year. As there is a provision for compensating the revenue loss incurred by the States following the implementation of the VAT, it is unlikely that shifting to the VAT regime will have any adverse impact on revenue receipts for the current year. Excluding sales tax revenue (which is the predominant tax) while the share of Stamps and Registration fees in States' Own Revenue has increased over the period, the shares of Profession Tax, Tax on Goods and Passengers and Electricity Duties have recorded declines. Taxes other than Sales Tax of State Governments need to be exploited for higher revenue mobilisation (Chart 6).

States' own non-tax revenue, on the other hand, is budgeted to decline to 1.3 per cent of

GDP in 2005-06 from the previous year's level of



1.6 per cent of GDP, mainly as a result of a sharp decline in interest receipts. The inapt application of user charges by State Governments due to various constraining factors has resulted in inadequate recoveries from public services and hence the subdued levels of non-tax revenues. The information on cost recovery of select services are set out in Table X. It may be mentioned that the sudden rise in non-tax receipts from the power sector in 2004-05 (RE) is due to Madhya Pradesh accounting for 56.3 per cent of the rise due to repayment by Madhya Pradesh Electricity Board. Hence, the sudden rise in cost recovery from power sector in 2004-05 (RE) (Chart 7).

The rate of return from investment by State Governments has been very low. It may be observed from Chart 8 that while the share of interest receipts in non-tax receipts would decline in 2005-06, the shares of dividends and profits have remained abysmally low. The Eleventh Finance Commission had observed that the average rate of return on capital invested in the State Electricity Boards that account for the bulk of the States' investment in Public Sector Undertakings, had been persistently negative.

II.C.(iii) Revenue Expenditure

Revenue expenditure is budgeted to increase by 6.1 per cent in 2005-06 as compared with 13.5

Table X: Cost Recovery of Select Services
(Ratio of Non-Tax Revenue to Non-Plan Revenue Expenditure)

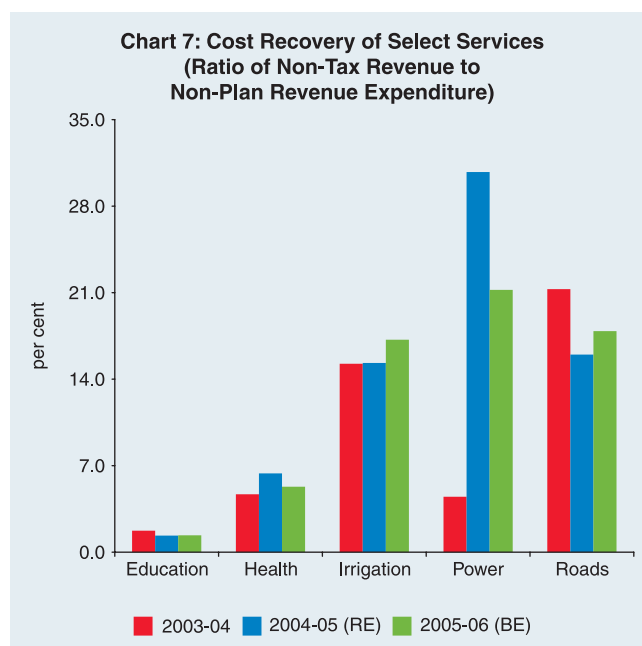
(per cent)						
Items	2000-01	2001-02	2002-03	2003-04	2004-05 (RE)	2005-06 (BE)
1	2	3	4	5	6	7
Social Services						
(a) Education	1.2	1.2	1.6	1.7	1.3	1.4
(b) Health	4.6	6.1	5.4	4.7	6.4	5.3
Economic Services						
(a) Irrigation#	8.2	7.5	8.4	15.2	15.3	17.2
(b) Power	6.5	6.4	5.8	4.5	30.8	21.2
(c) Roads	16.1	19.3	15.5	21.3	16.0	17.9

BE : Budget Estimates

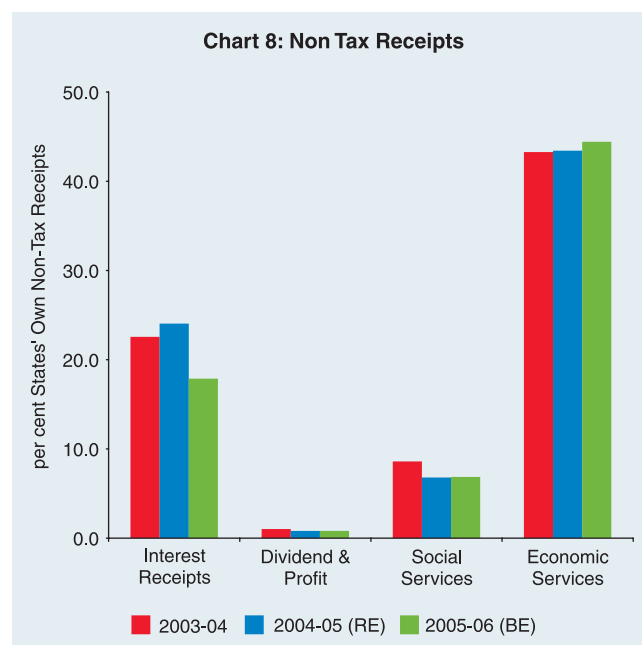
RE: Revised Estimates

: Relates to irrigation and flood control for non-plan revenue expenditure.

Source : Same as Table II.



per cent increase in the previous year. As a ratio to GDP, revenue expenditure would decline to 13.1 per cent from 13.8 per cent in the previous year, but would still remain higher than the average level of 12.8 per cent during the first half of the 1990s. The increase in revenue expenditure during 2005-06 would emanate to a large extent from the increase in expenditure on education, sports, art and culture. Further, provisions in respect of interest payments,



administrative services, miscellaneous general services (including lotteries) and pensions are budgeted for substantial increases in 2005-06 (Table VI). Interest payments and pensions are, however, expected to pre-empt a lower proportion (31.4 per cent) of revenue receipts in 2005-06 compared to 32.8 per cent in the previous year (Chart 9). Among the few sectors for which revenue expenditure is budgeted to decline, the power sector's sharp decline of 17 per cent stands out (Appendix Table 17-18).

II.C.(iv) Capital Receipts

The impact of some of the recent developments in State finances would be largely on the capital account. Discontinuation of DSS has entailed the entire small savings collections accruing to the States. As per the recommendations of TFC, Central loans for State Plans would be phased out. Capital receipts are budgeted to decline by 13.5 per cent in 2005-06 as against a decline of 17.3 per cent in the previous year. Most of the reduction in capital receipts in 2005-06 is due to the substantial decline in Special Securities issued to NSSF (29.6 per cent) and market borrowings (42.2 per cent) from their levels in the previous year. It needs to be mentioned that the State Governments have budgeted a substantially lower

amount than budgeted by Union Budget 2005-06 in respect of Securities issued to NSSF.

Gross loans from the Centre are budgeted to record a decline of 5.2 per cent in 2005-06 as against an increase of 26.1 per cent in the previous year. As ratio to GDP, gross loans from the Centre would, therefore, decline to 0.9 per cent in 2005-06 from 1.1 per cent in the previous year. It may be stated that the TFC has recommended phasing out of Central loans for State plan schemes and accordingly the Union Budget for 2005-06 has not provided for the same. Loans from financial institutions have experienced decline (as percentage of States' own capital receipts) in recent years and are also budgeted for a decline of 5.2 per cent in 2005-06 (BE) mainly due to loans from LIC. The major components of capital receipts as a ratio to total capital receipts (net of recoveries) of the States are depicted in Chart 10.

II.C.(v) Market Borrowings

The net allocation of market borrowings to the State Governments, as per Reserve Bank Records, have increased since 2002-03 (Table XI and Statement 29). Additional allocations have, however, witnessed a sharp decline over this period. Taking cognisance of repayments, gross allocation of market loans is budgeted to decline sharply to

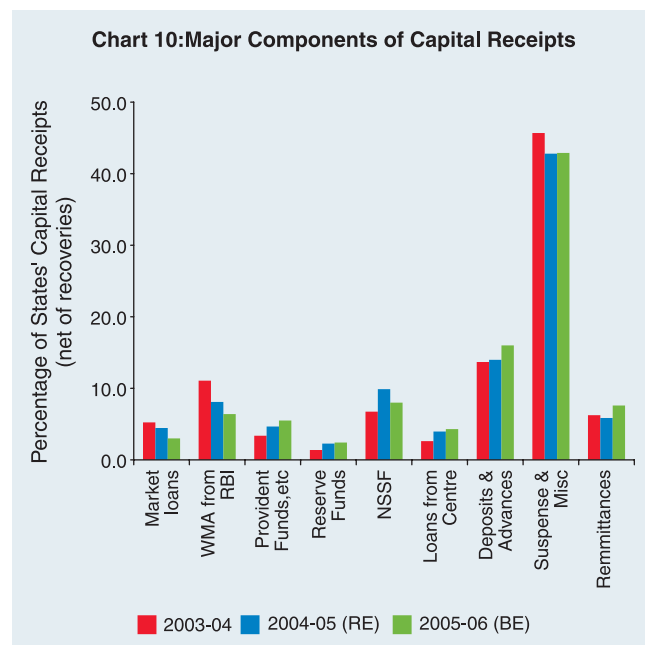
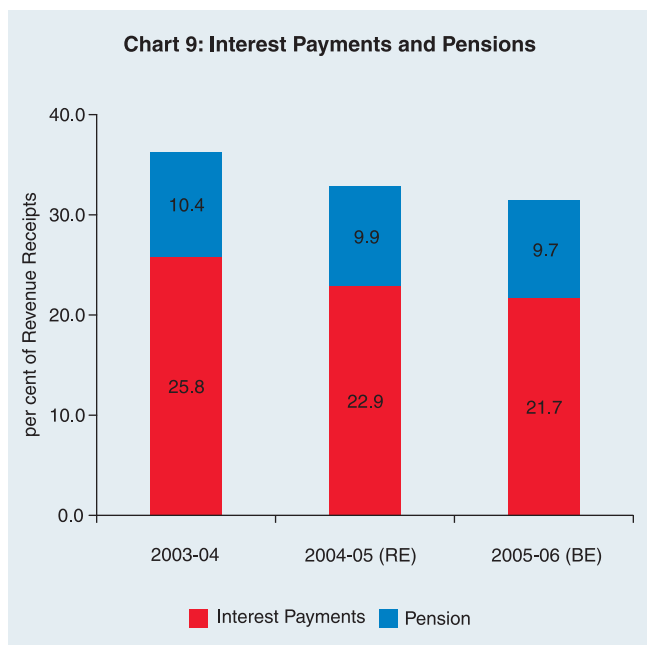


Table XI: Market Borrowings of State Governments

(Rs. crore)

Items	2002-03	2003-04	2004-05	2005-06*
1	2	3	4	5
1. Net Allocation	12,722	12,767	13,969	16,112
2. Additional Allocation	6,422	4,893	4,160	2,159
3. Allocation under DSS	10,000	29,000	18,805	—
4. Total (1+2+3)	29,144	46,660	36,935	18,272
5. Repayments	1,789	4,145	5,123	6,274
6. Gross Allocation (4+5)	30,933	50,805	42,058	24,546
7. Amount raised under DSS	10,000	26,623	16,943	—
8. Amount raised to prepay RIDF loans	—	—	—	1,387
9. Total Amount Raised	30,853	50,521	39,101	16,184
Through				
Tap Issues	27,880	47,626	38,216	11,186
Auctions	2,973	2,895	885	4,999
	(13)	(8)	(3)	(14)
10. Net Amount Raised (9-5)	29,064	46,376	33,978	9,910
11. Net Amount Raised (other than DSS) (9-7)	20,853	23,898	22,158	16,184
12. Net Amount Raised (other than DSS & RIDF) (11-8)	20,853	23,898	22,158	14,797
<i>Memo-Items</i>				
(i) Coupon/Cut-off Yield Range (%)	6.67-8.00	5.78-6.40	5.60-7.36	7.32-7.77
(ii) Weighted Average Interest Rate (%)	7.49	6.13	6.32	7.60
(iii) Average Maturity (in years)	10.00	10.05	10.01	10.00

DSS : Debt Swap Scheme '—': Nil/Not Applicable

RIDF: Rural Infrastructure Development Fund

*: Amount raised up to January 20, 2006

Notes : (i) Figures in brackets represent number of States opting for the auction route.

(ii) The data on market borrowings as per RBI records may differ from that reported in the budget documents of the State Governments.

Source : As per Reserve Bank records.

Rs.24,546 crore in 2005-06 (Appendix Table 10). Incorporating the net Central loans for State Plans as reported in the Union Budget 2005-06 and assuming that the State Plans are maintained at the budgeted level, the market borrowings during 2005-06 would not be substantially higher than the budgeted level on account of higher devolution of taxes and grants as envisaged in the Union Budget in accordance with the TFC recommendations and larger receipts from NSSF.

Nearly two-third of the gross allocated amount has been raised during 2005-06 so far (January 20, 2006). The rate of interest on market

loans which had declined since the mid-1990s upto 2003-04, firmed up during 2004-05 and further during 2005-06 so far. Open market loans of some of the State Governments have faced problems of under-subscription in recent years. Factors that influenced the liquidity of the market for State Government bonds include the health of the finances of the State Governments, the credibility of their prospective policy actions and transparency of their budgets.

The weighted average maturity of State Governments securities issued during the current year was at the same level of 10 years since 2002-03. In the composite portfolio of outstanding market loans of the State Governments, securities in the maturity range of 6-10 years constituted the largest share (62.8 per cent), followed by 0-5 years (25.9 per cent) and above 10 years (11.3 per cent) (Statements 36-37). The State-wise and scrip-wise details of outstanding market loans are presented in Statement 33.

II.C.(vi) Capital Expenditure

Capital disbursements (including the public account) would decline by 12.8 per cent in 2005-06 as against a decline of 16.0 per cent in the previous year. Over half of the decline in capital disbursements would be on account of discharge of internal debt (mainly NSSF and WMA from RBI). Another 43 per cent of the decline would emanate from suspense and miscellaneous account particularly Cash Balance Investment Account.

Capital outlay is envisaged to increase by 12.5 per cent during 2005-06 compared with 30.1 per cent increase in the previous year. As a ratio to GDP, capital outlay would, however, be maintained at 2.2 per cent in 2005-06, as that of in the previous year. Repayments on account of loans from Centre have been budgeted for a sharp decline in 2005-06 on account of State Plan Schemes in respect of States such as Tamil Nadu, Madhya Pradesh, NCT Delhi and Rajasthan.

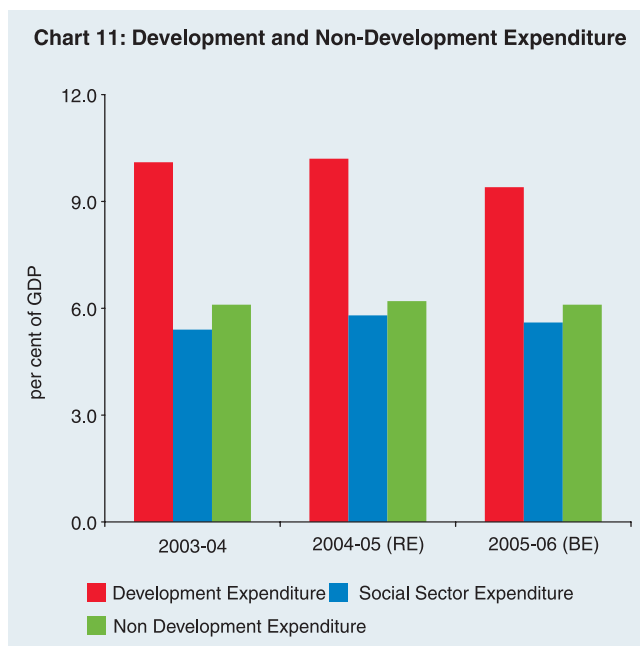
II.C.(vii) Devolution and Transfer of Resources from the Centre

Gross devolution and transfer of resources (i.e., shareable tax revenue, grants and loans and advances) from the Centre are estimated to increase by 10.5 per cent to Rs.1,99,691 crore in 2005-06 compared with a growth of 25.1 per cent in the previous year. As a ratio to GDP, gross devolution and transfers from the Centre would decline marginally to 5.7 per cent in 2005-06 from 5.8 per cent in the previous year and from the average level of 6.8 per cent during the first half of the 1990s. Gross devolution and transfers from the Centre would finance 17.3 per cent of the aggregate disbursements of the State Governments in 2005-06 as compared with 14.7 per cent in the previous year. The prospective (from 2005-06 to 2009-10) mechanism of devolution of transfer of resources from the Centre to the States would, however, be in accordance with the recommendations of the Twelfth Finance Commission (Appendix Table 19 & Statement 25).

II.C.(viii) Developmental and Non-Developmental Expenditure

The fiscal correction envisaged in the State Budgets of 2005-06 may adversely impact upon their development expenditure. Total developmental expenditure (revenue plus capital) would be placed lower at 9.4 per cent of GDP in 2005-06 compared to 10.2 per cent in the previous year (Chart 11). The growth rate of almost all major developmental heads under revenue expenditure is budgeted to decelerate. Within developmental expenditure, social sector expenditure (comprising social services, food storage, rural development and warehousing) would be placed at 5.6 per cent of GDP in 2005-06 as compared with 5.8 per cent in the previous year (Appendix Tables 11-16).

Furthermore, non-developmental expenditure in 2005-06 at 6.1 per cent would be marginally lower than the previous year's level of 6.2 per cent of GDP. Within non-developmental revenue expenditure, the



growth rate of interest payments would decelerate, while that of administrative services is estimated to increase sharply. Non-Plan Non-Developmental expenditure, as ratio to GDP, would be placed at 5.9 per cent, lower than the previous year's level of 6.1 per cent. In the aggregate, the ratio of developmental expenditure to GDP would record a larger decline than that of non-developmental expenditure to GDP during 2005-06. It may be mentioned that committed expenditure (consisting of interest payments, administrative services and pension), which had been rising in the past, showed some signs of stabilising in the recent years. As a percentage of revenue expenditure, it would remain at around 38 per cent. As ratio to own revenue, committed expenditure would, however, go down from 72.5 per cent in 2003-04 to 66.0 per cent in 2005-06 (BE). There is considerable variation across the States as can be seen from the Statements 34 and 35.

Against the above backdrop, the expenditure pattern in detail is given in Table XII.

II.C.(ix) Liquidity and Cash Management

A revised Scheme of WMA was affected on March 3, 2003 based on the recommendations of the Ramachandran Committee and after consultations with the State Governments. Under

Table XII: Expenditure Pattern of State Governments

(Rs. crore)

Items	2005-06 (BE)	2004-05 (RE)	2003-04 (Accounts)	2000-03 (Avg.)	1995-00 (Avg.)	1990-95 (Avg.)	Variations (per cent)	
							Col.3/4	Col.2/3
1	2	3	4	5	6	7	8	9
Aggregate Expenditure (1+2 =3+4+5)	1,153,938 (33.1) <i>16.6</i>	1,230,076 (39.6) <i>19.1</i>	1,331,748 (48.3) <i>19.1</i>	(16.7)	(15.3)	(16.0)	-7.6	-6.2
1. Revenue Expenditure <i>of which</i>	455,040 (13.1)	428,741 (13.8)	377,681 (13.7)	(13.8)	(12.6)	(12.8)	13.5	6.1
Interest payments	93,298 (2.7)	87,899 (2.8)	81,763 (3.0)	(2.7)	(2.0)	(1.7)	7.5	6.1
2. Capital Expenditure <i>of which</i>	698,898 (20.1) <i>3.5</i>	801,335 (25.8) <i>5.3</i>	954,068 (34.6) <i>5.4</i>	(2.9)	(2.7)	(3.2)	-16.0	-12.8
Capital outlay	76764 (2.2)	68231 (2.2)	52426 (1.9)	(1.5)	(1.4)	(1.6)	30.1	12.5
3. Developmental Expenditure	325,672 (9.4)	316,172 (10.2)	280,099 (10.1)	(9.6)	(9.6)	(10.8)	12.9	3.0
4. Non-Developmental Expenditure	211,368 (6.1)	193,602 (6.2)	169,021 (6.1)	(6.0)	(4.9)	(4.3)	14.5	9.2
5. Others*	616,898 (17.7)	720,303 (23.2)	882,628 (32.0)	(1.2)	(0.7)	(0.9)	-18.4	-14.4
<i>Memo-Item</i> <i>Non-Plan Non-Developmental Expenditure</i>	(5.9)	(6.1)	(6.0)	(5.9)	(4.8)	(4.3)	14.0	8.2

* Comprises Compensation and Assignments to local bodies, Grants-in-aid and contributions, Reserve with Finance Department, Discharge of Internal Debt, Repayment of loans to the Centre till 2002-03. Since 2003-04, it also includes Inter-State Settlement, Contingency Fund, Small Savings, Provident Fund, etc., Reserve Funds, Deposits & Advances, Suspense & Miscellaneous, Appropriation to Contingency Fund and Remittances.

Notes : 1. Figures in brackets are percentages to GDP.

2. Capital expenditure starting with 2003-04 includes corresponding heads of public account, which were hitherto included on a net basis under capital receipts. The figures, therefore, are not comparable with that of earlier years. Figures in italics are also percentages to GDP with expenditure heads of public account being excluded from capital expenditure and are given for comparison with earlier years.

Source : Same as Table II.

the revised Scheme, the total normal WMA limit for the State Governments was enhanced by 18.8 per cent and further by 13.5 per cent (to Rs.8,140 crore) with effect from April 1, 2004. During 2005-06, the total normal WMA limit was increased further by 9.8 per cent to Rs.8,935 crore with effect from April 1, 2005 (Table XIII).

Most of the State Governments lessened their recourse to normal WMA and overdrafts (OD) during 2004-05. This reflected a change mainly on account of the provision under the revised Scheme that special WMA should be availed before taking recourse to normal WMA. The special WMA facility is linked to the investment in Government of India Securities by the State Governments. The rate of interest charged on special WMA is one percentage point less than that on normal WMA. Higher mobilisation of Small

Savings and enhanced market borrowings (other than those under the DSS) also facilitated the reduction in recourse to normal WMA. Furthermore, the frequency of overdrafts declined in the case of all States during 2004-05 (Statement 38).

Table XIII: Normal WMA Limits - 1996 to 2005

Period	Amount (Rs. crore)	Increase over earlier limits (per cent)
1	2	3
1. August 1996 to February 1999	2,234	100.0
2. March 1999 to January 2001	3,941	76.4
3. February 2001 to March 2002	5,283	34.1
4. April 2002 to March 2, 2003	6,035	14.2
5. March 3, 2003 to March 31, 2004	7,170	18.8
6. April 1, 2004 to March 31, 2005	8,140	13.5
7. April 1, 2005 to till date	8,935	9.8

Source : As per RBI records.

During 2005-06 so far (upto December, 2005), the average utilisation of WMA and OD has been lower than that in the corresponding period of the previous year (Chart 12). The frequency of resort to OD has also been lower during 2005-06 (so far) than that in the (full) previous year. Even so, a few State Governments such as Assam, Kerala, Maharashtra and Uttar Pradesh have resorted to OD much more frequently than the other State Governments during 2005-06 so far. The trend in the actual recourse to WMA/OD by the States from the Reserve Bank during 2005-06 so far (upto January 18, 2006), generally reflected the surplus cash balances of the State Governments.

Apart from the WMA from the Reserve Bank, the Central Government also provides WMA to the State Governments, which unlike the former is, however, not a direct source of monetary expansion. Data on Centre's (gross) WMA to the State Governments, as reported in the budget documents of the State Governments, during 2000-01 to 2005-06 (BE) are set out in Statement 39. The total amount of such advances has declined from Rs.3,329 crore in 2002-03 (12 States) to Rs.1,315 crore in 2004-05 (7 States). Among the Special Category States, these advances have been

persistent and usually large in the case of Manipur. Non-Special Category States like Punjab and Kerala have also accessed these advances to different degrees, but not to the same extent as Manipur. Five States viz., Assam, Kerala, Manipur, Nagaland and Punjab have budgeted for such advances in 2005-06. This probably reflects their anticipation of continued short-term (liquidity) pressures on their budgets. Furthermore, States like Manipur, Kerala, and Punjab which accessed a relatively higher amount of WMA from the Centre, are also the ones in respect of which the number of occasions as well as the number of days on which overdrafts were resorted to from the Reserve Bank, remained high during 2004-05.

Another issue that has a bearing on the liquidity management by the State Governments relates to their surplus cash balance. The surplus cash balances of State Governments, as reflected in their investments in 14-Day Intermediate Treasury Bills, have been rising during recent years. They have also risen sharply since the beginning of the financial year 2005-06 and are placed much higher than in the corresponding period of the previous year. The investment (weekly average) in 14-Day Intermediate Treasury Bills increased from Rs.14,764 crore during the month of April to Rs.44,109 crore in December 2005, which is reflective of improved liquidity position of the State Governments (Statement 40).

Chart 12: Utilisation of WMA and Overdraft (Weekly Average)



II.C.(x) Likely Outturn of Budget Estimates of 2005-06: A Technical Exercise

Evidence suggests that the likely outturn of fiscal position during a year undergoes large slippages from that of the budget estimates. This is usually reflected in an over-estimation of revenue receipts and under-estimation of revenue expenditure. The analysis of the data for period 1999-2004 indicates that on an average RD and GFD deviated from their budget estimates by 31 per cent and 15 per cent, respectively, in the revised estimates. In view of this, a technical exercise has

been attempted to assess the likely outturn of budget estimates of 2005-06 by correcting for the over/under-estimation.

The error estimation in budget estimates were worked out taking into account the slippages under different heads of budgetary items of budget estimates over revised estimates on the basis of 5-yearly annual average for the period 2000-01 to 2004-05 (Table XIV).

Taking into account the direction and magnitude of the slippages as indicated in Table XIV, an attempt has been made to correct the likely slippage in the budget estimates for 2005-06 to arrive at a likely outturn. It may be mentioned that many of the State Governments have not taken into account recommendations of TFC regarding devolution and transfer of resources while presenting their budgets. The Union Government has, however, considered the same in its Budget for 2005-06. While adjustments in sharable Central taxes and grants have been made as provided in the Union Budget 2005-06, the other items of receipts and expenditure have been adjusted for slippages in revised estimates over budget estimates, based on trend averages of last five years (Table XV).

In terms of the reassessed data, the likely

Table XIV: Deviation from Budget Estimates of Major Budgetary Items

Item	Percentage Deviation
1	2
1. Revenue Receipts (a+b+c+d)	@
a. Own Tax Revenue	-3.57
b. Own Non Tax Revenue	-2.52
c. Share in Central taxes	-2.87
d. Grants	-2.93
2. Revenue Expenditure (a+b)	@
a. Interest Payments	+0.16
b. Non-Interest Revenue Expenditure	+3.08
3. Revenue Deficit	@
4. Capital Outlay	+3.11
5. Net Lending	+2.18
Gross Fiscal Deficit (3+4+5)	@

@ : Not independently estimated
 '-' : indicates overestimation
 '+' : indicates underestimation

Table XV: Likely Outturn for 2005-06 for State Government Finances

(Rs. crore)

Item	Budget Estimates	Likely Outturn	Variation
1	2	3	4 (3-2)
I. Revenue Receipts (a+b+c+d)	430,270	426,377	-3,893
(a) Own Tax Revenue	215,243	207,559	-7,684
(b) Own Non Tax Revenue	46,552	45,379	-1,173
(c) Share in Central taxes	90,003	94,959	4,956
(d) Grants	78,472	78,480	8
II. Revenue Expenditure (a+b)	455,040	466,331	11,291
(a) Interest Payments	93,298	93,447	149
(b) Non-Interest Revenue Expenditure	361,742	372,884	11,142
III. Revenue Deficit	24,770	39,954	15,184
IV. Capital Outlay	76,764	79,151	2,387
V. Net Lending	8,536	8,722	186
VI. Gross Fiscal Deficit	110,070	127,828	17,757
RD/GDP	0.7	1.1	0.4
GFD/GDP	3.2	3.7	0.5

Note : The adjustments have been made to shareable taxes and grants from Centre as provided in the Union Budget 2005-06. The other items have been adjusted for slippages in revised estimates over budget estimates based on trend averages of previous 5 years.

outturn of 2005-06 budget estimates of State Governments would indicate deterioration in the key fiscal indicators. The RD-GDP ratio would likely to be placed higher at 1.1 per cent than the budgeted level of 0.7 per cent. Similarly, the GFD-GDP ratio would be placed at 3.7 per cent, which is close to the level in the previous year (4.0 per cent), against the budgeted level of 3.2 per cent.

III. STATE-WISE ANALYSIS OF FISCAL PERFORMANCE

From the foregoing analysis in Section II, it may be concluded that the consolidated position of the State finances has witnessed a significant fiscal correction. However, the fiscal correction has not been uniform across the States. Reflecting this, an attempt has been made for State-wise analysis. The analysis is restricted to 2004-05 (RE) because of a clear evidence of fiscal slippages taking place in budget estimates as explained in the previous Section.

This Section presents the State-wise emerging fiscal situation as evident from the revised estimates for 2004-05 and contrasts it with the position prevailing, on an average, during the triennium 2001-02 through 2003-04 (Accounts). The discussion is based on the analysis

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of 15 fiscal indicators that are classified into four broad groups viz., (a) resource gap, (b) revenue performance, (c) expenditure pattern, and (d) debt position¹⁰. Most of the fiscal indicators are expressed in terms of GSDP at current prices, as provided by the Central Statistical Organisation (CSO) and website of Ministry of Finance, Government of India (for 2004-05). State-wise GSDP data were not available for three States in 2002-03, six

States in 2003-04 and one State in 2004-05 and GSDP for these States have been worked out on the basis of the respective average GSDP growth rates for the previous five-years. State-wise data on these fiscal indicators for 2001-04 and 2004-05 are presented in Tables XVI A and B, respectively.

The analysis of fiscal indicators is undertaken separately for special and non-special category States.

Table-XVI A: Fiscal Indicators 2001-04 (Average)

(Per cent)																
States	GFD/ GSDP	RD/ GSDP	PD/ GSDP	RD/ GFD	RD/ RR	OTR/ GSDP	ONTR/ GSDP	CT/ GSDP	DEV/ GSDP	NON DEV/ GSDP	SSE/ GSDP	CO/ GSDP	DEBT/ GSDP	IP/ RR	PRB/ GSDP	R-G
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
Non Special Category																
1 Andhra Pradesh	4.4	1.8	0.9	40.9	12.5	7.9	2.0	4.6	12.7	6.6	7.2	2.2	34.3	24.4	-1.7	3.1
2 Bihar	8.3	3.8	2.4	45.1	17.4	5.4	0.7	16.2	17.3	13.4	12.2	2.9	73.3	26.4	-2.1	2.6
3 Chhattisgarh	4.1	1.3	1.6	30.5	8.4	7.0	2.8	6.1	13.7	5.8	8.6	2.3	30.3	16.2	-1.3	-6.4
4 Goa	4.7	2.1	1.4	43.7	10.0	7.2	11.2	2.1	15.0	10.2	7.1	2.6	41.2	16.5	-1.2	1.2
5 Gujarat	5.1	3.4	1.6	67.5	27.5	7.0	2.6	2.6	12.1	5.9	6.2	1.7	38.6	28.6	0.0	-5.1
6 Haryana	3.6	1.0	0.7	31.5	8.2	8.3	2.8	1.7	10.6	6.0	4.7	1.2	29.3	21.8	-1.8	0.2
7 Jharkhand	5.0	0.1	2.5	0.2	0.3	6.0	2.8	10.1	16.4	7.4	11.7	4.0	32.0	13.0	-2.4	-4.4
8 Karnataka	4.4	1.9	1.7	39.2	13.4	9.1	1.4	3.9	12.3	6.3	6.5	2.2	29.8	18.6	-0.8	2.2
9 Kerala	5.6	4.3	2.0	76.2	32.9	8.7	0.8	3.4	10.4	8.1	7.1	0.8	41.3	27.8	0.7	1.4
10 Madhya Pradesh	5.5	3.2	2.5	58.9	22.8	6.6	1.8	6.2	13.8	6.4	7.5	2.5	35.0	20.4	0.2	-1.5
11 Maharashtra	4.8	2.9	2.3	62.4	27.2	7.7	1.4	1.5	9.3	6.0	5.6	1.6	30.7	22.8	0.5	-2.5
12 NCT Delhi	2.9	-2.4	1.4	-82.9	-27.0	7.1	1.2	0.7	8.6	3.3	4.4	1.0	16.5	16.6	-3.9	1.1
13 Orissa	7.5	4.3	1.3	55.7	24.6	6.2	1.9	9.7	14.4	10.9	9.1	2.0	64.2	34.9	-1.9	-0.8
14 Punjab	6.5	5.1	1.8	78.2	35.2	7.6	5.3	1.7	9.5	11.8	4.5	0.9	54.9	32.4	0.4	3.9
15 Rajasthan	6.9	4.1	2.2	58.9	27.8	6.9	1.8	5.9	13.2	8.4	9.0	2.5	51.0	31.9	-0.6	0.4
16 Tamil Nadu	3.7	2.0	1.0	52.6	14.8	9.3	1.2	3.1	10.3	6.4	6.5	1.5	27.9	19.4	-0.6	4.5
17 Uttar Pradesh	6.0	4.9	1.7	76.0	33.8	6.2	1.0	7.1	13.0	8.7	6.5	2.1	54.1	29.8	0.6	1.0
18 West Bengal	6.9	5.3	2.4	75.9	58.5	4.4	0.4	4.2	8.4	7.5	5.4	0.6	45.0	50.7	0.7	1.4
Special Category																
1 Arunachal Pradesh	12.0	-4.5	5.7	-40.0	-7.1	1.8	4.3	54.1	52.9	19.5	24.0	16.5	42.9	10.2	-10.6	7.5
2 Assam	3.4	1.7	0.1	48.1	9.4	5.0	1.9	11.6	13.4	8.7	9.1	1.5	32.6	18.3	-1.7	3.5
3 Himachal Pradesh	12.7	8.0	5.2	62.6	34.7	5.7	1.3	16.2	22.5	13.4	12.7	4.7	80.5	32.3	0.5	1.2
4 Jammu & Kashmir	3.9	-6.0	-2.4	3,785.2	-14.1	5.6	1.9	34.5	25.8	20.1	13.8	9.5	58.1	15.1	-12.3	1.1
5 Manipur	8.0	2.8	2.0	32.6	7.8	1.7	1.2	32.5	26.6	16.8	15.5	5.2	53.6	16.9	-3.2	2.3
6 Meghalaya	4.4	-1.0	1.0	-26.4	-3.2	3.4	2.4	22.7	22.1	11.1	13.3	4.3	39.5	11.8	-4.3	0.6
7 Mizoram	16.2	5.1	9.4	23.0	11.5	1.2	2.3	45.2	46.0	19.7	26.8	10.2	79.8	14.0	-1.7	-2.1
8 Nagaland	5.1	-2.9	0.6	119.8	-6.2	1.3	1.1	33.5	23.9	17.1	12.1	7.9	51.0	13.4	-7.5	-4.2
9 Sikkim	3.5	-13.4	-3.7	-846.7	-9.8	7.8	81.2	52.2	52.9	91.9	28.5	16.9	79.7	5.3	-20.5	-2.1
10 Tripura	7.2	-0.4	2.9	-8.7	-1.2	2.8	1.8	24.8	23.3	12.8	14.5	7.5	43.2	14.8	-4.7	-1.1
11 Uttaranchal	6.1	2.9	2.3	43.0	13.0	7.3	2.1	12.8	19.0	8.6	11.7	10.6	45.5	17.4	-0.9	2.0

Minus (-) sign indicates surplus in deficit indicators

Note: 1. Outstanding debt for the composite State of Bihar as on March 2000, was bifurcated in the population ratio of 74.71 per cent and 25.29 per cent for Bihar and Jharkhand. Similarly, for Madhya Pradesh and Chhattisgarh the proportion of 73.3739 per cent and 26.6203 per cent, respectively have been applied and for Uttar Pradesh and Uttaranchal a proportion of 94.9676 per cent and 5.0324 per cent, respectively were applied.

2. Figures in bold pertain to median States for the given indicator.

GSDP - Gross State Domestic Product

RD - Revenue Deficit

CT - Current Transfers

SSE - Social Sector Expenditure

IP - Interest Payments

R-G - Average interest rate on debt minus rate of growth of GSDP

GFD - Gross Fiscal Deficit

OTR - Own Tax Revenue

DEV - Development Expenditure

CO - Capital Outlay

RR - Revenue Receipts

PD - Primary Deficit

ONTR - Own Non-Tax Revenue

NONDEV - Non-Developmental Expenditure

DEBT - Debt

PRB - Primary Revenue Balance

¹⁰ The analysis on the debt position of the States has been provided in Section VI which is a Special Theme on 'Outstanding Liabilities of State Governments'. However, the base data (ratios) for the analysis is provided in this section.

Table-XVI B: Fiscal Indicators 2004-05 (R.E.)

(Per cent)

States	GFD/ GSDP	RD/ GSDP	PD/ GSDP	RD/ GFD	RD/ RR	OTR/ GSDP	ONTR/ GSDP	CT/ GSDP	DEV/ GSDP	NON DEV/ GSDP	SSE/ GSDP	CO/ GSDP	DEBT/ GSDP	IP/ RR	PRB/ GSDP	R-G
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
Non Special Category																
1 Andhra Pradesh	3.4	0.7	-0.3	21.8	4.6	8.7	2.1	5.2	13.3	6.7	7.5	2.9	36.4	22.6	-2.9	0.7
2 Bihar	5.6	0.5	-0.2	9.6	2.0	5.5	0.5	20.7	18.7	13.7	12.8	3.1	77.3	21.8	-5.3	-2.8
3 Chhattisgarh	5.6	1.1	2.6	19.3	5.5	8.0	3.1	8.6	17.7	7.0	11.5	4.2	35.2	14.9	-1.9	11.2
4 Goa	3.9	0.6	1.4	14.0	3.9	6.1	5.8	2.2	12.8	5.4	6.1	3.3	32.3	17.7	-2.0	-33.4
5 Gujarat	6.3	2.4	2.5	38.8	19.1	7.9	1.8	3.1	12.8	6.3	6.8	3.3	46.6	30.1	-1.4	15.1
6 Haryana	1.3	0.3	-1.4	22.0	2.0	9.2	3.1	1.9	9.3	6.2	4.5	0.8	31.0	19.0	-2.4	2.2
7 Jharkhand	8.1	2.5	6.4	30.5	15.2	5.3	2.7	8.2	17.7	6.7	11.4	4.5	36.6	10.6	0.8	-4.1
8 Karnataka	2.7	-0.3	0.3	-12.1	-2.0	10.1	2.4	3.7	11.7	6.8	6.3	2.6	29.2	14.9	-2.8	-8.1
9 Kerala	5.3	4.5	1.6	86.2	31.9	9.3	0.8	4.0	11.1	8.4	8.5	0.6	43.9	25.5	0.9	-3.0
10 Madhya Pradesh	6.3	-1.4	3.0	-21.9	-7.3	7.3	4.1	7.5	17.6	7.3	7.4	5.1	41.1	17.1	-4.6	2.4
11 Maharashtra	5.2	2.6	2.7	49.8	21.5	8.6	1.2	2.2	11.0	6.4	6.0	2.1	35.0	20.7	0.1	1.5
12 NCT Delhi	2.5	-2.1	0.8	-83.0	-24.3	7.0	1.0	0.6	7.8	3.4	4.7	1.6	17.7	19.5	-3.8	-2.0
13 Orissa	5.6	3.8	-0.3	68.7	19.2	6.2	1.8	11.9	12.6	13.0	8.9	1.3	62.5	29.4	-2.0	3.0
14 Punjab	5.2	3.2	1.0	60.4	19.1	7.5	6.7	2.5	11.0	10.8	5.4	2.0	54.4	25.3	-1.0	-9.6
15 Rajasthan	6.5	2.4	1.7	37.6	15.1	7.7	1.9	6.5	14.6	8.1	9.3	3.6	56.8	29.6	-2.3	5.4
16 Tamil Nadu	2.9	0.9	0.2	30.9	6.2	9.8	1.1	3.4	10.0	6.7	6.5	1.9	28.4	18.4	-1.7	-1.9
17 Uttar Pradesh	5.6	2.9	1.1	52.4	18.7	6.4	0.9	8.4	11.7	9.2	7.4	2.6	54.7	28.3	-1.5	-3.4
18 West Bengal	5.4	4.0	0.9	75.4	44.0	4.4	0.7	4.1	7.5	7.3	4.8	0.9	46.0	48.3	-0.4	-5.7
Special Category																
1 Arunachal Pradesh	22.9	6.5	17.5	28.6	13.5	1.6	7.1	39.8	52.5	18.9	24.3	16.1	50.2	11.1	1.2	-8.0
2 Assam	10.6	3.6	6.2	34.0	11.1	6.3	7.9	18.2	37.7	11.2	14.5	10.2	38.4	13.5	-0.8	6.0
3 Himachal Pradesh	6.9	4.2	0.2	60.8	21.8	4.9	2.0	12.5	14.9	11.6	9.4	2.7	73.7	34.7	-2.5	-22.1
4 Jammu and Kashmir	3.7	-5.8	-0.6	-156.4	-16.1	5.1	2.5	28.2	25.4	14.2	11.4	9.3	45.1	12.0	-10.1	-26.5
5 Manipur	9.6	-0.6	5.9	-5.8	-2.1	1.3	1.3	24.0	25.1	11.0	15.1	9.6	50.4	14.0	-4.3	-48.2
6 Meghalaya	4.0	-2.0	0.3	-49.2	-6.1	3.9	2.7	26.1	25.8	11.2	15.4	5.4	42.2	11.3	-5.7	0.7
7 Mizoram	14.4	0.2	7.9	1.1	0.3	1.2	2.3	47.8	47.0	19.3	22.7	13.6	82.6	12.6	-6.3	-6.1
8 Nagaland	5.3	-2.9	1.0	-53.4	-9.7	1.2	1.0	27.0	19.9	14.8	10.3	8.3	41.6	14.9	-7.2	-11.5
9 Sikkim	12.2	-13.7	7.1	-112.5	-13.0	5.0	51.3	49.4	57.6	60.3	27.9	25.9	62.8	4.8	-18.8	-33.9
10 Tripura	4.0	-1.9	1.0	-48.1	-9.3	2.2	1.3	17.3	15.0	9.4	9.6	6.0	33.8	14.5	-4.9	-44.1
11 Uttaranchal	13.8	5.5	9.7	39.9	21.3	6.7	2.1	16.9	25.7	12.8	14.6	7.3	55.3	16.0	1.4	-13.8

Minus (-) sign indicates surplus in deficit indicators

Note : 1. Outstanding debt for the composite State of Bihar as on March 2000, was bifurcated in the population ratio of 74.71 per cent and 25.29 per cent for Bihar and Jharkhand. Similarly, for Madhya Pradesh and Chhattisgarh the proportion of 73.3739 per cent and 26.6203 per cent, respectively have been applied and for Uttar Pradesh and Uttaranchal a proportion of 94.9676 per cent and 5.0324 per cent, respectively were applied.

2. Figures in bold pertain to median States for the given indicator.

In the case of each category of States, comparisons are made over time and across space. At each of the above-specified time periods, the State Governments are placed (separately for special and non-special categories) in ascending order for each fiscal indicator. In order to facilitate a qualitative assessment of the data presented in Tables XVI A & XVI B, the State Governments have been ranked into four quartiles for each fiscal indicator for the years 2001-04 and 2004-05. Given that there are 18 non-special category States and 11 special category States, the size of the second and third quartiles for each category of States has been

adjusted for expositional convenience. The indicator relating to the difference between the average interest rate on debt and the growth rate of GSDP, has not been classified into quartiles.

The summary position is presented in Tables XVII A & B (non special category States) and Tables XVIII A & B (special category States), respectively. These Tables, at a glance, indicate the relative ranking of different States for the broad range of fiscal indicators. The summary position of debt indicators is provided in Table XXV in Section VI. The discussion of trends is set out below.

Table XVII A : Summary Position of Non-Special Category States for 2001-04 (Average)

INDICATOR	Quartile 1 (Q1)	Quartile 2 (Q2)	Quartile 3 (Q3)	Quartile 4 (Q4)
(A) RESOURCE GAP				
1. GFD/GSDP	RANGE: 2.9 to 4.1 Delhi, Haryana, Tamil Nadu, Chhattisgarh	RANGE: 4.4 to 5.0 Karnataka, Maharashtra, Goa, Andhra Pradesh, Jharkhand	RANGE: 5.1 to 6.5 Madhya Pradesh, Kerala, Gujarat , Uttar Pradesh, Punjab	RANGE: 6.9 to 8.3 West Bengal, Rajasthan, Orissa, Bihar
2. RD/GSDP	RANGE: -2.4 to 1.3 Delhi, Jharkhand, Haryana, Chhattisgarh	RANGE: 1.8 to 2.9 Andhra Pradesh, Karnataka, Tamil Nadu, Goa, Maharashtra	RANGE: 3.2 to 4.3 Madhya Pradesh , Gujarat, Bihar, Rajasthan, Kerala	RANGE: 4.3 to 5.3 Orissa, Uttar Pradesh, Punjab, West Bengal
3. PD/GSDP	RANGE: 0.7 to 1.3 Haryana, Andhra Pradesh, Tamil Nadu, Orissa	RANGE: 1.4 to 1.7 Delhi, Goa, Gujarat, Uttar Pradesh, Chhattisgarh	RANGE: 1.7 to 2.3 Karnataka , Kerala, Rajasthan, Punjab, Maharashtra	RANGE: 2.4 to 2.5 West Bengal, Madhya Pradesh, Jharkhand, Bihar
4. PRB/GSDP	RANGE: -3.9 to -1.9 Delhi, Jharkhand, Orissa, Bihar	RANGE: -1.8 to -0.8 Haryana, Andhra Pradesh, Chhattisgarh, Goa, Karnataka	RANGE: -0.6 to 0.4 Tamil Nadu , Rajasthan, Gujarat, Madhya Pradesh, Punjab	RANGE: 0.5 to 0.7 Maharashtra, Uttar Pradesh, Kerala, West Bengal
5. RD/GFD	RANGE: -82.9 to 31.5 Delhi, Jharkhand, Chhattisgarh, Haryana	RANGE: 39.2 to 52.6 Karnataka, Andhra Pradesh, Goa, Bihar, Tamil Nadu	RANGE: 55.7 to 67.5 Orissa , Madhya Pradesh, Rajasthan, Maharashtra, Gujarat	RANGE: 75.9 to 78.2 West Bengal, Uttar Pradesh, Kerala, Punjab
6. RD/RR	RANGE: -27.0 to 8.4 Delhi, Jharkhand, Haryana, Chhattisgarh	RANGE: 10.0 to 17.4 Goa, Andhra Pradesh, Karnataka, Tamil Nadu, Bihar	RANGE: 22.8 to 27.8 Madhya Pradesh , Orissa, Maharashtra, Gujarat, Rajasthan	RANGE: 32.9 to 58.5 Kerala, Uttar Pradesh, Punjab, West Bengal
(B) REVENUE PERFORMANCE				
7. OTR/GSDP	RANGE: 4.4 to 6.2 West Bengal, Bihar, Jharkhand, Orissa	RANGE: 6.2 to 7.0 Madhya Pradesh, Rajasthan, Gujarat, Uttar Pradesh, Chhattisgarh	RANGE: 7.1 to 7.9 Goa, Punjab, Delhi , Maharashtra, Andhra Pradesh	RANGE: 8.3 to 9.3 Haryana, Kerala, Tamil Nadu, Karnataka
8. ONTR/GSDP	RANGE: 0.4 to 1.0 West Bengal, Bihar, Kerala, Uttar Pradesh	RANGE: 1.2 to 1.8 Tamil Nadu, Delhi, Maharashtra, Karnataka, Madhya Pradesh	RANGE: 1.8 to 2.8 Rajasthan , Orissa, Andhra Pradesh, Gujarat, Jharkhand	RANGE: 2.8 to 11.2 Chhattisgarh, Haryana, Punjab, Goa
9. CT/GSDP	RANGE: 0.7 to 1.7 Delhi, Maharashtra, Punjab, Haryana	RANGE: 2.1 to 3.9 Goa, Gujarat, Tamil Nadu, Kerala, Karnataka	RANGE: 4.2 to 6.2 West Bengal , Andhra Pradesh, Rajasthan, Madhya Pradesh, Chhattisgarh	RANGE: 7.1 to 16.2 Uttar Pradesh, Orissa, Jharkhand, Bihar
(C) EXPENDITURE PATTERN				
10. DEV/GSDP	RANGE: 8.4 to 9.5 West Bengal, Delhi, Maharashtra, Punjab	RANGE: 10.3 to 12.3 Tamil Nadu, Kerala, Haryana, Gujarat, Karnataka	RANGE: 12.7 to 13.8 Uttar Pradesh, Rajasthan, Madhya Pradesh, Andhra Pradesh , Chhattisgarh	RANGE: 14.4 to 17.3 Goa, Bihar, Jharkhand, Orissa
11. NONDEV/GSDP	RANGE: 3.3 to 6.0 Delhi, Gujarat, Haryana, Chhattisgarh	RANGE: 6.0 to 6.6 Madhya Pradesh, Tamil Nadu, Karnataka, Andhra Pradesh, Maharashtra	RANGE: 7.4 to 8.7 West Bengal, Kerala, Jharkhand , Uttar Pradesh, Rajasthan	RANGE: 10.2 to 13.4 Goa, Orissa, Punjab, Bihar
12. SSE/GSDP	RANGE: 4.5 to 5.4 Delhi, Punjab, Haryana, West Bengal	RANGE: 5.6 to 6.5 Maharashtra, Gujarat, Uttar Pradesh, Tamil Nadu, Karnataka	RANGE: 7.1 to 8.6 Kerala, Andhra Pradesh, Goa , Madhya Pradesh, Chhattisgarh	RANGE: 9.0 to 12.2 Orissa, Bihar, Jharkhand, Rajasthan
13. CO/GSDP	RANGE: 0.6 to 1.0 West Bengal, Kerala, Punjab, Delhi	RANGE: 1.2 to 2.0 Haryana, Tamil Nadu, Maharashtra, Gujarat, Orissa	RANGE: 2.1 to 2.5 Uttar Pradesh , Andhra Pradesh, Karnataka, Madhya Pradesh, Chhattisgarh	RANGE: 2.5 to 4.0 Rajasthan, Goa, Bihar, Jharkhand

Notes : 1. The quartile position indicated in this Table is based on the data of fiscal indicators provided in Table XVI A. The grouping of States into four quartiles viz., Q1, Q2, Q3 and Q4 provides the relative position of each State vis-à-vis others for each fiscal indicator. The quartiles have been computed by grouping the States into Special and Non-Special Categories and then arranging the indicators in each category in an ascending order. The type of indicator qualifies the relative position of the quartile. To illustrate, for Debt-GSDP ratio, States in Q1 are the better performed States for that indicator, while for development expenditure to GSDP (DEV/GSDP) ratio, States in Q4 portrays a similar position.

2. Minus (-) indicates surplus in deficit indicators.

3. Figures in bold pertain to median States for the given indicator.

Table XVII B : Summary Position of Non-Special Category States for 2004-05 (R.E.)

INDICATOR	Quartile 1 (Q1)	Quartile 2 (Q2)	Quartile 3 (Q3)	Quartile 4 (Q4)
(A) RESOURCE GAP				
1. GFD/GSDP	RANGE: 1.3 to 2.9 Haryana, Delhi, Karnataka, Tamil Nadu	RANGE: 3.4 to 5.3 Andhra Pradesh, Goa, Kerala, Maharashtra, Punjab	RANGE: 5.4 to 5.6 West Bengal , Chhattisgarh, Uttar Pradesh, Orissa, Bihar	RANGE: 6.3 to 8.1 Gujarat, Rajasthan, Madhya Pradesh, Jharkhand
2. RD/GSDP	RANGE: -2.1 to 0.3 Delhi, Madhya Pradesh, Karnataka, Haryana	RANGE: 0.5 to 1.1 Goa, Andhra Pradesh, Tamil Nadu, Chhattisgarh, Bihar	RANGE: 2.4 to 2.9 Rajasthan , Gujarat, Maharashtra, Jharkhand, Uttar Pradesh	RANGE: 3.2 to 4.5 Punjab, Orissa, West Bengal, Kerala
3. PD/GSDP	RANGE: -1.4 to -0.2 Haryana, Orissa, Andhra Pradesh, Bihar	RANGE: 0.2 to 1.0 Karnataka, Delhi, Tamil Nadu, West Bengal, Punjab	RANGE: 1.1 to 2.5 Uttar Pradesh , Goa, Kerala, Rajasthan, Gujarat	RANGE: 2.6 to 6.4 Chhattisgarh, Maharashtra, Madhya Pradesh, Jharkhand
4. PRB/GSDP	RANGE: -5.3 to -2.9 Madhya Pradesh, Bihar, Delhi, Andhra Pradesh	RANGE: -2.8 to -2.0 Haryana, Rajasthan, Orissa, Goa, Karnataka	RANGE: -1.9 to -1.0 Chhattisgarh , Tamil Nadu, Uttar Pradesh, Gujarat, Punjab	RANGE: -0.4 to 0.9 West Bengal, Maharashtra, Jharkhand, Kerala
5. RD/GFD	RANGE: -83.0 to 9.6 Delhi, Madhya Pradesh, Karnataka, Bihar	RANGE: 14.0 to 30.5 Chhattisgarh, Goa, Andhra Pradesh, Haryana, Jharkhand	RANGE: 30.9 to 52.4 Tamil Nadu , Rajasthan, Gujarat, Maharashtra, Uttar Pradesh	RANGE: 60.4 to 86.2 Punjab, Orissa, West Bengal, Kerala
6. RD/RR	RANGE: -24.3 to 2.0 Delhi, Madhya Pradesh, Karnataka, Haryana	RANGE: 2.0 to 6.2 Goa, Andhra Pradesh, Bihar, Chhattisgarh, Tamil Nadu	RANGE: 15.1 to 19.1 Rajasthan , Jharkhand, Uttar Pradesh, Punjab, Gujarat	RANGE: 19.2 to 44.0 Orissa, Maharashtra, Kerala, West Bengal
(B) REVENUE PERFORMANCE				
7. OTR/GSDP	RANGE: 4.4 to 6.1 West Bengal, Bihar, Jharkhand, Goa	RANGE: 6.2 to 7.5 Uttar Pradesh, Orissa, Delhi, Punjab, Madhya Pradesh	RANGE: 7.7 to 8.7 Andhra Pradesh, Gujarat, Chhattisgarh, Maharashtra, Rajasthan	RANGE: 9.2 to 10.1 Kerala, Haryana, Karnataka, Tamil Nadu
8. ONTR/GSDP	RANGE: 0.5 to 0.9 Bihar, West Bengal, Kerala, Uttar Pradesh	RANGE: 1.0 to 1.8 Delhi, Tamil Nadu, Maharashtra, Gujarat, Orissa	RANGE: 1.9 to 3.1 Rajasthan , Andhra Pradesh, Karnataka, Jharkhand, Haryana	RANGE: 3.1 to 6.7 Chhattisgarh, Madhya Pradesh, Goa, Punjab
9. CT/GSDP	RANGE: 0.6 to 2.2 Delhi, Haryana, Goa, Maharashtra	RANGE: 2.5 to 4.0 Punjab, Gujarat, Tamil Nadu, Karnataka, Kerala	RANGE: 4.1 to 8.2 West Bengal , Andhra Pradesh, Rajasthan, Madhya Pradesh, Jharkhand	RANGE: 8.4 to 20.7 Chhattisgarh, Orissa, Bihar, Uttar Pradesh
(C) EXPENDITURE PATTERN				
10. DEV/GSDP	RANGE: 7.5 to 10.0 West Bengal, Delhi, Haryana, Tamil Nadu	RANGE: 11.0 to 11.7 Kerala, Maharashtra, Punjab, Uttar Pradesh, Karnataka	RANGE: 12.6 to 14.6 Andhra Pradesh, Gujarat, Goa, Orissa , Rajasthan,	RANGE: 17.6 to 18.7 Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh
11. NONDEV/GSDP	RANGE: 3.4 to 6.3 Delhi, Goa, Haryana, Gujarat	RANGE: 6.4 to 6.8 Maharashtra, Karnataka, Tamil Nadu, Chhattisgarh, Andhra Pradesh, Jharkhand	RANGE: 7.0 to 8.4 West Bengal, Madhya Pradesh, Rajasthan, Kerala, Chhattisgarh	RANGE: 9.2 to 13.7 Uttar Pradesh, Punjab, Bihar, Orissa
12. SSE/GSDP	RANGE: 4.5 to 5.4 Haryana, Delhi, West Bengal, Punjab	RANGE: 6.0 to 6.8 Maharashtra, Goa, Karnataka, Tamil Nadu, Gujarat	RANGE: 7.4 to 8.9 Uttar Pradesh , Madhya Pradesh, Kerala, Andhra Pradesh, Orissa	RANGE: 9.3 to 12.8 Bihar, Chhattisgarh, Jharkhand, Rajasthan
13. CO/GSDP	RANGE: 0.6 to 1.3 Kerala, Haryana, West Bengal, Orissa	RANGE: 1.6 to 2.6 Delhi, Tamil Nadu, Punjab, Maharashtra, Uttar Pradesh	RANGE: 2.6 to 3.3 Karnataka , Andhra Pradesh, Bihar, Gujarat, Goa	RANGE: 3.6 to 5.1 Rajasthan, Chhattisgarh, Jharkhand, Madhya Pradesh

Notes : 1. The quartile position indicated in this Table is based on the data of fiscal indicators provided in Table XVI B. The grouping of States into four quartiles viz., Q1, Q2, Q3 and Q4 provides the relative position of each State vis-à-vis others for each fiscal indicator. The quartiles have been computed by grouping the States into Special and Non-Special Categories and then arranging the indicators in each category in an ascending order. The type of indicator qualifies the relative position of the quartile. To illustrate, for Debt-GSDP ratio, States in Q1 are the better performed States for that indicator, while for development expenditure to GSDP (DEV/GSDP) ratio, States in Q4 portrays a similar position.

2. Minus (-) indicates surplus in deficit indicators.

3. Figures in bold pertain to median States for the given indicator.

III.A. Non-Special Category States

The summary position of the non-special category States into their quartile position is provided in Tables XVII A & B for 2001-04 (average) and 2004-05 (RE), respectively.

III.A.(i) Indicators of Resource Gap

Improvement in fiscal performance, in terms of deficit indicators, was clearly discernible across the States in 2004-05 as compared to the period 2001-04. The ratio of GFD to GSDP was below 3 per cent for four out of eighteen States in 2004-05 (Haryana, Delhi, Karnataka and Tamil Nadu) as against just one State namely, Delhi in 2001-04. Similar improvement was also reflected in RD-GSDP and PD-GSDP ratios (Charts 13 A-C) (also see Statements 1-11).

The ratio of RD to GFD, which indicates the extent of pre-emption of borrowings for current expenditure, also showed a decline in the case of all but three State Governments in 2004-05, except Orissa and Kerala. In 2004-05, less than one-third of the overall borrowings was pre-empted by current expenditure in ten out of eighteen States while the extent of pre-emption was above three-fourth in two States namely, Kerala and West Bengal.

It may be mentioned that TFC recommended the States to achieve the target of GFD-GSDP ratio

of 3.0 per cent by 2009-10 and revenue balance by 2008-09. There are five States in this category viz., Haryana, Delhi, Karnataka and Tamil Nadu which have already achieved the final target for GFD-GSDP ratio of 3.0 per cent during 2004-05, while Delhi, Madhya Pradesh and Karnataka have already achieved revenue balance in 2004-05.

In general, during 2004-05, resource gaps (as percentage of GSDP) were the highest in the case of Jharkhand, Madhya Pradesh, Gujarat and Rajasthan with the GFD-GSDP ranging between 6.3 per cent and 8.1 per cent.

III.A.(ii) Revenue Performance

Most of the State Governments showed signs of improvement in their own tax revenue performance (as percentage of GSDP) during 2004-05 over 2001-04. States like Chhattisgarh, Karnataka and Gujarat witnessed maximum improvement between the comparable periods. Karnataka, Tamil Nadu, Haryana and Kerala accounted for the highest own-tax-GSDP ratios (more than 9.0 per cent) during both 2001-04 and 2004-05, while West Bengal, Jharkhand and Bihar occupied the lowest rungs (less than 6.2 per cent) (Chart 14 A) (also see Statements 18-23).

In contrast to the trends in own tax revenues, half of the State Governments showed deterioration in own non-tax-GSDP ratio during 2004-05 over

Chart 13 : Quartile Position of Non-Special Category States - Resource Gap (Contd.)

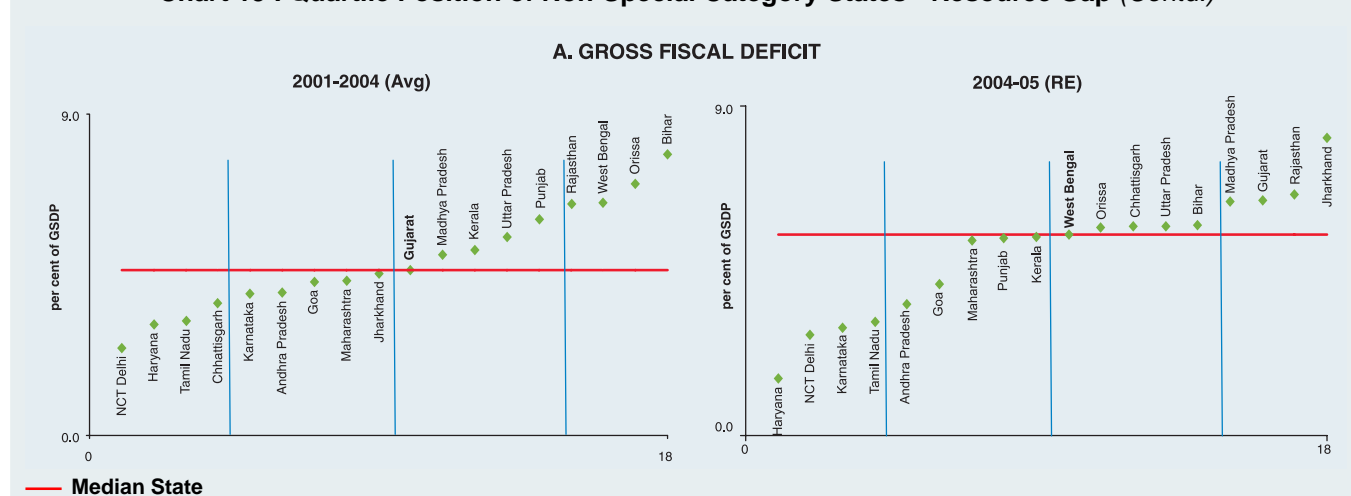
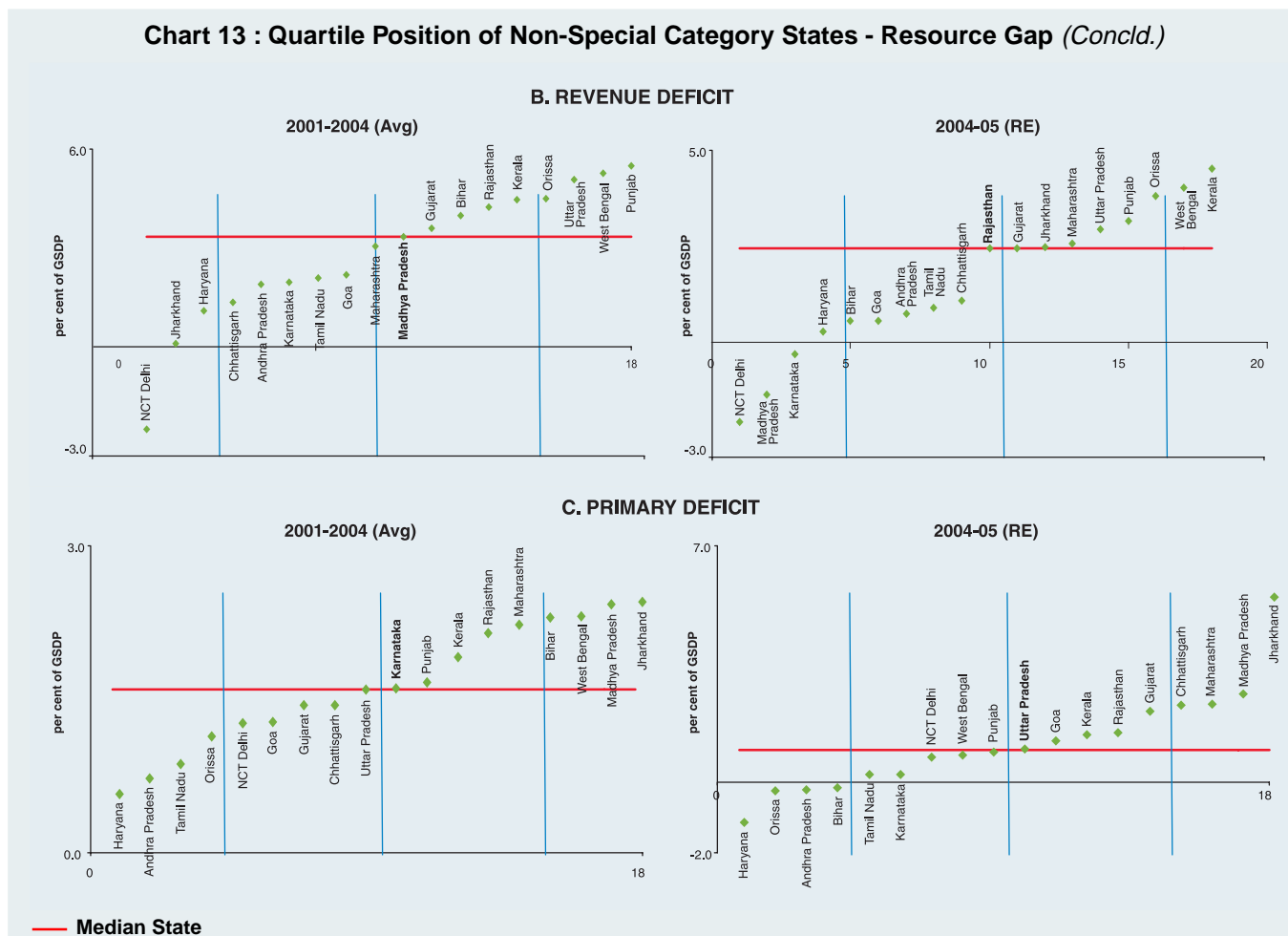


Chart 13 : Quartile Position of Non-Special Category States - Resource Gap (Concl'd.)

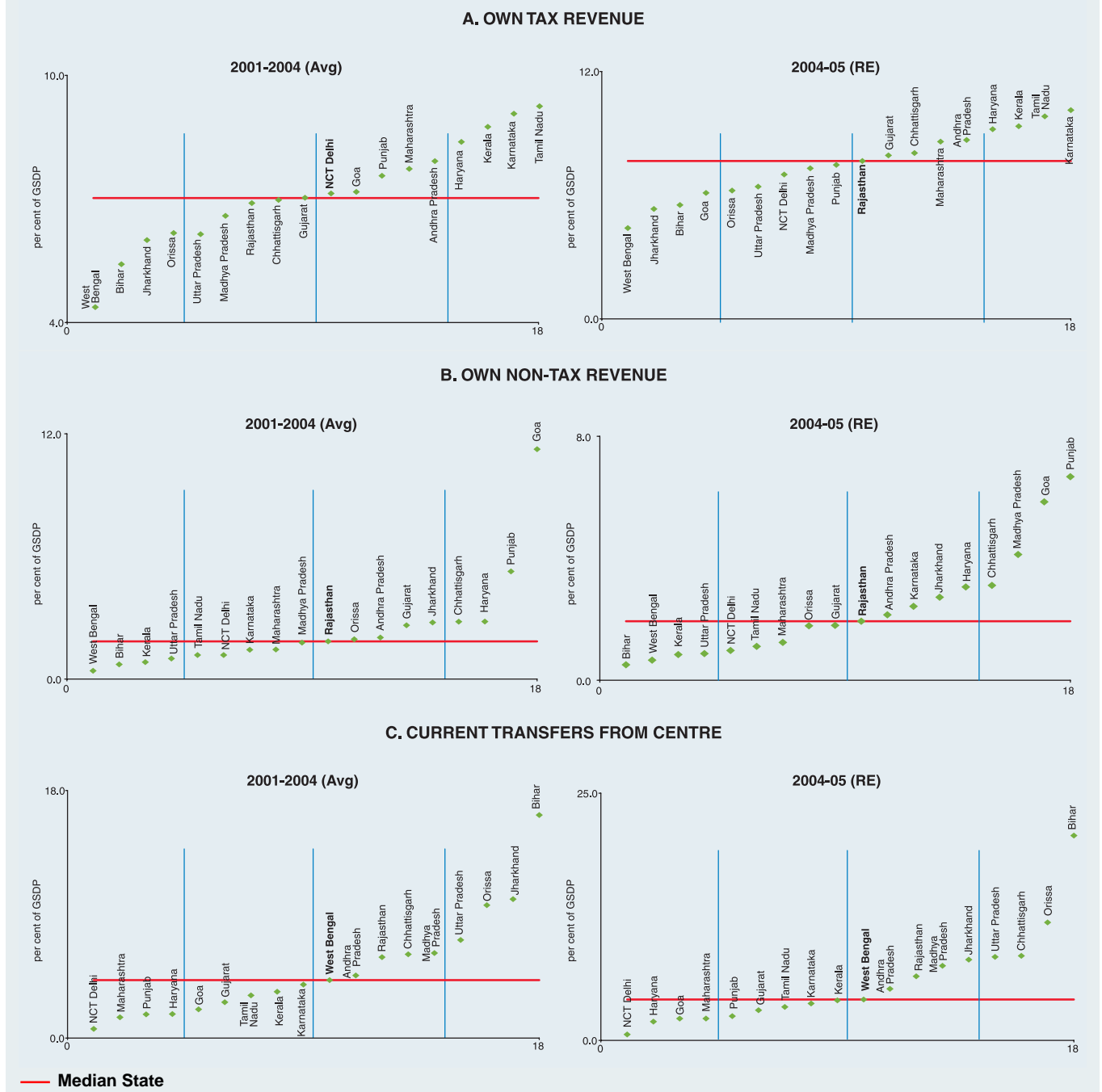
2001-04. However, Madhya Pradesh, Punjab, Karnataka, Jharkhand, West Bengal and Haryana showed signs of improvement with increase in the ratio for the first three States being more than one percentage point. While Punjab, Chattisgarh and Goa continued to occupy the highest ranks in terms of own non-tax-GSDP ratio, States like Bihar, West Bengal, Kerala and Uttar Pradesh occupied the lowest ranks (Chart 14 B).

Current transfers (sum of share in central tax revenues and grants) were highest for Bihar, Uttar Pradesh and Orissa as a ratio to GSDP during both the periods 2001-04 and 2004-05 (more than 8.4 per cent), while Delhi, Haryana and Maharashtra had the lowest current transfers-GSDP ratio (less than 2.2 per cent) (Chart 14 C).

III.A.(iii) Pattern of Expenditure

There was no uniformity in trend of developmental expenditure and non-developmental expenditure (as percentage of GSDP) across the States in 2004-05 over 2001-04 (Charts 15 A & B). The States of Chhattisgarh, Madhya Pradesh, Maharashtra and Punjab witnessed a marked hike (more than 1.5 per cent) in developmental expenditure while the reduction was prominent (more than 1.3 per cent) in Goa, Orissa, Haryana and Uttar Pradesh. The States of Jharkhand and Bihar had the highest ranking in terms of developmental expenditure-GSDP ratio (over 17 per cent) in both the periods, whereas West Bengal and Delhi had the lowest ranking (less than 8 per cent). The ratio of non-developmental expenditure to GSDP was highest in Orissa, Bihar and Punjab (above 10 per cent) and the ratio was lowest for

Chart 14 : Quartile Position of Non-Special Category States - Revenue Performance



Gujarat, Haryana and Delhi (3.4 per cent) (also see Statements 12-17).

A mixed trend is also evident in respect of social sector expenditure (comprising social services, rural development, food storage and warehousing) as a ratio to GSDP, with ten States

showing an increase and eight States indicating a decline during 2004-05 over that of 2001-04. Amongst all the States, Jharkhand, Chhattisgarh, Bihar and Rajasthan continued to provide for the highest level of social sector expenditure during 2004-05 (more than 9.3 per cent). In contrast,

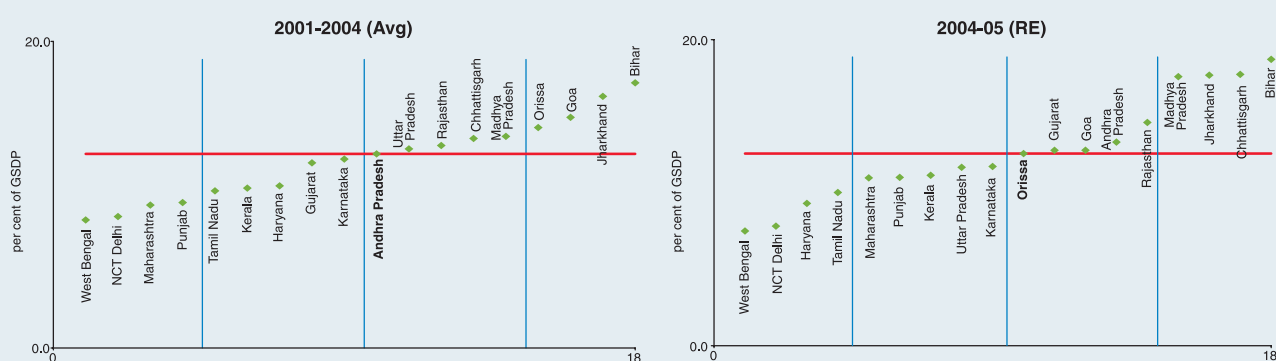
Haryana, Delhi, West Bengal and Punjab formed part of the lowest quartile during both the periods (less than 5.4 per cent).

Most of the States showed an increase in the ratio of capital outlay to GSDP during 2004-05 over 2001-04. Increase in the ratio was above one percentage point in the States of Madhya Pradesh,

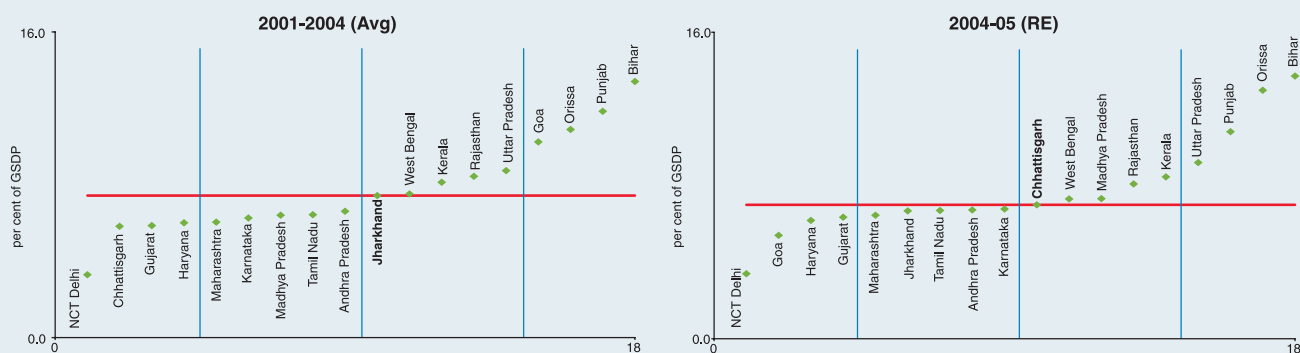
Chhattisgarh, Gujarat, Rajasthan and Punjab, while it declined to the extent of 0.7 percentage points in Orissa. In terms of the ratio of capital outlay to GSDP, Jharkhand and Rajasthan continued to occupy the top quartile, while Kerala and West Bengal continued to form part of the lowest quartile during 2004-05 (Chart 15 C).

Chart 15 : Quartile Position of Non-Special Category States - Expenditure Pattern

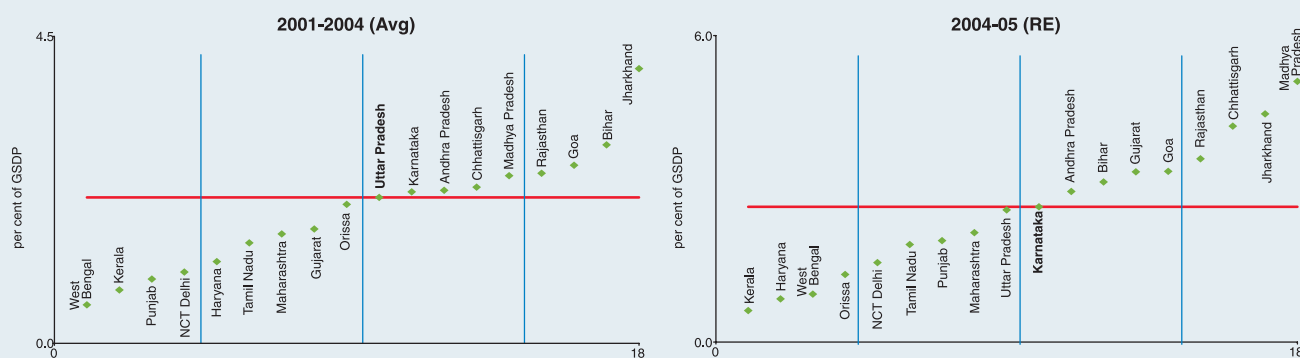
A. DEVELOPMENTAL EXPENDITURE



B. NON DEVELOPMENTAL EXPENDITURE



C. CAPITAL OUTLAY



— Median State

The proportions of expenditure (revenue and capital outlay) on broad heads of education (Statement 41) and health (Statement 42) to aggregate disbursements have largely increased between 2003-04 and 2004-05. However, across the States there was considerable variation. In 2004-05, expenditure on broad head of education constituted less than 5 per cent of aggregate disbursements in Punjab, Madhya Pradesh, Gujarat, Tamil Nadu, Chhattisgarh and West Bengal, while the ratio was above 10 per cent in Bihar, Delhi and Jharkhand. Expenditure under the board head of health services as a percentage of total disbursements varied within a narrow range of 1.0 per cent in Gujarat to 2.9 per cent in Jharkhand (barring 6.7 per cent in Delhi). There is an imperative need to enhance the share of expenditure on education and health for wider coverage of education and medical services across the States which would improve the quality of life and in turn, human development index of the country.

III.B. Special Category States¹¹

The summary position of the special category States into their quartile position is provided in Tables XVIII A & B for 2001-04 (average) and 2004-05 (RE), respectively.

III.B.(i) Indicators of Resource Gap

The performance of special category States in terms of deficit indicators did not exhibit any uniform pattern. The deficit indicators significantly deteriorated, in 2004-05 over 2001-04, in Arunachal Pradesh, Sikkim, Uttaranchal and Assam, while there were signs of improvement in Himachal Pradesh, Tripura, Mizoram, Meghalaya, and Jammu and Kashmir. In terms of GFD-GSDP ratio, Meghalaya, Tripura and Jammu and Kashmir constituted the first quartile in 2004-05 (less than 4 per cent), while Mizoram and Arunachal Pradesh

continued to be placed in the fourth quartile. It is interesting to note that six out of the eleven States in special category recorded a revenue surplus during 2004-05 and two States namely, Arunachal Pradesh and Uttaranchal had more than 5 per cent RD-GSDP ratio (Charts 16 A-C).

III.B.(ii) Revenue Performance

The own tax-GSDP ratio showed sign of improvement in Assam and Meghalaya in 2004-05 (RE) over 2001-04. The ratio continued to be low in the case of Mizoram, Nagaland, Manipur and Arunachal Pradesh constituting less than 2 per cent, and was high in the case of Uttaranchal, Assam and Jammu and Kashmir (above 5 per cent) in 2004-05. On the other hand, Assam and Arunachal Pradesh witnessed significant improvement in the own non-tax to GSDP ratio in 2004-05 over 2001-04. The ratio was exceptionally high in the case of Sikkim in both the periods, essentially reflecting the impact of State lotteries. Central transfers in the form of share in Central taxes and grants continued to be a dominant source of revenue for all the special category States. The ratio of central transfers constituted as high as around 50 per cent of GSDP in Mizoram and Sikkim (Charts 17 A-C).

III.B.(iii) Pattern of Expenditure

Share of developmental expenditure in GSDP in special category States was significantly higher as compared to non-special category States. There were eight States in special category for which developmental expenditure constituted more than one-fourth of GSDP in 2004-05. In States like Sikkim and Arunachal Pradesh the ratio of developmental expenditure to GSDP was above 50 per cent (Charts 18 A-C). In this category of States, expenditure on the broad head of education as a ratio of aggregate disbursements was higher in 2004-05 (RE) over 2003-04 for all the States except,

¹¹ A distinction is drawn between Special and Non-special Category States in the context of Plan allocations. The Special Category States are Arunachal Pradesh, Assam, Himachal Pradesh, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura and Uttaranchal.

Table XVIII A : Summary Position of Special Category States 2001-04 (Average)

INDICATOR	Quartile 1 (Q1)	Quartile 2 (Q2)	Quartile 3 (Q3)	Quartile 4 (Q4)
(A) RESOURCE GAP				
1. GFD/GSDP	RANGE: 3.4 to 3.9 Assam, Sikkim, Jammu and Kashmir	RANGE: 4.4 to 5.1 Meghalaya, Nagaland	RANGE: 6.1 to 8.0 Uttaranchal , Tripura, Manipur	RANGE: 12.0 to 16.2 Arunachal Pradesh, Himachal Pradesh, Mizoram
2. RD/GSDP	RANGE: -13.4 to -4.5 Sikkim, Jammu and Kashmir, Arunachal Pradesh	RANGE: -2.9 to -1.0 Nagaland, Meghalaya	RANGE: -0.4 to 2.8 Tripura , Assam, Manipur	RANGE: 2.9 to 8.0 Uttaranchal, Mizoram, Himachal Pradesh
3. PD/GSDP	RANGE: -3.7 to 0.1 Sikkim, Jammu and Kashmir, Assam	RANGE: 0.6 to 1.0 Nagaland, Meghalaya	RANGE: 2.0 to 2.9 Manipur , Uttaranchal, Tripura	RANGE: 5.2 to 9.4 Himachal Pradesh, Arunachal Pradesh, Mizoram
4. PRB/GSDP	RANGE: -20.5 to -10.6 Sikkim, Jammu and Kashmir, Arunachal Pradesh	RANGE: -7.5 to -4.7 Nagaland, Tripura	RANGE: -4.3 to -1.7 Meghalaya , Manipur, Mizoram	RANGE: -1.7 to 0.5 Assam, Uttaranchal, Himachal Pradesh
5. RD/GFD	RANGE: -846.7 to -26.4 Sikkim, Arunachal Pradesh, Meghalaya	RANGE: -8.7 to 23.0 Tripura, Mizoram	RANGE: 32.6 to 48.1 Manipur , Uttaranchal, Assam	RANGE: 62.6 to 3785.2 Himachal Pradesh, Nagaland, Jammu and Kashmir
6. RD/RR	RANGE: -14.1 to -7.1 Jammu and Kashmir, Sikkim, Arunachal Pradesh	RANGE: -6.2 to -3.2 Nagaland, Meghalaya	RANGE: -1.2 to 9.4 Tripura , Manipur, Assam	RANGE: 11.5 to 34.7 Mizoram, Uttaranchal, Himachal Pradesh
(B) REVENUE PERFORMANCE				
7. OTR/GSDP	RANGE: 1.2 to 1.7 Mizoram, Nagaland, Manipur	RANGE: 1.8 to 2.8 Arunachal Pradesh, Tripura	RANGE: 3.4 to 5.6 Meghalaya , Assam, Jammu and Kashmir	RANGE: 5.7 to 7.8 Himachal Pradesh, Uttaranchal, Sikkim
8. ONTR/GSDP	RANGE: 1.1 to 1.3 Nagaland, Manipur, Himachal Pradesh	RANGE: 1.8 to 1.9 Tripura, Jammu and Kashmir	RANGE: 1.9 to 2.3 Assam , Uttaranchal, Mizoram	RANGE: 2.4 to 81.2 Meghalaya, Arunachal Pradesh, Sikkim
9. CT/GSDP	RANGE: 11.6 to 16.2 Assam, Uttaranchal, Himachal Pradesh	RANGE: 22.7 to 24.8 Meghalaya, Tripura	RANGE: 32.5 to 34.5 Manipur , Nagaland, Jammu and Kashmir	RANGE: 45.2 to 54.1 Mizoram, Sikkim, Arunachal Pradesh
(C) EXPENDITURE PATTERN				
10. DEV/GSDP	RANGE: 13.4 to 22.1 Assam, Uttaranchal, Meghalaya	RANGE: 22.5 to 23.3 Himachal Pradesh, Tripura	RANGE: 23.9 to 26.6 Nagaland , Jammu and Kashmir, Manipur	RANGE: 46.0 to 52.9 Mizoram, Sikkim, Arunachal Pradesh
11. NONDEV/GSDP	RANGE: 8.6 to 11.1 Uttaranchal, Assam, Meghalaya	RANGE: 12.8 to 13.4 Tripura, Himachal Pradesh	RANGE: 16.8 to 19.5 Manipur , Nagaland, Arunachal Pradesh	RANGE: 19.7 to 91.9 Jammu and Kashmir, Sikkim, Mizoram
12. SSE/GSDP	RANGE: 9.1 to 12.1 Assam, Uttaranchal, Nagaland	RANGE: 12.7 to 13.3 Himachal Pradesh, Meghalaya	RANGE: 13.8 to 15.5 Jammu and Kashmir , Tripura, Manipur	RANGE: 24.0 to 28.5 Arunachal Pradesh, Mizoram, Sikkim
13. CO/GSDP	RANGE: 1.5 to 4.7 Assam, Meghalaya, Himachal Pradesh	RANGE: 5.2 to 7.5 Manipur, Tripura	RANGE: 7.9 to 10.2 Nagaland , Jammu and Kashmir, Mizoram	RANGE: 10.6 to 16.9 Uttaranchal, Sikkim, Arunachal Pradesh

Note : 1. The quartile position indicated in this Table is based on the data of fiscal indicators provided in Table XVI A. The grouping of States into four quartiles viz., Q1, Q2, Q3 and Q4 provides the relative position of each State vis-à-vis others for each fiscal indicator. The quartiles have been computed by grouping the States into Special and Non-Special Categories and then arranging the indicators in each category in an ascending order. The type of indicator qualifies the relative position of the quartile. To illustrate, for Debt-GSDP ratio, States in Q1 are the better performed States for that indicator, while for development expenditure to GSDP (DEV/GSDP) ratio, States in Q4 portrays a similar position.

2. Minus (-) indicates surplus in deficit indicators.

3. Figures in bold pertain to median States for the given indicator.

Table: XVIII B Summary Position of Special Category States for 2004-05 (R.E.)

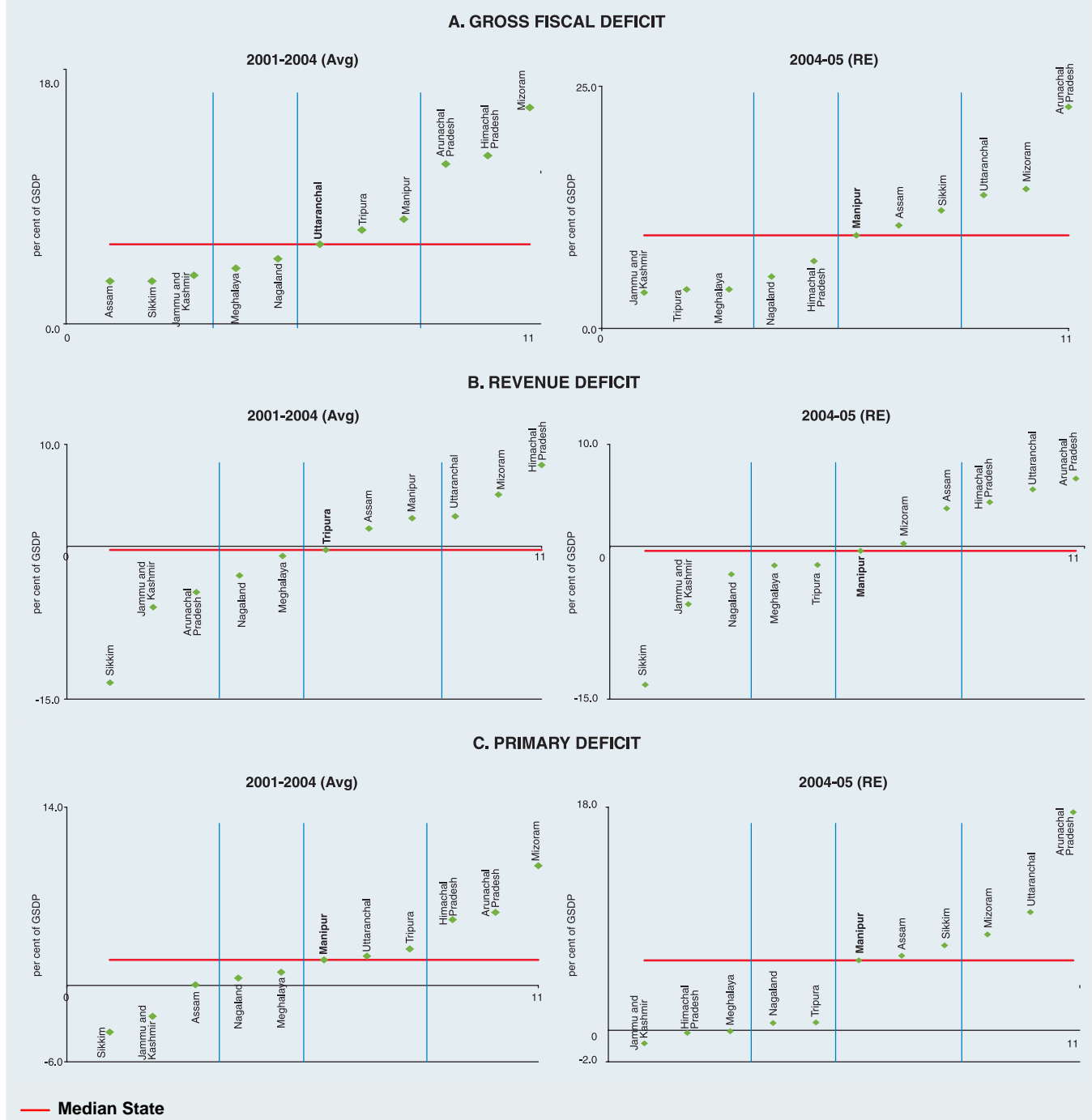
INDICATOR	Quartile 1 (Q1)	Quartile 2 (Q2)	Quartile 3 (Q3)	Quartile 4 (Q4)
(A) RESOURCE GAP				
1. GFD/GSDP	RANGE: 3.7 to 4.0 Meghalaya, Jammu and Kashmir, Tripura	RANGE: 5.3 to 6.9 Nagaland, Himachal Pradesh	RANGE: 9.6 to 12.2 Manipur , Assam, Sikkim	RANGE: 13.8 to 22.9 Uttaranchal, Mizoram, Arunachal Pradesh
2. RD/GSDP	RANGE: -13.7 to -2.9 Sikkim, Jammu and Kashmir, Nagaland	RANGE: -2.0 to -1.9 Tripura, Meghalaya	RANGE: -0.6 to 3.6 Manipur , Mizoram, Assam	RANGE: 4.2 to 6.5 Himachal Pradesh, Uttaranchal, Arunachal Pradesh
3. PD/GSDP	RANGE: -0.6 to 0.3 Jammu and Kashmir, Himachal Pradesh, Meghalaya	RANGE: 0.98 to 1.02 Nagaland, Tripura	RANGE: 5.9 to 7.1 Assam, Manipur , Sikkim	RANGE: 7.9 to 17.5 Mizoram, Uttaranchal, Arunachal Pradesh
4. PRB/GSDP	RANGE: -18.8 to -7.2 Sikkim, Jammu and Kashmir, Nagaland	RANGE: -6.3 to -5.7 Mizoram, Meghalaya	RANGE: -4.9 to -2.5 Tripura , Manipur, Himachal Pradesh	RANGE: -0.8 to 1.4 Assam, Uttaranchal, Arunachal Pradesh
5. RD/GFD	RANGE: -156.4 to -53.4 Jammu & Kashmir, Sikkim, Nagaland	RANGE: -49.2 to -48.1 Meghalaya, Tripura	RANGE: -5.8 to 28.6 Manipur , Mizoram, Arunachal Pradesh	RANGE: 34.0 to 60.8 Assam, Uttaranchal, Himachal Pradesh
6. RD/RR	RANGE: -16.1 to -9.7 Jammu and Kashmir, Sikkim, Nagaland	RANGE: -9.3 to -6.1 Tripura, Meghalaya	RANGE: -2.1 to 11.1 Manipur , Mizoram, Assam	RANGE: 13.5 to 21.8 Arunachal Pradesh, Uttaranchal, Himachal Pradesh
(B) REVENUE PERFORMANCE				
7. OTR/GSDP	RANGE: 1.0 to 1.3 Mizoram, Nagaland, Manipur	RANGE: 1.6 to 2.2 Arunachal Pradesh, Tripura	RANGE: 3.9 to 5.0 Meghalaya , Himachal Pradesh, Sikkim	RANGE: 5.1 to 6.7 Jammu and Kashmir, Assam, Uttaranchal
8. ONTR/GSDP	RANGE: 1.0 to 1.3 Nagaland, Manipur, Tripura	RANGE: 2.0 to 2.1 Himachal Pradesh, Uttaranchal	RANGE: 2.3 to 2.7 Mizoram , Meghalaya, Jammu and Kashmir	RANGE: 7.1 to 51.3 Arunachal Pradesh, Assam, Sikkim
9. CT/GSDP	RANGE: 12.5 to 17.3 Himachal Pradesh, Uttaranchal, Tripura	RANGE: 18.2 to 24.0 Assam, Manipur	RANGE: 26.1 to 28.2 Nagaland, Jammu and Kashmir, Meghalaya	RANGE: 39.8 to 49.4 Arunachal Pradesh, Mizoram, Sikkim
(C) EXPENDITURE PATTERN				
10. DEV/GSDP	RANGE: 14.9 to 19.9 Himachal Pradesh, Tripura, Nagaland	RANGE: 25.1 to 25.4 Manipur, Jammu and Kashmir	RANGE: 25.7 to 37.7 Uttaranchal , Assam, Meghalaya	RANGE: 47.0 to 57.6 Mizoram, Arunachal Pradesh, Sikkim
11. NONDEV/GSDP	RANGE: 9.4 to 11.2 Tripura, Manipur, Assam, Meghalaya	RANGE: 11.2 to 11.6 Himachal Pradesh, Kashmir, Nagaland	RANGE: 12.8 to 14.8 Uttaranchal , Jammu and Mizoram, Sikkim	RANGE: 18.9 to 60.3 Arunachal Pradesh
12. SSE/GSDP	RANGE: 9.4 to 10.3 Himachal Pradesh, Tripura, Nagaland	RANGE: 11.4 to 14.5 Jammu and Kashmir, Assam	RANGE: 14.6 to 15.4 Meghalaya, Uttaranchal , Manipur	RANGE: 22.7 to 27.9 Mizoram, Arunachal Pradesh, Sikkim
13. CO/GSDP	RANGE: 2.7 to 6.0 Himachal Pradesh, Meghalaya, Tripura	RANGE: 7.3 to 8.3 Uttaranchal, Nagaland	RANGE: 9.3 to 10.2 Assam, Jammu and Kashmir , Manipur	RANGE: 13.6 to 25.9 Mizoram, Arunachal Pradesh, Sikkim

Note: 1. The quartile position indicated in this Table is based on the data of fiscal indicators provided in Table XVI B. The grouping of States into four quartiles viz., Q1, Q2, Q3 and Q4 provides the relative position of each State vis-à-vis others for each fiscal indicator. The quartiles have been computed by grouping the States into Special and Non-Special Categories and then arranging the indicators in each category in an ascending order. The type of indicator qualifies the relative position of the quartile. To illustrate, for Debt-GSDP ratio, States in Q1 are the better performed States for that indicator, while for development expenditure to GSDP (DEV/GSDP) ratio, States in Q4 portrays a similar position.

2. Minus (-) indicates surplus in deficit indicators.

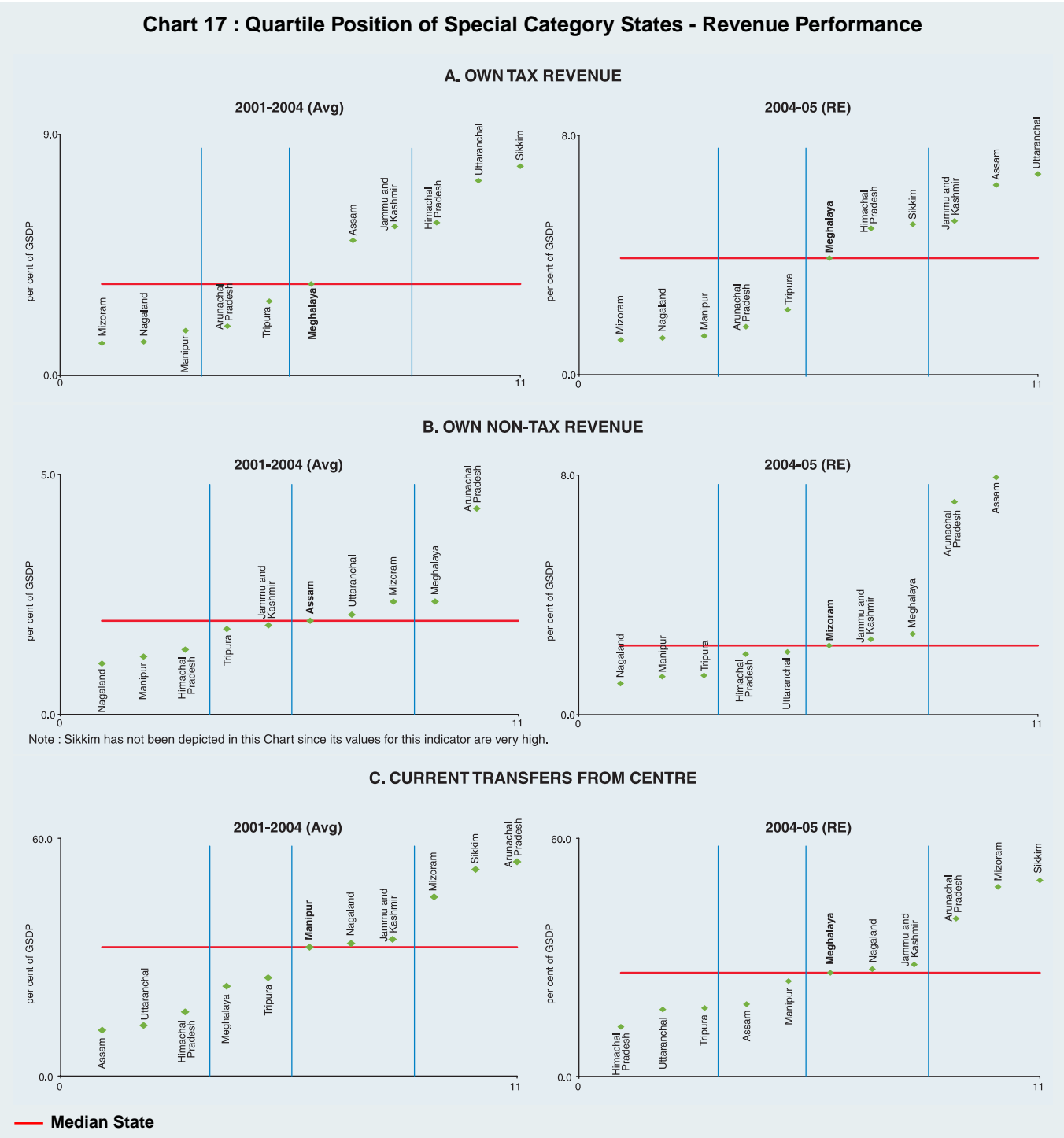
3. Figures in bold pertain to median States for the given indicator.

Chart 16 : Quartile Position of Special Category States - Resource Gap



Assam and Sikkim (Statement 41). On the other hand, barring a marginal decline in Meghalaya, the ratio of expenditure on the broad head of health services to aggregate disbursements improved in all States in 2004-05 (RE) over 2003-04 (Statement

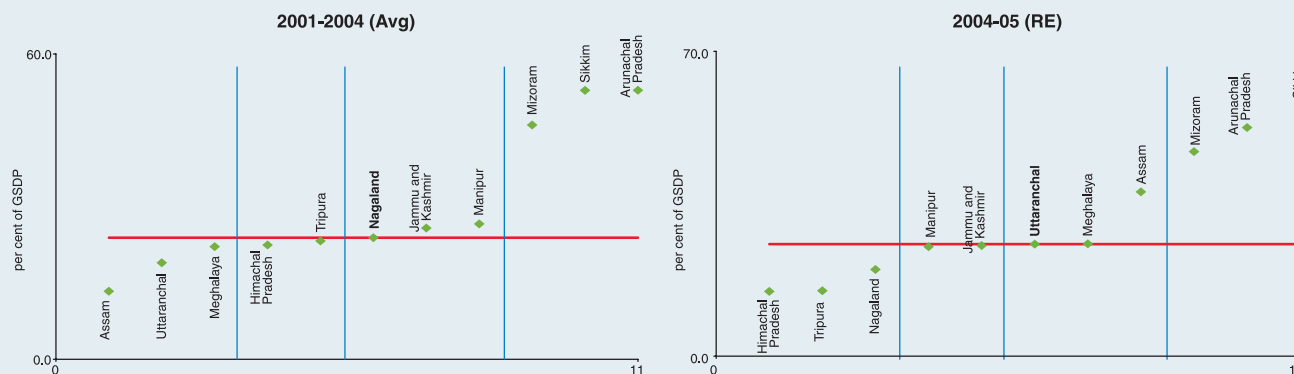
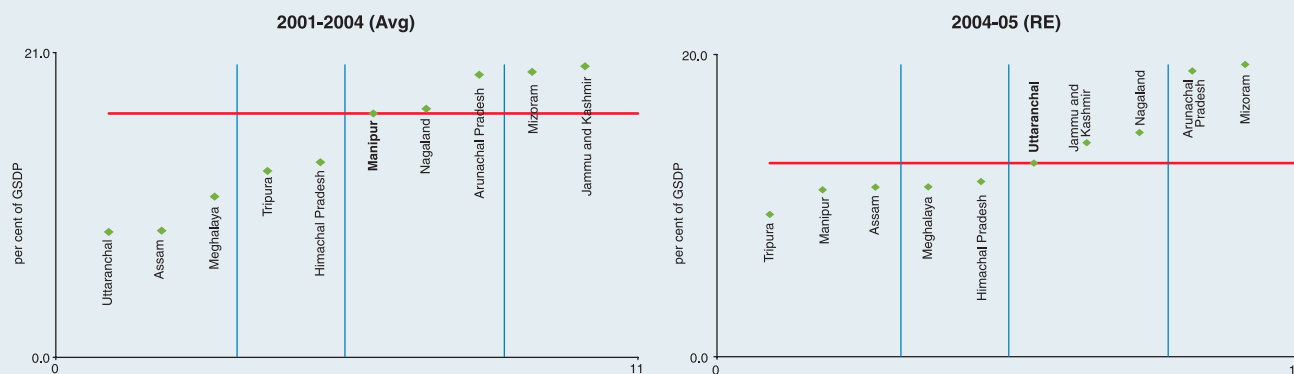
42). However, the ratio was maximum at 4.5 per cent for Jammu and Kashmir in 2004-05 (RE) followed by 3.9 per cent for Himachal Pradesh. This indicates inadequacy of budgetary provisions for the basic health services.



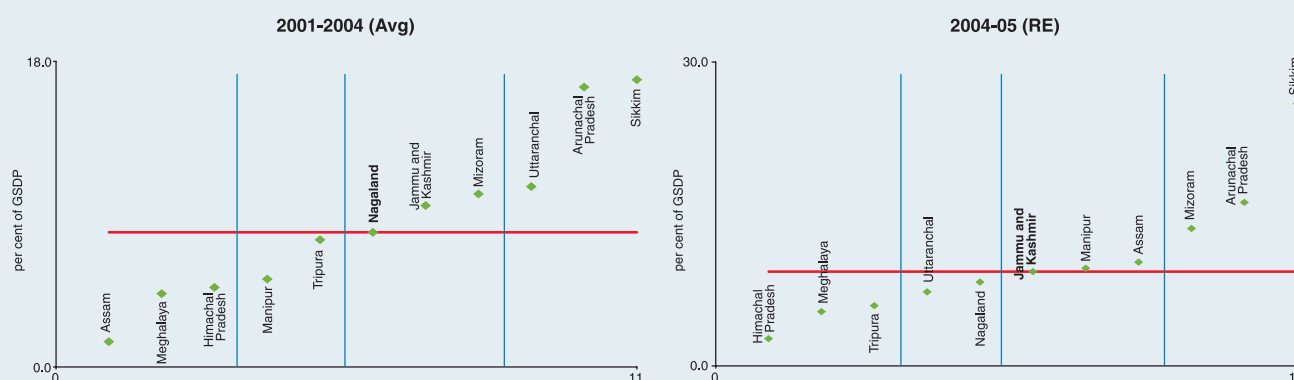
IV.IMPLICATIONS OF TFC RECOMMENDATIONS FOR STATE FINANCES

The Report of the Twelfth Finance Commission (TFC) was presented against the backdrop of the persistent weaknesses in the finances of the State Governments, notwithstanding

the initiatives towards fiscal and institutional reforms by some State Governments in the recent period. Recommendations of TFC have far reaching implications on State finances. This Section discusses implications of major recommendations of TFC relating to State finances.

Chart 18 : Quartile Position of Special Category States - Revenue Performance**A. DEVELOPMENTAL EXPENDITURE****B. NON-DEVELOPMENTAL EXPENDITURE**

Note : Sikkim has not been depicted in this Chart since its values for this indicator are very high.

C. CAPITAL OUTLAY

— Median State

IV.A. Restructuring of Public Finance

In the perspective of restructuring public finance, TFC recommended the States to achieve revenue balance by 2008-09 and reducing GFD to 3 per cent of GSDP by 2009-10. The scheme of fiscal correction included achieving, by 2009-10,

own tax-GDP ratio of 6.8 per cent, primary expenditure-GDP ratio of 14.3 per cent and limiting interest payments of States to 15 per cent of revenue receipts (Table XIX). From the point of view of debt sustainability, TFC recommended a target of 75 per cent for the combined debt-GDP ratio by

Table XIX: Restructuring Plan: State Finances

(As percentage of GDP)

Sr. No.	Items	TFC		Average Annual Adjustment	Sr. No.	Items	TFC		Average Annual Adjustment
		2004-05	2009-10				2004-05	2009-10	
1	2	3	4	5	1	2	3	4	5
1.	States' Own Tax Revenues	5.9	6.8	0.17	9.	Total Expenditure	16.2	16.3	0.01
2.	Tax Revenues	8.4	9.7	0.25	10.	Primary Expenditure	13.3	14.3	0.20
3.	Own Non-tax Revenue	1.2	1.4	0.03	11.	Revenue Deficit*	2.0	0.0	-0.40
4.	Non Tax revenues	3.2	3.5	0.07	12.	Fiscal Deficit	4.5	3.0	-0.30
5.	Total Revenue Receipts	11.6	13.2	0.32	13.	Primary Deficit	1.6	1.0	-0.12
6.	Interest Payments	2.9	2.0	-0.18	14.	Interest Payments/Revenue Receipts	24.9	15.0	-1.99
7.	Total Revenue Expenditure	13.6	13.2	-0.08	15.	Debt (end-Year Adjusted Liabilities)	30.3	30.8	0.11
8.	Capital Expenditure	2.6	3.1	0.10					

* : The target for achieving revenue deficit of zero is 2008-09.

Source : Report of the Twelfth Finance Commission.

2009-10 (30.8 per cent for the States). In terms of long-term target, TFC recommended reduction of the debt-GDP ratio to 28 per cent, each for the Centre and States. As discussed earlier, TFC also provided incentives for fiscal correction by linking it to benefits under debt relief.

IV.B. Fiscal Correction: Distance Path for TFC Targets

The TFC recommended that the States should achieve revenue balance by 2008-09, and reduce the ratio of GFD-GSDP to 3 per cent by 2009-10. It also recommended that the States should bring out in their respective FRL the annual reduction targets for RD and GFD. Benefits in the form of debt relief are linked to enactment of FRL. In view of this, a technical exercise was attempted to measure the distance path for RD and GFD of the States from the respective targets set out by the TFC based on the 2004-05 (RE) estimates of State Governments (Table XX).

As can be observed from Table XX, among the non-special category States, there are two States, namely Karnataka and Madhya Pradesh, which are already in revenue surplus and three States, namely Haryana, Karnataka and Tamil Nadu, which have already achieved the GFD-GSDP target in 2004-05 (RE). The annual average adjustment (reduction) in RD-GSDP ratio to achieve revenue balance in 2008-09 varies from 0.07 per

cent for Haryana to 1.14 per cent for Kerala. Similarly, the annual adjustment (reduction) in GFD-GSDP ratio varies from 0.07 per cent for Andhra Pradesh to 1.02 per cent for Jharkhand. Among the special category States, six out of eleven States were in revenue surplus in 2004-05. However, others (barring Mizoram) had high levels of deficit in revenue account with RD-GSDP ratio placed at 6.5 per cent for Arunachal Pradesh, 5.5 per cent for Uttaranchal and 4.2 per cent for Himachal Pradesh. The annual average reduction in RD-GSDP ratio to achieve revenue balance in 2008-09 varies from 0.04 per cent in Mizoram to 1.64 per cent in Arunachal Pradesh. Contrary to the performance in revenue account, none of the special category States were within the GFD-GSDP target of 3.0 per cent. Annual average reduction in GFD-GSDP ratio to achieve the target of 3.0 per cent by 2009-10 varies from 0.14 per cent for Jammu and Kashmir to 3.97 per cent in Arunachal Pradesh.

Charts 19 to 22 depict the present position of the non-special category and special category States for the revised estimates of 2004-05 in the light of TFC targets recommended for various fiscal parameters.

The position of the States on the various indicators is varied and so is the path they need to traverse in order to achieve the set targets.

Table XX: State-wise Distance Path for Revenue Deficit and Gross Fiscal Deficit

(Per cent)

States	RD-GSDP Ratio			GFD-GSDP Ratio		
	2004-05 (RE)	2008-09 TFC Target	Average Annual Adjustment	2004-05 (RE)	2009-10 TFC Target	Average Annual Adjustment
1	2	3	4	5	6	7
Non-Special Category						
Andhra Pradesh	0.73	0.0	-0.18	3.36	3.0	-0.07
Bihar	0.54	0.0	-0.14	5.64	3.0	-0.53
Chhattisgarh	1.08	0.0	-0.27	5.59	3.0	-0.52
Goa	0.55	0.0	-0.14	3.94	3.0	-0.19
Gujarat	2.45	0.0	-0.16	6.31	3.0	-0.66
Haryana	0.28	0.0	-0.07	1.27	3.0	0.35
Jharkhand	2.47	0.0	-0.62	8.10	3.0	-1.02
Karnataka	-0.33	0.0	0.08	2.70	3.0	0.06
Kerala	4.54	0.0	-1.14	5.27	3.0	-0.45
Madhya Pradesh	-1.38	0.0	0.34	6.29	3.0	-0.66
Maharashtra	2.58	0.0	-0.65	5.19	3.0	-0.44
Orissa	3.82	0.0	-0.95	5.56	3.0	-0.51
Punjab	3.16	0.0	-0.79	5.24	3.0	-0.45
Rajasthan	2.44	0.0	-0.61	6.48	3.0	-0.70
Tamil Nadu	0.89	0.0	-0.22	2.89	3.0	0.02
Uttar Pradesh	2.94	0.0	-0.73	5.60	3.0	-0.52
West Bengal	4.05	0.0	-1.01	5.37	3.0	-0.47
Special Category						
Arunachal Pradesh	6.54	0.0	-1.64	22.87	3.0	-3.97
Assam	3.62	0.0	-0.90	10.63	3.0	-1.53
Himachal Pradesh	4.23	0.0	-1.06	6.95	3.0	-0.79
Jammu and Kashmir	-5.79	0.0	1.45	3.70	3.0	-0.14
Manipur	-0.55	0.0	0.14	9.61	3.0	-1.32
Meghalaya	-1.98	0.0	0.50	4.03	3.0	-0.21
Mizoram	0.17	0.0	-0.04	14.39	3.0	-2.28
Nagaland	-2.85	0.0	0.71	5.34	3.0	-0.47
Sikkim	-13.70	0.0	3.42	12.18	3.0	-1.84
Tripura	-1.93	0.0	0.48	4.02	3.0	-0.20
Uttaranchal	5.48	0.0	-1.37	13.76	3.0	-2.15

‘-’ sign indicates surplus in revenue account

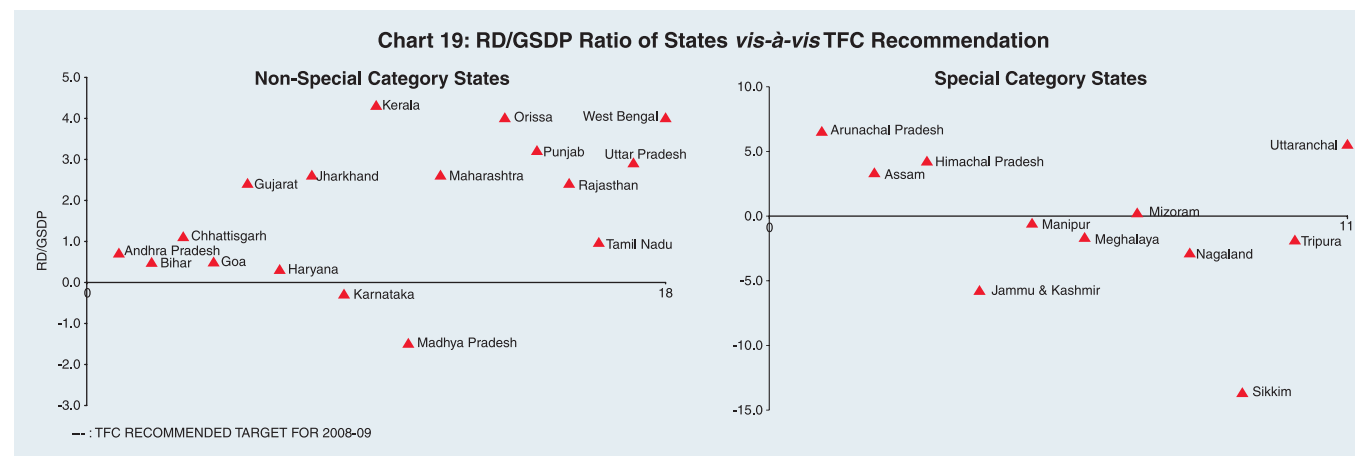
Source : Figures on Revenue Deficit and Gross Fiscal Deficit for 2004-05 (RE) are obtained from the State Budgets while figures on GSDP for 2004-05 are obtained from the website of Ministry of Finance, Government of India.

V. ISSUES AND PERSPECTIVES

V.A. Fiscal Correction and Consolidation

In recent years, fiscal correction and consolidation measures undertaken by several

State Governments have impacted the State finances favourably as is evident from the reduction in fiscal imbalances during the three-year period 2000-01 to 2002-03. The direction of fiscal



State Finances : A Study of Budgets of 2005-06

Chart 20: GFD/GSDP Ratio of States vis-à-vis TFC Recommendation

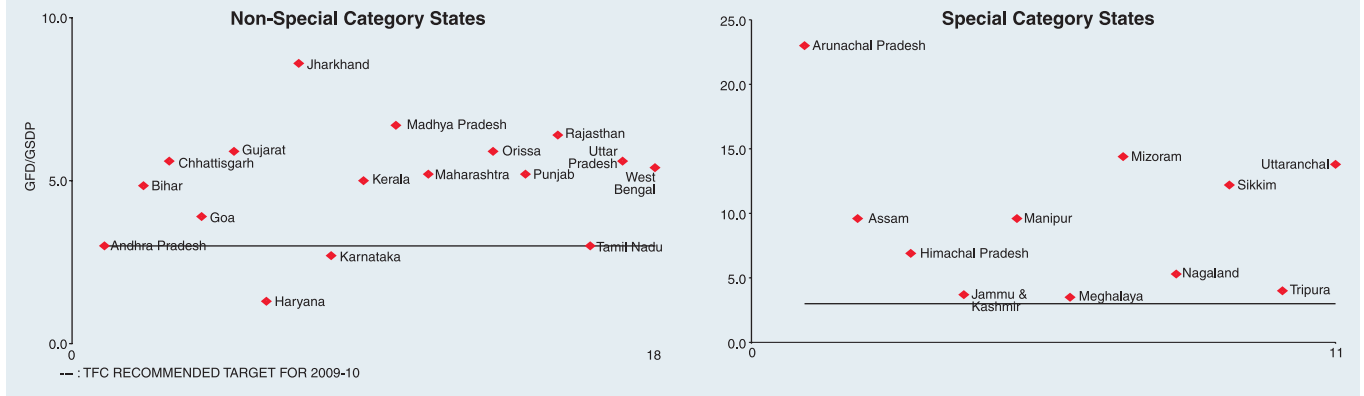


Chart 21 : Debt/GSDP Ratio of States vis-à-vis TFC Recommendation

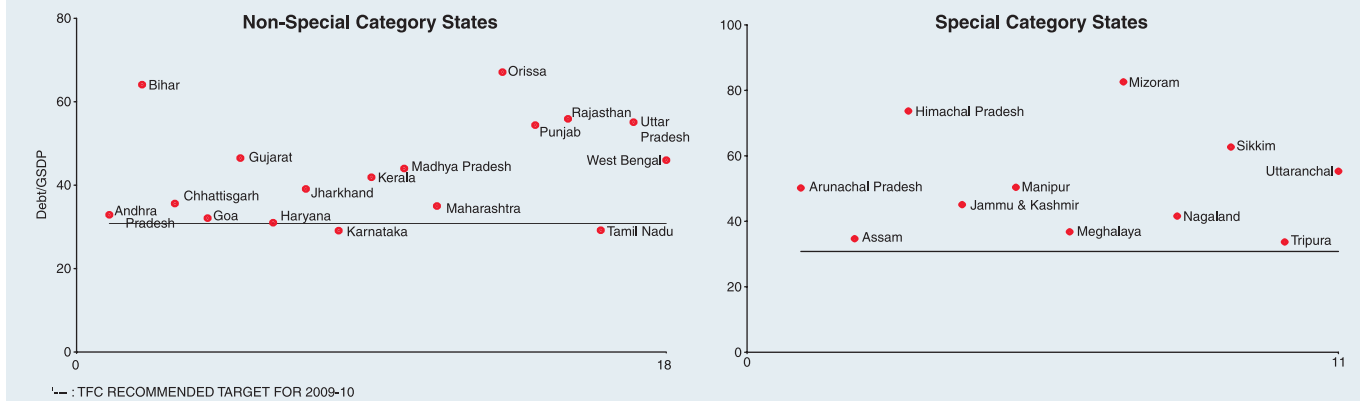
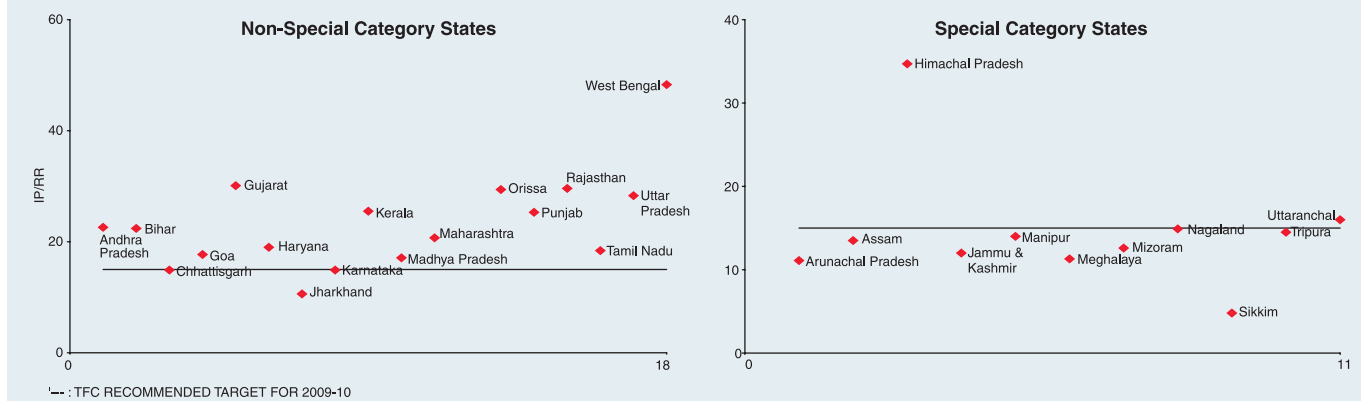


Chart 22 : IP/RR Ratio of States vis-à-vis TFC Recommendation



correction, however, witnessed a setback during 2003-04 partly due to one-off factors relating to the settlement of dues of the State Electricity Boards by the issue of Power Bonds. In the Budgets for 2005-06, the State Governments have committed to carry forward the correction process further and expect to regain the fiscal position as

reflected in key deficit indicators (as a percentage of GDP) that prevailed in the early 1990s. In this context, it is important to recognise that the fiscal position of the States in the medium term would, to a large extent, be shaped by the recommendations of the TFC and the implementation of VAT. Another important

development relates to enactment of FRLs by a majority of the States and proposals to enact legislation by some others. A few issues need to be addressed, so that fiscal correction eventually translates into durable fiscal consolidation.

First, the State Budgets have envisaged sharp correction in the key deficit indicators in 2005-06, particularly in the revenue account. It is also important to note that bulk of the fiscal correction is accounted for by a few major States. However, given the past track record of weak fiscal marksmanship of the State Governments, such a high level of correction within a span of one year appears to be difficult. TFC has provided an overall road-map towards fiscal correction and restructuring of the States in a medium term perspective. To be effective, the States may consider following a gradual and steady approach as specified in the TFC's restructuring scheme.

Second, in its scheme of restructuring, TFC prescribed for progressive correction of a whole set of fiscal indicators, which included targets for different items of receipt, expenditure, debt in addition to targets for deficit indicators. Following a holistic approach, the path for fiscal correction and consolidation of the State Governments should emphasise revenue augmentation, compression and rationalisation of expenditure and containment of debt within sustainable limits.

Third, enactment of FRL providing the path of fiscal correction by majority of the States is a very encouraging development in 2005-06. Making the process of fiscal correction a binding force through FRL is expected to augment fiscal discipline and provide a more realistic correction path.

Fourth, the need for emphasis on the quality of fiscal correction of fiscal imbalances cannot be overemphasised. In the process of correction, capital expenditure and spending on social services should not suffer by falling below some critical threshold level.

V.B. Fiscal Empowerment

Prudent fiscal management prescribes that the path to durable fiscal consolidation lies most importantly through fiscal empowerment *i.e.*, by expanding the scope and size of revenue flows into the budget. A fiscal strategy based on revenue maximisation would also provide the necessary flexibility to shift the pattern of expenditure and redirect them productively. On the other hand, fiscal adjustments based predominantly on expenditure reduction involve welfare losses and risk the danger of triggering a downturn of overall economic activity. There has been some progress in reforming the tax system, although the leakages in tax base through exemptions continue to pose problems. Adoption of the VAT regime by the majority of the States in the current fiscal year is expected to enhance transparency, promote compliance and lead to higher revenue mobilisation. The VAT system would also eliminate the problems of cascading tax burden due to double taxation of commodities as well as multiplicity of taxes through provision of input tax credit and abolition of other related indirect taxes. Thus, there is some merit in extending the VAT principles to tax the consumption of almost all goods and services in the economy.

In this context of fiscal empowerment of the States, augmenting resource mobilisation from non-tax revenues through appropriate user charges, cost recovery from social and economic services and restructuring of State PSUs have to be given due importance. The health of State finances will benefit vastly from improvements in cost recovery of various public services and rationalisation of subsidies. At present, user charges are inadequate for two reasons. First, it is perceived that services are provided by the Government and, therefore need not have to be paid for. Second, with the inferior quality of services, the public is loath to pay higher charges for public services. The attainment of higher efficiency in the provision of services can progressively lead to lower charges. Better cost-recovery will not only improve State finances but

will also create enabling grounds for financial sector development so that each activity becomes financially viable.

V.C. State Finances and Social Sector Development

It is widely recognised that the level of social sector expenditure has important implications for long-term prospects of the economy, with bulk of the responsibilities pertaining to public expenditure on social services including education and health placed in the domain of State Governments. Moreover, the States provide most of the infrastructure services except for telecommunications, civil aviation, railways and major ports and maintain law and order. Therefore, the ability of the States to spend on social services has important implications for social development¹². This is more so in the Indian context as the National Human Development Report (NHDR) has revealed wide disparities in the level of human development across the States. States like Bihar, Uttar Pradesh, Madhya Pradesh, Rajasthan and Orissa had HDI close to just half of that of Kerala in 1981. The situation has improved since then. Besides Kerala, among the major States, Punjab, Tamil Nadu, Maharashtra, and Haryana have done well on HDI. In general, HDI is better in smaller States and Union Territories. In terms of the pace of development, Tamil Nadu, Rajasthan, Madhya Pradesh, West Bengal and Bihar improved their HDI significantly in the 1980s. In the 1990s this momentum was maintained in Rajasthan, Madhya Pradesh and Uttar Pradesh, while it appeared to slow down in other less developed States. Nevertheless, State-wise analysis in the NHDR indicated a decline in such regional disparity during the last two decades. Further convergence can take place alongwith substantial improvement in the national human development index if efforts are focused on those States that have low levels of measured HDI.

Strengthened policy measures and improvement in health, education and other aspects of rural development in these States will contribute greatly to the overall improvement in human development in the country. It turns out that the economically less developed States are also the ones with low HDI and economically better off States are the ones with relatively better performance on HDI. However, the relation between the HDI and the level of development does not show any correspondence among the middle-income States in the country. In this category of States, some States like Kerala, have high attainment of HDI, at the same time, there are States like Andhra Pradesh, or even West Bengal, where HDI values are not as high.

As widely documented¹³, fiscal predicaments of States became evident since 1998-99 due to a variety of factors. While factors like Fifth Pay Commission recommendations, decline in Central transfers, increase in committed expenditure such as interest payments and pensions and low economic growth rate account for the acuteness of the ailment, there are also underlying structural reasons for the persistence of fiscal deterioration. This was having consequent deleterious impact on the States' social sector expenditure including those on education and health. With active initiatives of the States towards fiscal correction and consolidation, some signs of improvements have been visible in State finances in the recent period. Consequent to improvement in State finances, there is also a reversal of the trend of developmental expenditure. Stepping up of expenditure on education and health would be beneficial for promoting human development and improving the quality of overall social infrastructure in the country.

In the above context, it is important to note that availability of resources alone cannot generate social sector development. Effective and efficient use of the funds provided for social services is equally important. In this context, the distinction has

¹² Mohan, Rakesh (2005): "Human Development and State Finances", RBI Bulletin, December, pp.1123-1129.

¹³ Economic Survey, Government of India, 2004-05 and RBI Annual Report, 2004-05.

to be made between the outlay and the outcome. Recent attempt by the Union Government to come out with 'Outcome Budget' is very encouraging. The States should follow suit. There is an imperative need to devise innovative measures in the developmental activities like active participation of *Panchayati Raj* Institutions (PRIs), Non-Government Organisations (NGOs), *etc.* and promotion of micro-finance. In this regard, it is also important to mention that the rural connectivity plays a critical role for higher human development index. Evidence suggests that the States like Kerala, Tamil Nadu, Goa, Punjab and Himachal Pradesh that have invested heavily in the provision of better rural connectivity are also better placed in terms of human development. Thus, better rural infrastructure and connectivity is necessary to accomplish developmental programmes related to human development.

V.D. Debt Sustainability

Another important issue related to State finances pertains to sustainability of debt, which embodies concern about the ability of the State Governments to service their debt obligations. Over the years, large revenue deficits have led to large fiscal deficits and spiraling debt resulting in the emergence of a vicious cycle of deficit, debt and debt service payments for most of the State Governments. There is an increasing market perception that the level of debt is increasingly becoming unsustainable in case of many States as reflected in the under-subscription in the tap issues under the market borrowing programme, despite the prevalence of favourable liquidity conditions. Furthermore, the State Governments have also been increasingly resorting to off-budget borrowings through guarantees and constituting SPVs.

Recognising the magnitude of the problem, several national level agencies such as CAG, Finance Commissions and the Reserve Bank have repeatedly stressed the need to address the

underlying issues related to debt sustainability. In this context, TFC had emphasised the need for imposing a hard budget constraint and suggested that the overall borrowing programme of a State should be within a prescribed limit, determined annually, taking into account borrowings from all sources. A Study¹⁴ on debt sustainability undertaken by the Reserve Bank (a brief summary of which is presented in *Box 2*) emphasised the measures for expenditure compression, improvement in own revenue collection effort and several institutional changes to contain the problem of State level debt in India. Important measures of institutional changes included enactment of FRL for making the process of fiscal discipline legally binding, introduction of guarantee ceilings, participation in the Consolidated Sinking Fund and the Guarantee Redemption Fund. In this connection, it is noteworthy that the FRLs of several State Governments included provisions for caps on the debt-GSDP ratio as well as State guarantees.

V. E. Financing of Resource Gap: Implications of Article 293

In recent years, there has been a substantial increase in the resource gap of the States largely indicating the structural infirmities as reflected in sharp increase in their GFD. In the context of high level of fiscal deficit and debt, a critical issue that has come to the forefront is the imposition of certain restrictions under Article 293 of the Indian Constitution on the borrowings by State Governments. Under Article 293, the States are not allowed to borrow directly from external sources and require the Centre's permission to raise loans domestically as long as, they are indebted to the Centre or have taken guarantees from the Centre in respect of loans raised by them (*Box 3*). It may be indicated that in practice the borrowings under Public Accounts are not subject to Article 293 as these funds do not belong to the State and are raised by the State as a banker.

¹⁴ Rajaraman, I., S. Bhide and R.K. Pattnaik (2005), "A Study of Debt Sustainability at State Level in India", RBI, Mumbai.

BOX 2: A Study of Debt Sustainability at the State level in India – Highlights

Studies on debt sustainability in India, in respect of States, have mostly addressed the issue at an aggregate level. Since the States are heterogeneous in terms of size and characteristics, there was a need for State-specific assessment of debt sustainability. As public debt accumulates, there is legitimate concern over whether the State Governments will be in a position to service its debt. Ultimately, if markets perceive the debt stock of any State as unsustainable, it would cease to hold the securities issued by that State. Several State Governments in India have experienced sharp deterioration in critical indicators of debt sustainability since the mid-1990s. It is in this context that the Reserve Bank conducted an internal study on Debt Sustainability at State Level in India in 2005 with the help of external experts. The Study has been published as a stand alone publication by the Reserve Bank. The major findings of the Study are summarised below :

- By 2002-03, the debt of major States stood at 41 per cent of their combined GSDP, higher by 15.7 percentage points than the average for the five-year period 1992-97. Among the major States, the rise in Bihar was 33 per cent, as against a fall by nearly 1 per cent in Goa.
- Among special category States, the disparity was even wider, between Mizoram, which saw a large increase in debt ratio, and Arunachal Pradesh and Jammu and Kashmir, which actually saw a decline, *albeit*, from high initial levels.
- The worrying aspect of the trajectory of debt among the major States is that the more indebted States prior to 1997 saw larger increases in their debt ratio. Excluding Goa, the rank correlation co-efficient between rankings by levels in 1992-97, and the ranking by change to 2002-03, works out to 0.73, and is statistically significant.
- The interest rate on State debt surpassed the nominal growth rate of GSDP during the period 1997-02. The interest rate on debt of major States, at 10.4 per cent on an average in 1997-02, was higher than the nominal growth rate of GSDP, of 9.9 per cent. This is in contrast to 1992-97, when the interest rate was at 9.9 per cent, as against nominal GSDP growth of 16.1 per cent.
- There was a similar trend for special category States, from average interest of 10.3 per cent and nominal GSDP growth of

13.3 per cent in 1992-97, to 11.7 and 11.5 per cent, respectively in 1997-02. Thus, States will now have to carry overall primary surpluses in order to stabilise debt as a per cent of GSDP.

- States were grouped and ranked by some selected indicators, which were (i) the change in debt/GSDP starting from the average for 1992-97; (ii) the sign of the primary revenue balance in aggregate over 1997-02; (iii) own tax buoyancy, estimated over the period 1980-02 and (iv) the annual growth in non-interest revenue expenditure over 1997-02.
- States in need of expenditure compression and improvement in own revenue collection were identified, and four other institutional changes that were required were listed. These are (i) introduction of guarantee caps; (ii) introduction of fiscal responsibility legislation; (iii) participation in the Consolidated Sinking Fund and (iv) participation in the Guarantee Redemption Fund.
- Budget documents do not provide the full picture on State liabilities including contingent liabilities that would enable a comprehensive assessment of risk. This is important as transparency in budgetary practices enhances credibility of the State Governments.
- There is a need to make a qualitative shift in capital expenditure that will be growth promoting and self-financing, in terms of yielding user charges and other budgetary non-tax revenues in subsequent years. Budgetary cover through the capital account for loss-making non-departmental State PSUs has to be specifically prohibited in the design of fiscal responsibility legislation.
- In a fiscal federation, the ultimate responsibility for macroeconomic control rests with the Government at the national level, the provision for which is enshrined under Article 293(3) of the Indian Constitution. Central control of State borrowings up to now has been partial, and has not been extended to borrowings against small savings collections, or direct borrowings from the public through small savings schemes floated by the State Governments. It is only when the coverage of Article 293(3) is comprehensively extended to all avenues of possible borrowings, then enabling conditions for unsustainable debt paths will be eliminated. This may be possible if the TFC's recommendation for comprehensive borrowing cap to be set by the Centre is operationalised.

Historically, items under Article 293 dominated financing of GFD of the State Governments. Particularly, the component of loans from the Centre, the largest amongst Article 293 items of borrowings of States, accounted for the bulk. However, with

introduction of NSSF and consequent change in accounting, its share declined since 1999-00. In the recent period, securities issued to NSSF have emerged as the dominating component of GFD financing for the States. As a consequence, the

Box 3: Provisions Under Article 293

- (1) Subject to the provisions of this article, the executive power of a State extends to borrowing within the territory of India upon the security of the Consolidated Fund of the State within such limits, if any, as may from time to time be fixed by the Legislature of such State by law and to the giving of guarantees within such limits, if any, as may be so fixed.
- (2) The Government of India may, subject to such conditions as may be laid down by or under any law made by Parliament, make loans to any State or, so long as any limits fixed under Article 292 are not exceeded, give guarantees in respect of loans raised by any State, and any sums required for the

purpose of making such loans shall be charged on the Consolidated Fund of India.

- (3) A State may not without the consent of the Government of India raise any loan if there is still outstanding any part of a loan which has been made to the State by the Government of India or by its predecessor Government, or in respect of which a guarantee has been given by the Government of India or by its predecessor Government.
- (4) A consent under clause (3) may be granted subject to such conditions, if any, as the Government of India may think fit to impose.

Source : Constitution of India

financing pattern of GFD reveals that the share of borrowings under Article 293 has fallen to 33.4 per cent of GFD in 2004-05 from an annual average of 59.5 per cent during 1995-2000. Of the outstanding liabilities of the State Governments as of end-March 2005, about 54 per cent are not covered under Article 293. There is, therefore, a concern that notwithstanding explicit and implicit restrictions under Article 293 with regard to borrowings by the States, the provisions in practice has not been strictly adhered to.

In this backdrop, there is a view that Article 293 restrictions could be extended to encompass all borrowings that finance GFD keeping in view

the increasing concerns over States' debt sustainability. One option could be that a global cap on borrowed resources could be fixed rather than separate caps for each individual instrument. In the event of the sources of borrowings exceeded the global cap, the States would have the following options: (i) use fresh surplus borrowings to prepay their outstanding high cost liabilities (*e.g.*, NSSF) and/or (ii) reduce their recourse to market borrowings.

In this backdrop, the international experience on borrowing restrictions in sub-national Governments is briefly discussed in the *Box 4*.

Box 4: Borrowing Restrictions in Sub-National Governments: Principles, Practices and Lessons

Under a federal fiscal structure, the sub-national Governments may borrow excessively to the level their debts become non-sustainable, unless restrained. Counties have adopted various institutional approaches to contain sub-national borrowings as set out below:

(i) **Market Discipline** - Many counties rely on capital markets to contain sub-national borrowings. In such cases, the Central Government does not set any limits on sub-national borrowings and the provincial Governments are free to decide how much to borrow, whom to borrow from and what to spend the borrowed money on. Sub-national Governments may decide by themselves to adopt a fiscal rule in order to enhance their credit standing in the market. Such self-imposed rules exist in Canada, Switzerland and the United States.

(ii) **Administrative Constraints** - In several counties, the Central Government is empowered with direct control over sub-national borrowings. This control may take various forms, including the setting of annual (or more frequent limits) on the overall debt of individual sub-national jurisdictions (as in Lithuania since 2001), special treatment or prohibition of external borrowings, review and authorisation of individual borrowing operations (including approval of the terms and conditions as in Bolivia), or the centralisation of all Government borrowings with on-lending to sub-national Governments (as in Latvia and Indonesia).

(iii) **Rule Based Controls** - The Central Government can contain sub-national borrowings by imposing fiscal rules. Rules may take the form of restrictions on overall budget deficits (Austria, Spain), operating budget deficits (Norway), indicators of debt-servicing capacity (Spain, Japan, Brazil, Korea), level of accumulated sub-national debt (Austria), or level of spending (Belgium, Germany). Alternatively, 'golden rules' establish no ceilings but limit borrowings to investment purposes (Germany).

(iv) **Co-operative Arrangements** - Under the co-operative approach, variations of which exist in several European countries and in Australia, a negotiation process between the Federal and the lower levels of Government designs sub-national borrowing controls. Sub-national Governments are actively involved in formulating macro-economic objectives and the key fiscal parameters underpinning these objectives, thus becoming co-responsible for their achievements. This process leads to an agreement on the overall deficit targets for the general government, as well as on the main items of revenue and expenditure. Specific limits are then agreed upon for the financing requirements of individual sub-national jurisdictions.

Based on their survey of the approaches to control sub-national borrowings, Ter-Minassian and Craig (1997) drew four main conclusions:

- Sole reliance on market discipline for Government borrowings is unlikely to be appropriate in many circumstances. However, market discipline can be useful complement to other forms of borrowing control.
- The case for centralised administrative controls on sub-national borrowings is not strong; in particular, it undermines transparency.
- Rules-based approaches to debt control would appear preferable, in terms of transparency and certainty, to administrative controls.
- These considerations would argue for setting global limits on the debt of individual sub-national jurisdictions on the basis of criteria that mimic market discipline.

Singh and Plekhanov (2005) in a recent cross-country empirical analysis have come out with the following inferences:

- No single institutional arrangement seems to be superior to all the other under all circumstances.
- Giving unconstrained borrowing authority to sub-national Governments is unlikely to be an optimal solution. At low levels of vertical fiscal imbalances, fiscal rules adopted by sub-national Government themselves seem to lead to better fiscal outcomes.
- As vertical imbalances widen, the positive effect of self-imposed rules declines rapidly and centrally imposed fiscal rules seem to become the best option both in the short and long runs, especially in emerging economies.
- Central Governments should avoid bailing out sub-national Governments wherever possible, as bailouts significantly erode the effectiveness of borrowing controls. In the presence of bailout experiences, centrally imposed fiscal rules seem to be the most effective.

References :

1. Singh, Raju and Alexander Plekhanov (2005): "How Should Sub-national Government Borrowing Be Regulated?" IMF Working Paper, WP/05/54, International Monetary Fund, March.
2. Ter-Minassian, Terra and John Craig (1997): "Control of Sub-national Government Borrowing", in Ter-Minassian, Terra (*Eds.*), *Fiscal Federalism in Theory and Practice*, International Monetary Fund.
3. World Bank (2005): "State Fiscal Reforms in India - Progress and Prospects", Macmillan India.

V.F. Market Borrowings *versus* NSSF

Among the items of GFD financing, the securities issued to NSSF have emerged as the dominant component constituting over two-third of GFD in the recent period. This is an exogenous source of financing GFD for the States as determination of the quantum and cost of these borrowings are not under their purview. Given the higher cost of small savings than the market borrowings at present, at least in respect of those States who receive over-subscription in tap issues and a finer spread at the auctions, a few States put forth their preferences for market borrowings over NSSF.

High cut-off yields in auctions and under subscriptions in tap issuances were generally evident in the past, even when interest rates remained soft. On the other hand, there is a view that securities issued to NSSF provides a secure, steady and a regular source of borrowing for funding GFD with a longer redemption profile unlike market borrowings that carries a lower maturity profile of about ten years and large bullet repayments, even though the interest rate is lower. Thus, in the context of borrowings from NSSF *versus* market borrowings, there are trade-offs between lower interest rates of market borrowings and longer maturity and stability of NSSF.

In light the above the following issues need to be addressed. First, a close look at the repayment profile of the States reveals that the redemption profile is sharply skewed resulting in large bullet repayments during 2012-13 to 2014-15 (Statement 36-37). The repayment schedule of market loans has a bearing on the future volume of gross borrowings. It is pertinent to note that repayment of market borrowings would double by 2007-08 (Rs.14,544 crore) from the level of 2005-06 (Rs.6,274 crore). Further, the repayment would rise to the level of three-fold by 2010-11 (Rs.18,859 crore) and nearly six times by 2014-15 (Rs.36,374 crore).

Second, with the passage of the Bill for Pension Fund Regulatory and Development Authority (PFRDA), tax savers/small savers may substitute pension funds for small savings as an investment avenue. Withdrawal of presently available fiscal concessions on small savings would also have implications for accretion of small savings. In view of this the Government of India has recently appointed a Committee to draw a road map for moving towards an 'Exempt-Exempt-Tax' regime for all savings instruments (including small savings schemes) which are exempted from tax at all three stages i.e. contribution, accumulation and withdrawal.

Third, given the trade-off as discussed above, one option could be to give the States freedom to exercise the choice of borrowing instruments *viz.*, NSSF *versus* market borrowings based on the relative advantage for respective States. While the better creditworthy States may prefer market borrowings on account of its perceived lower interest cost, others may prefer the small savings route on account of their relative certainty and stability. Moreover, if a State does not require excess receipts from NSSF, the Centre may either use the excess amount to finance its own GFD or empower NSSF to lend to other States that do not have resources to match their approved overall borrowing limits.

Fourth, in the context of perceived high cost nature of NSSF, prepayments of loans from NSSF by the State Governments and realignment of interest rates on NSSF to market rates may also be explored (*Box 5*).

V.G. Surplus Cash Balances

There has been a sharp accumulation of the surplus cash balances of the State Governments in the recent years, particularly since the beginning of the fiscal 2005-06 (*Box 6*). This could be attributed to several factors such as (i) containment of expenditures by the State

Box 5: Prepayment of Loans from National Small Savings Fund

The National Small Savings Fund (NSSF) set up in April 1999 invests in Special State Government Securities (SSGS) from the net small savings collections so as to facilitate the States in financing their fiscal deficits. These securities have a 25-year tenor with a 5-year moratorium on repayments. The interest rate on SSGS has been gradually reduced from 13.5 per cent in 1999-2000 to 9.5 per cent since 2003-04. The entire net collections accredited to the NSSF are being invested in SSGS since 2002-03, although the States used a portion of this to prepay their high cost liabilities to the Centre under the Debt Swap Scheme (DSS) operated between 2002-03 and 2004-05. With the discontinuance of the DSS in 2005-06, the States have access to the entire net small savings collections as against only 60 per cent in 2004-05. Buoyant small savings collections have led to a sharp increase in the annual investment made by NSSF in SSGS (excluding the liabilities of the Union Territories with legislatures to the NSSF) from Rs.25,753 crore during 1999-2000 to Rs.83,746 crore in 2004-05. As at end-March 2005, the outstanding amount of SSGS was Rs.2,86,357 crore. Maharashtra had the highest outstanding investment made by the NSSF at Rs.47,010 crore, followed by West Bengal (Rs.42,017 crore) and Gujarat (Rs.30,163 crore). Out of the total debt outstanding with the NSSF as at the end of March 2005, Rs.1,39,515 crore was raised at interest rates higher than the rate on SSGS prevailing at present *i.e.*, 9.5 per cent. A few State Governments expressing concerns regarding the level of interest rates charged on the SSGS have proposed prepayment of outstanding amount of SSGS with debts contracted at market-related rates. In this context, some options to reduce the interest burden of State Governments are set out below:

One option is to swap the existing high cost debt carrying interest rates over 9.5 per cent with fresh receipts from the NSSF in a phased manner. A second option could be to allow the States to enter the market to raise the required resources for the debt swap. However, given the investors' lack of appetite for the State Development Loans (SDLs), only the fiscally prudent States

would be in a position to raise market borrowings at relatively cheaper rate of interest. Further, such additional market borrowings would put pressure on debt and monetary management. Moreover, replacing SSGS, which have a 25-year tenor and a repayment schedule spread over 20 years, with market loans which have a maximum tenor of 13 years and involve bullet repayments, would create humps in repayment schedule of market borrowings and, therefore, may not be in the interests of the States. A third option could be to switch to back-to-back repayments as suggested by the Expert Committee to Review the System of Administered Interest Rates and Other Related Issues (Chairman: Dr.Y.V.Reddy) in order to eliminate the maturity mismatches arising out of the maturity structure of small savings schemes and the terms of repayment by the States. In this regard, the Committee favoured elongating the tenor of the small savings schemes towards medium to long-term as against rescheduling the entire outstanding loans and shortening the maturity of loans to six years as the latter option would exert pressure on the State Government finances, given the present fiscal position of the States and the ongoing fiscal reforms. A fourth option may be to revert back to the 80:20 formula which will limit NSSF investment in SSGS to 80 per cent of the net collections with the balance to be invested in Central Government securities.

The Central Government may also consider realignment of the administered interest rates of small savings to market rates. In this regard, implementation of the Advisory Committee to Advise on the Administered Interest Rates and the Rationalisation of Savings Instruments (Chairman: Dr. Rakesh Mohan) recommendation would imply rate reductions ranging from 0.75 per cent to 2.16 per cent from the prevailing small savings rates. This would stem the losses that the NSSF is facing at present. It would further enable a reduction in the interest rates of SSGS from the present level of 9.5 per cent. The Central and State Governments could also consider reducing the commissions that are currently being offered to the small savings agencies so as to bring down the cost of mobilising small savings deposits.

Governments particularly, non-interest revenue expenditure and stagnant capital outlay, (ii) large Central transfers in the light of TFC recommendations and higher economic growth, (iii) buoyant receipts under various small savings schemes, (iv) completion of DSS and (v) better liquidity management by the States. States invest their temporary surplus cash balances in 14-Day Intermediate Treasury Bills with current rate of return of 5.0 per cent. The States earn a negative spread on the reverse flow of resources from the Centre since the surpluses are funded by the borrowings mobilised at a significantly higher costs. This has debilitating impact on the revenue

balances of the State Governments. Furthermore, the volatile nature of investments in 14-Day Intermediate Treasury Bills complicates the Centre's cash management. In view of the above, if the States perceive their surplus cash balances to be of enduring nature, appropriate options may be given for deployment of such balances.

V.H. Loans from Banks and Financial Institutions (Negotiated Loans)

The borrowing requirements of the State Governments has made the State Governments raise loans from banks and financial institutions, *inter alia*, LIC, GIC, NABARD, NCDC, HUDCO and

Box 6: Surplus Cash Balances of State Governments

The surplus cash position of State Governments could be attributed to the various factors as follows:

- Increase in Central transfers in the form of grants and share in Central taxes as recommended by TFC and implemented by the Central Government which has lowered the financing gaps of the States.
- Enactment of FRL and adherence to the fiscal restructuring plan of the TFC would enable the State Governments to avail of debt relief in terms of debt write-off and rescheduling of loans from the Centre. If States were able to pursue the roadmap as chalked out by the Report of the TFC, their fiscal situation would improve further.
- There has been buoyancy in small savings collection over the last few years. Small savings collection is expected to remain buoyant in 2005-06 on account of the favourable interest spread and tax concessions *vis-à-vis* other savings instruments such as bank deposits. In terms of the Union Budget 2005-06, investments in SSGS would amount to Rs.90,000 crore in 2005-06 as against Rs.85,000 crore in 2004-05.
- Since 2002-03, the entire small savings collection (net of repayments) accrue to the States. With the discontinuance of the DSS, the entire small savings receipts (investments in SSGS by NSSF) is available for funding the gross fiscal deficit for 2005-06 as against only 60 per cent in 2004-05.

In view of the above reasons, there has been a surplus funding of gross fiscal deficit (GFD) during 2005-06 so far, as reflected in the turnaround in the liquidity position of States. It may, however, be noted that the degree of such over-funding varies across States with the possibility that some States may revert to WMA in the future that would likely be more in the nature of temporary liquidity mismatches. At the aggregate level, however, the liquidity position of the States is expected to remain in surplus. The build-up in the surplus cash balances has implications on (i) revenue balance of States, (ii) Centre's cash management and (iii) open market operations of the Reserve Bank. First, the interest cost of borrowings against small savings at 9.5 per cent and of market borrowings at around 7.4 per

cent is significantly higher than the return earned by States in its investments of surplus cash balances in 14-Day Intermediate Treasury Bills at 5.0 per cent, implying a reverse transfer of resources from States to the Centre and a lower rate of return to States, which has an adverse impact on their revenue balances.

Second, the Centre enjoyed a surplus cash balance during the first half of 2005-06. The peak surplus cash balances recorded during this period amounted to Rs.23,685 crore. On June 20, 2005, Centre's cash balances amounted to Rs.18,038 crore. On the same day, States' surplus cash balances amounted to Rs.28,552 crore. Had it not been for the investments of States' surplus cash balances in 14-Day Intermediate Treasury Bills, the Centre would have been in WMA. It may be indicated that the volatile nature of investments in 14-Day Intermediate Treasury Bills complicates Centre's cash management.

Third, the Centre deploys the surplus cash balances in Government Securities held by the Reserve Bank thereby saving on the interest that it would have to pay otherwise on the dated Government securities held by the Reserve Bank. The yield on such securities is higher than that received by States in their investments in Centre's 14-Day intermediate Treasury Bills, thereby enabling the Centre to earn a positive spread on its investments of surplus cash balances. Finally, investments of Centre's surplus cash balances constrain RBI's open market operations in view of the finite stock of Government securities available with the Reserve Bank.

Whenever States have surplus cash balances, they find it prudent to lock in the funds by investing in consolidated sinking fund (CSF) and guarantee redemption fund (GRF) to meet future redemptions/devolvments. The investments in CSF and GRF are deployed in Government of India dated securities held by the Reserve Bank. States, nevertheless, would earn a negative spread on account of their higher cost of market borrowings *vis-à-vis* the Centre that would impact on their revenue balances. Some States have sought the Reserve Bank's permission to utilise the interest income accrued and invested in CSF to redeem part repayment of market borrowings for the year 2005-06, presumably to improve upon their fiscal indicators for the current year.

REC. The interest rates and other terms and conditions on such loans are negotiated between State Governments and the lending institutions may depend upon the creditworthiness and fiscal soundness of individual State Governments, track record of the State Governments and honouring of guaranteed obligations.

Since the loans from banks and other financial institutions (*i.e.*, negotiated loans) compromise the discipline of having an overall market borrowing programme, as well as go against the norms of credit discipline, the Reserve Bank does not allow the commercial banks to lend directly to State

Governments. Accordingly, the commercial banks do not lend directly to the State Governments except under market borrowing programme. Banks can, however, fund viable projects guaranteed by State Governments. The data on the negotiated loans are not transparently presented in the Budget documents and due to non-availability of data on the maturity structure and rate of interest in the State Budgets, it is difficult to work out the share of high cost borrowings. However, the information obtained from a few State Governments reveals the high cost nature of this category of debt on which interest rate varies in the range of 8 to 24 per cent,

reflecting significantly high risk premia. This brings into picture the case of debt-swap for prepayment of these high cost loans. It may be noted that the Union Budget 2004-05 had proposed extending the facility of debt swap by allowing States to raise fresh loans and repay their old high-cost loans to NABARD and some other agencies.

Consideration for further prepayment of balance high cost negotiated loans may be viewed in the context that any additional market borrowings to meet such prepayments over and above the level projected by the Reserve Bank would have implications for monetary management. Moreover, this could also exert pressure on debt management on account of lack of investors' appetite for SDLs.

V.I. Discontinuation of Central Plan Loans: Implications for Market Borrowings

As observed by TFC, due to multiplicity of transfers from the Centre to the States through the Finance Commission, the Planning Commission and various Central Ministries, the inter-governmental fiscal transfers suffers from many inadequacies and inefficiencies. With particular reference to Central Plan Assistance (CPA) from the Planning Commission, TFC highlighted that the rate of interest charged is, at times, higher by 300 to 400 basis points than the cost of funds for the Centre. Furthermore, such an arrangement is pushing the States into higher indebtedness on account of structurally mandated borrowings. In this backdrop, TFC has recommended for doing away with Plan loans and extending entire Plan assistance in the form of grants only. Furthermore, TFC recommended that States be allowed to decide whether to borrow from the market or from the Centre, thus eliminating the process of on-lending. However, if fiscally weaker States are unable to raise funds from the market, TFC recommended that the Centre could borrow for on-lending to such States and charge a rate of interest aligned to the marginal cost of its borrowings.

The recommendation of the TFC on doing away with the loan portion of the CPA and discontinuation of Central intermediation have significant implications for the future market borrowings of the State Governments. Assuming all other sources of financing GFD remaining unchanged, the shortfall due to elimination of Central Plan loans is expected to be compensated by the increase in market borrowings. By resorting to the market borrowings, the State Governments would be exposed to market discipline. It is important to note that the quantum of market borrowings by the State Governments in the future has to be consistent with the GFD envisaged in their FRLs and would also critically depend upon the other sources of borrowing in the Consolidated Fund and the Public Account.

The immediate concern of the various stake holders associated with the market borrowings of the States is regarding their ability to raise additional resources directly from the market over and above their normal open market borrowings for the current year. Such concerns emanated from the experience of open market borrowings during 2003-04 and 2004-05, when the open market borrowing programme of the State Governments had received lukewarm response from investors, reflecting in part, their excess holdings of Government securities for the purpose of maintenance of statutory liquidity ratio (SLR) with the banking system, the increasing availability of alternative avenues for lending as economic activity gathered momentum and apprehensions regarding the quality of fiscal and economic performance of the State Governments.

To address various issues related to future market borrowings of the States, the Government of India has constituted a Technical Group (Chairperson: Smt. Shyamala Gopinath, Deputy Governor, RBI). The Group is constituted with representatives from the Government of India, the Reserve Bank and select State Governments.

V.J. Contingent Liabilities

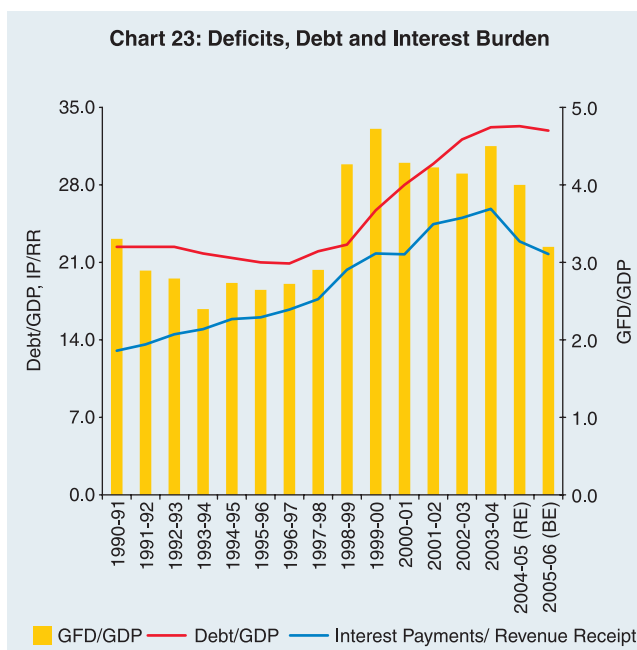
Apart from the borrowings routed through the budget, State Governments have resorted to off-budget borrowings. States have taken recourse to borrowings through public sector enterprises (PSEs) under their control, enabling them to float bonds against State Government guarantees. Other special purpose vehicles mainly for infrastructure financing have also come into the picture. Although the contingent liabilities do not form a part of the debt of States, in the event of default by the borrowing entities, the States will be required to meet the debt service obligations. At the same time, non-adherence to the payment obligations committed by the States in respect of guarantees already provided by them would have adverse implications on the sovereign credibility. In addition, this may pose difficulties for the States to raise resources from the market in future.

The amount of outstanding contingent liabilities (guarantees), the information on which is available for select 17 State Governments, has moved up sharply from Rs. 40,158 crore as of end-March 1992 to Rs.1,84,294 crore as of end-March 2003. The latest available information in respect of 14 States¹⁵ indicates that the amount of guarantees has gone up to Rs.2,05,785 crore by end-March 2004 (Statement 43). While five States have set up Guarantee Redemption Funds (GRF), nine State Governments have fixed statutory/ administrative ceilings on State Government guarantees. It would be useful if rest of the States also implement such institutional measures. In this connection, it is noteworthy that the FRLs enacted by the State Governments already contain provisions relating to a cap on the debt-GSDP ratios as also on the guarantees. Thus, progressive enactment of FRLs by rest of the State Governments would invoke discipline with regard to guarantees.

VI. SPECIAL THEME: OUTSTANDING LIABILITIES OF STATE GOVERNMENTS

The structural weaknesses of the State finances manifested in large and persistent revenue deficit resulting in high GFD and large accumulation of debt and a concomitant increase in debt service burden. Interest payments on the debt of State Governments have pre-empted an increasing proportion of revenue receipts. The debt and interest and deficit spiral has adversely affected the State Governments (Chart 23). It needs to be mentioned that DSS had brought about a decline in the interest burden of the State Governments.

While analysing the debt position of States, an important issue which needs to be addressed is the methodology and the coverage of outstanding liabilities of State Governments. Conceptually, the coverage of debt needs to be GFD consistent implying that all the items covered under GFD necessarily should form part of debt. Hitherto, however, reserve funds, deposits and advances and contingency funds were excluded from the coverage of debt in this Study



¹⁵ The amount of guarantees provided by these 14 State Governments amounted to Rs. 34,172 crore as on end-March 1992 and Rs. 177,751 crore as of end-March 2003.

in the earlier years. Hence, this Study has expanded the coverage of debt to include reserve funds, deposits and advances and contingency funds. Consequent upon discussions in an earlier Conference of State Finance Secretaries organised by the Reserve Bank, a Working Group on Compilation of Data on State Government Liabilities was set up with the members comprising select State Finance Secretaries, Government of India and Comptroller and Auditor General (CAG). The Report has since been submitted. This Study has prepared a new series of debt for each of the State Governments on the basis of the expanded coverage.

VI. A. Revised Coverage and Methodology

In an attempt to construct a new data series on State debt, the methodology that had been hitherto adopted in this Study has been revised to make it GFD consistent. These data series provides a detailed State-wise and item-wise break-ups of outstanding liabilities. The methodology and coverage for preparing the comprehensive database on State Governments debt is provided in *Box 7*.

VI. B. Consolidated Position

The data on aggregate outstanding liabilities

along with component break-up as well as their proportions to GDP are provided in Appendix Tables 19-20.

VI.B.(i) Aggregate Outstanding Liabilities

In absolute terms, outstanding liabilities of State Governments have increased over 8 times from Rs.1,28,095 crore in 1991 to Rs.10,40,834 crore in 2005 at an average annual growth rate of 15.6 per cent (Table XXI). As a ratio to GDP, the outstanding liabilities moved up from 22.5 per cent at end-March 1991 to 33.5 per cent at end-March 2005. It may be mentioned that the TFC has recommended for States Government finances a target of 30.8 per cent for Debt-GDP ratio and 15.0 per cent for interest payments to revenue receipts ratio to be achieved by 2009-10.

The widening of fiscal deficits of the State Governments since 1998-99 have translated into a sharp rise in States' outstanding liabilities relative to GDP to 31.6 per cent during 2001-2005 *i.e.*, an increase of 9.0 percentage points (or 1.79 percentage points per annum) during the period 2001-05 over the previous quinquennium. As against this, the growth in debt-GDP ratio was 0.45 percentage points during the five-year period of

Box 7 : Revised Coverage, Methodology and Data Source of Debt

Revised Coverage

Total Outstanding Liabilities comprises of various account items under consolidated fund, public account and contingency fund.

I. Consolidated Fund

1. Public Debt

- a) Open Market Borrowings
- b) Borrowings from Banks and Financial Institutions
- c) Special Securities issued to NSSF
- d) Bonds/Debentures which are issued by the State Governments
- e) Loans from the Centre
- f) Others

2. Ways & Means Advances & Overdrafts from RBI

II. Public Accounts

1. State Provident Funds
2. Small Savings, Insurance and Pension Funds, Trust and Endowments, *etc.*
3. Reserve Funds/Sinking Funds
4. Other Items in Public Accounts
5. Deposits and Advances

III. Contingency Fund

Methodology

The Reserve Bank, based on CAG's data series on outstanding liabilities of State Governments with a base year has been compiling a data series of outstanding liabilities of the State Governments on yearly basis by adding the budgetary flows. In this year's Study, the data series of outstanding liabilities of State Governments has been revised by broadening its composition to include reserve funds, deposits and advances and contingency funds of State Governments. The debt series has been compiled by taking the data provided by the CAG in 'Combined Finances and Revenue Accounts of Union and State Governments in India'. In the absence of any particular data in the said publication, corresponding data from the State Budgets have been incorporated.

Data Source

The Combined Finance Accounts (CFA) of Central and State Governments published by the Comptroller and Auditor General, State Budgets and data from the Reserve Bank records.

Table XXI: Total Outstanding Liabilities of States

(per cent)

end March	Outstanding Liabilities		
	Amount (Rs.crore)	Annual Growth	Debt / GDP
1	2	3	4
1991	128,095.21	—	22.5
1992	146,966.01	14.7	22.5
1993	168,292.88	14.5	22.5
1994	187,912.46	11.7	21.9
1995	217,022.73	15.5	21.4
Average (1991-1995)	169,657.86	14.1	22.2
1996	250,813.06	15.6	21.1
1997	286,704.07	14.3	21.0
1998	336,346.65	17.3	22.1
1999	397,370.16	18.1	22.8
2000	505,009.26	27.1	26.1
Average (1996-2000)	355,248.64	18.5	22.6
2001	592,742.68	17.4	28.4
2002	685,473.90	15.6	30.2
2003	797,683.75	16.4	32.4
2004	922,262.92	15.6	33.4
2005 RE	1,040,834.36	12.9	33.5
Average (2001-2005)	807,799.52	15.6	31.6
2006 BE	1,152,530.07	10.7	33.1

1996-2000 over 1991-1995 (or 0.09 percentage points per annum) (Table XXI). Thus, the incremental debt-GDP ratio on an average has risen sharply in recent years, with the concomitant rise in debt service burden indicating a worrisome fiscal situation.

VI.B.(ii) Component-wise

The detailed annual component-wise break-up of outstanding liabilities of State Government from 1990-91 to 2005-06 (BE) are presented in Appendix Tables 20 and 21.

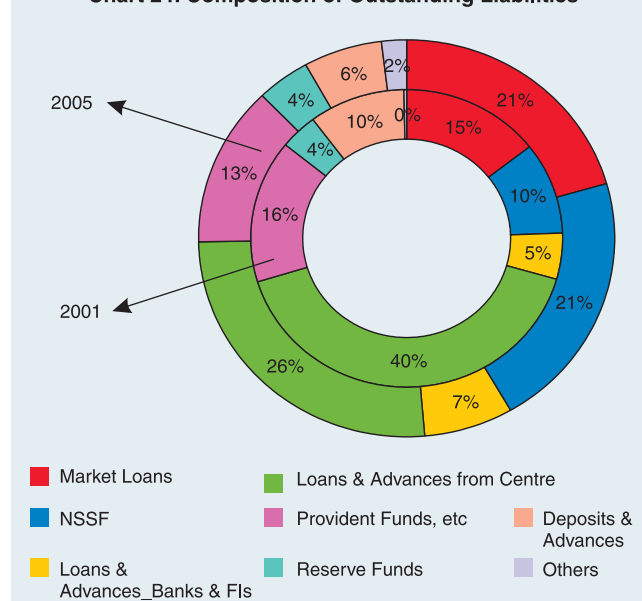
Outstanding debt of the States comprises internal debt (including market borrowings, special securities issued to the NSSF since 1999-2000, loans from banks and financial institutions, WMA and ODs from the Reserve Bank, loans from the Centre, Contingency Fund and public accounts liabilities (including State Small Savings, Reserve Funds and Deposits and

Table XXII: Components of Outstanding Liabilities of State Governments

(per cent to total)

Components of Outstanding Liabilities	End-March 1991	End-March 2000	End-March 2004	End-March 2005
1	2	3	4	5
1. Internal Debt	15.0	22.9	46.4	50.4
of which:				
(i) Market Loans	12.2	14.9	19.5	20.5
(ii) Small Savings (NSSF)	—	5.2	18.2	21.3
(iii) Loans from Banks & Financial Institutions*	2.0	3.4	6.6	6.8
2. Loans and Advances from the Centre	57.4	46.6	29.1	26.3
3. Public Account Liabilities	26.9	30.1	24.5	23.3
of which:				
(i) State Small Savings & Provident Funds	13.2	15.9	13.3	12.9
(ii) Reserve Funds	3.7	3.9	4.2	4.3
(iii) Deposits and Advances	10.0	10.3	7.0	6.1
4. Contingency Fund	0.8	0.3	0.0	0.0

Advances). Small savings transfer earlier formed part of loans from the Centre and since 1999-2000, with the formation of NSSF, these flows are treated separately and classified as part of internal debt of the State Governments. Table XXII sets out information on major components of outstanding liabilities of the State Governments.

Chart 24: Composition of Outstanding Liabilities

The composition of outstanding liabilities of the State Governments shows a sharp decline in the share of loans from the Centre with an upsurge in the shares of loans from NSSF, market loans and loans from banks and other financial institutions. Significantly, reserve funds and deposits and advances have constituted over 10 per cent in the last few years (Chart 24).

VI.B.(iii) Market Borrowings

As of end-March 1991, total internal debt constituted only 15.0 per cent of the outstanding liabilities of the State Governments with the proportion moving up sharply in recent years particularly since end-March 2000 (with change in classification of small savings and setting up of NSSF in 1999-2000) and reached the high level of 50.4 per cent at end-March 2005. Market borrowings of the State Governments constitute an important component of internal debt of the States.

The State Governments issue dated securities of varying tenors that have extended up to 12/13 years. Broadly, the banks and financial institutions subscribe to these securities floated through a process managed by the Reserve Bank. In the backdrop of a prevalent benign interest regime in recent

years, market borrowings have emerged as the cheapest source of raising funds for the State Governments with the weighted average rate of interest declining from 14.0 per cent in 1995-96 to a low of 6.13 per cent in 2003-04. However, the interest rate has firmed up to about 7.5 per cent in September 2005. Table XXIII sets out data on interest rate profile of Outstanding State Government Securities as at end-March 2005.

The share of market borrowings in total liabilities of the States has moved up from 12.2 per cent as at end-March 1991 to 20.5 per cent as at end-March 2005. The maturity profile of the market loans are largely bunched for repayment between 5 to 10 years (Table XXIV).

The annual schedule for repayment of State market loans is provided in Chart 25.

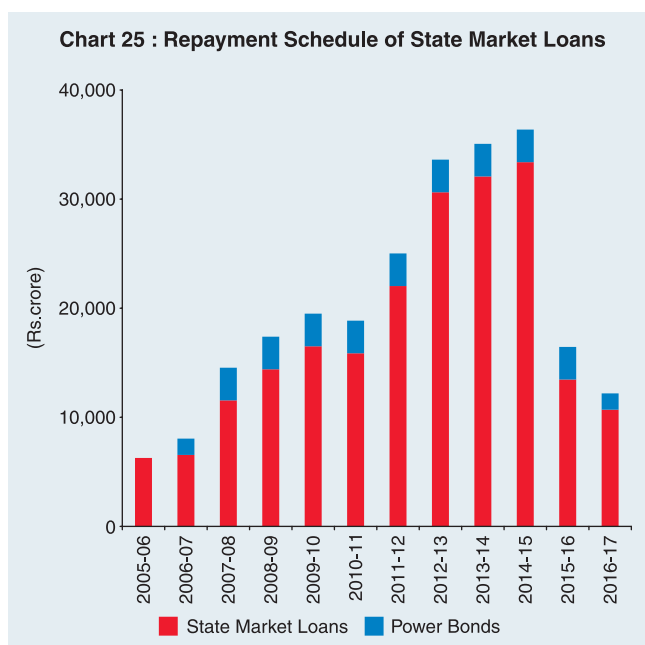
Table XXIV: Maturity Profile of State Government Securities (Outstanding as on March 31, 2005)

(percentage)			
States/Period (Years)	0-5	5-10	>10
1	2	3	4
Andhra Pradesh	30.01	64.59	5.40
Arunachal Pradesh	14.17	57.20	28.63
Assam	29.21	60.54	10.26
Bihar	26.83	59.46	13.71
Chattisgarh	26.59	55.99	17.43
Goa	25.57	60.78	13.64
Gujarat	20.69	66.99	12.32
Himachal Pradesh	15.36	72.65	11.99
Haryana	24.01	64.39	11.61
Jammu & Kashmir	19.21	68.65	12.13
Jharkhand	28.71	63.50	7.79
Karnataka	23.96	66.86	9.18
Kerala	29.89	62.27	7.84
Maharashtra	19.11	60.30	20.58
Madhya Pradesh	27.43	66.36	6.21
Manipur	25.37	54.38	20.25
Meghalaya	31.29	50.18	18.53
Mizoram	22.86	56.17	20.97
Nagaland	30.48	58.63	10.88
Orissa	31.88	57.07	11.05
Punjab	23.73	64.91	11.36
Rajasthan	28.77	63.00	8.23
Sikkim	46.63	32.21	21.16
Tamil Nadu	24.23	68.69	7.08
Tripura	25.09	47.17	27.74
Uttaranchal	13.63	68.85	17.52
Uttar Pradesh	33.43	57.11	9.46
West Bengal	19.26	63.65	17.09
All States	25.90	62.78	11.32

Source : Reserve Bank records.

Table XXIII: Interest Rate Profile of Outstanding State Government Securities (end-March 2005)

(percentage)			
Sr. No.	Range of Interest Rate (per cent)	Outstanding Amount (Rupees crore)	Percentage to Total
1	2	3	4
1.	5.00-5.99	34,612	16.22
2.	6.00-6.99	58,563	27.44
3.	7.00-7.99	27,872	13.06
4.	8.00-8.99	8,004	3.75
5.	9.00-9.99	5,412	2.54
6.	10.00-10.99	14,563	6.82
7.	11.00-11.99	17,062	7.99
8.	12.00-12.99	25,362	11.88
9.	13.00-13.99	15,720	7.37
10.	14.00	6,274	2.94
	Total	2,13,443	100



VI.B.(iv) Special Securities Issued to NSSF (Small Savings)

As mentioned earlier, with the setting up of the NSSF in 1999-2000, this source of borrowings has become part of the internal debt of the State Governments. This component of State borrowings is exogenously determined over which the Centre has no control. Over the years this source has emerged as the most important source of borrowings by the State Governments with its share in total debt rising from 5.2 per cent as at end - March 2000 to 21.3 per cent as at end - March 2005.

VI.B.(v) Loans from Banks and Financial Institutions

The borrowing requirements of the State Governments has made the State Governments raise loans from a host of financial institutions, *inter alia*, LIC, GIC, NABARD, NCDC, HUDCO and REC. The interest rates and other terms and conditions on such loans are negotiated between State Governments and the lending institutions which depend upon a host of factors. The detailed data/information relating to these loans are not transparently provided in the Budgets of the State Governments. Loans from banks and financial institutions is slowly emerging as an important source

of borrowings with its share in outstanding liabilities of the State Governments rising from 2.0 per cent as at end-March 1991 to 6.8 per cent as at end-March 2005.

VI.B.(vi) Loans from the Centre

Hitherto, 'Loans from the Centre' to the State Governments were broadly classified into Plan Loans, non-Plan Loans, Loans for Special Schemes and WMA from the Centre. Plan Loans were allocated under State Plan Schemes, Central Plan Schemes and Centrally Sponsored Schemes. The non-Plan Loans covered Loans against small savings, relief for natural calamities, *etc.* Three important developments, viz., i) institution of NSSF effective April 1, 1999, ii) introduction of DSS for the period 2002-03 to 2004-05 and iii) discontinuation of Plan loans since April 1, 2005 in accordance with the TFC have significantly reduced the importance of loans from the Centre as a financing item of the GFD (Statement 24).

Historically, loans from the Centre have been the most important source of borrowings accounting for 57.4 per cent of the borrowings of the State Governments as of end-March 1991. With changes in accounting norms in respect of small savings since 1999-2000 and repayment of loans to the Centre under DSS, the share of this source reached 26.3 per cent at end-March 2005. State-wise information on DSS is presented in Statement 32. As discussed in the Section I, the TFC has recommended debt relief for the State Governments linking them to certain pre-conditions, with regard to their loans from the Centre contracted up to end-March 2004 and outstanding as of end-March 2005.

VI.B.(vii) Public Account Liabilities

Public account liabilities are those where the State Governments act as a banker accepting deposits and funds and pay interests thereon. These liabilities are unfunded implying huge risks on the budgets of the States. The small saving schemes run by the States themselves and provident fund receipts form the major component of public account liabilities, which accounted for 12.9 per cent of the outstanding liabilities of the State Governments as of end-March

2005. The receipts and interest rates under State Provident Funds are guided by General Provident Fund rules (GPF), wherein there is a minimum contribution from employees (6 per cent of basic salary) and without any ceiling. Thus, the cost of borrowings and the receipts from State Provident Funds like that of NSSF are exogenous elements, which can increase autonomously. Deposits and Advances form the other important constituent of public account, whose share in total liabilities has been over 10.0 per cent but declined in recent years to 6.1 per cent as of end March 2005. The share of Reserve Funds, however, moved up from 3.7 per cent to 4.3 per cent during the same period.

VI.B.(viii) Contingency Fund

Under Contingency Fund, transactions connected with Contingency Fund established under Article 267¹⁵ of the Constitution of India are recorded. Its proportion in the total outstanding liabilities has been less than 1 per cent.

VI.C State-wise Position of Debt

The detailed annual State-wise component-wise break-ups of outstanding liabilities from 1990-91 to 2005-06 (BE) is provided in Statements 26-28. It may be mentioned that the outstanding liabilities as at end-March 2000 of the 3 bifurcated States (Bihar, Madhya Pradesh and Uttar Pradesh) have been apportioned

Table: XXV Summary Position of Debt of States

INDICATOR	Quartile 1 (Q1)	Quartile 2 (Q2)	Quartile 3 (Q3)	Quartile 4 (Q4)
(A) Non-Special Category States 2001-04 (Average)				
1. DEBT/GSDP	RANGE: 16.5 to 29.8 Delhi, Tamil Nadu, Haryana, Karnataka	RANGE: 30.3 to 35.0 Chhattisgarh, Maharashtra Andhra Pradesh, Madhya Pradesh, Jharkhand	RANGE: 38.6 to 51.0 Gujarat , Kerala, Goa, West Bengal, Rajasthan	RANGE: 54.1 to 73.3 Uttar Pradesh, Punjab, Bihar, Orissa
2. IP/RR	RANGE: 13.0 to 16.6 Jharkhand, Chhattisgarh, Goa, Delhi	RANGE: 18.6 to 22.8 Karnataka, Tamil Nadu, Madhya Pradesh, Haryana, Maharashtra	RANGE: 24.4 to 29.8 Andhra Pradesh , Bihar, Kerala, Gujarat, Uttar Pradesh	RANGE: 31.9 to 50.7 Rajasthan, Punjab, Orissa, West Bengal
(A) Non-Special Category States 2004-05 (RE)				
1. DEBT/GSDP	RANGE: 17.7 to 31.0 Delhi, Karnataka, Tamil Nadu, Haryana	RANGE: 32.3 to 36.6 Goa, Andhra Pradesh, Maharashtra, Chhattisgarh, Jharkhand	RANGE: 41.1 to 54.4 Kerala, Madhya Pradesh West Bengal, Gujarat, Punjab	RANGE: 54.7 to 77.3 Uttar Pradesh, Rajasthan, Bihar, Orissa
2. IP/RR	RANGE: 10.6 to 17.1 Jharkhand, Chhattisgarh, Karnataka, Madhya Pradesh	RANGE: 17.7 to 20.7 Goa, Tamil Nadu, Haryana, Delhi, Maharashtra	RANGE: 21.8 to 28.3 Bihar , Andhra Pradesh, Punjab, Kerala, Uttar Pradesh	RANGE: 29.4 to 48.3 Orissa, Rajasthan Gujarat, West Bengal
(B) Special Category States 2001-04 (Average)				
1. DEBT/GSDP	RANGE: 32.6 to 42.9 Assam, Meghalaya, Arunachal Pradesh	RANGE: 43.2 to 45.5 Uttaranchal, Tripura	RANGE: 51.0 to 58.1 Nagaland , Manipur, Jammu and Kashmir	RANGE: 79.7 to 80.5 Sikkim, Mizoram, Himachal Pradesh
2. IP/RR	RANGE: 5.3 to 11.8 Sikkim, Arunachal Pradesh, Meghalaya	RANGE: 13.4 to 14.0 Nagaland, Mizoram	RANGE: 14.8 to 16.9 Tripura , Jammu and Kashmir, Manipur	RANGE: 17.4 to 32.3 Uttaranchal, Assam, Himachal Pradesh
(B) Special Category States 2004-05 (RE)				
1. DEBT/GSDP	RANGE: 33.8 to 41.6 Tripura, Assam, Nagaland	RANGE: 42.2 to 45.1 Jammu & Kashmir Meghalaya	RANGE: 50.2 to 55.3 Arunachal Pradesh , Uttaranchal, Manipur	RANGE: 62.8 to 82.6 Sikkim, Himachal Pradesh, Mizoram
2. IP/RR	RANGE: 4.8 to 11.3 Sikkim, Arunachal Pradesh, Meghalaya	RANGE: 12.0 to 12.6 Jammu and Kashmir, Mizoram	RANGE: 13.5 to 14.5 Assam , Manipur, Tripura	RANGE: 14.9 to 34.7 Nagaland, Uttaranchal, Himachal Pradesh

Note :Figures in bold pertain to median States for the given indicator.

¹⁵ Article 267 (2) states that 'The Legislature of a State may by law establish a Contingency Fund in the nature of an imprest to be entitled "the Contingency Fund of the State" into which shall be paid from time to time such sums as may be determined by such law, and the said Fund shall be placed at the disposal of the Governor of the State to enable advances to be made by him out of such Fund for the purposes of meeting unforeseen expenditure pending authorisation of such expenditure by the Legislature of the State by law under Article 205 or Article 206.'

to the 3 newly formed States (Jharkhand, Chhattisgarh and Uttaranchal) respectively on the basis of their respective population proportions.

The position of States with regard to debt indicators is varied. The debt position of the States is provided in Table XVI A & B of Section III. Based on the quartile ranking of each State, the summary position regarding debt has been provided in Table XXV.

State-wise analysis indicates that many of the States had high level of outstanding liabilities as at end-March 2005. Mizoram had the highest Debt-GSDP ratio of 82.6 per cent followed by Bihar (77.3 per cent), Himachal Pradesh (73.7 per cent), Sikkim (62.8 per cent), Orissa (62.5 per cent) and Rajasthan (56.8 per cent).

Among non-special category States while Tamil Nadu, Karnataka and Haryana continue to be in a relatively better position on debt during 2001-2004 and 2004-05 (RE), States like Uttar Pradesh, Bihar and Orissa persisted to have high levels of debt. Jharkhand and Chhattisgarh were continuously the better States in terms of interest burden (IP/RR) while Rajasthan, Orissa and West Bengal were the persistently worse-off States in this regard (Charts 26 A & B).

Among special category States Assam remained at a better off position with relatively low levels of debt while Sikkim, Mizoram and Himachal Pradesh persisted with high debt position. With regard to interest burden Sikkim, Arunachal Pradesh and Meghalaya continued to be the better States, while Uttaranchal and Himachal Pradesh were the

Chart 26 : Quartile Position of Non Special Category States - Outstanding Liabilities

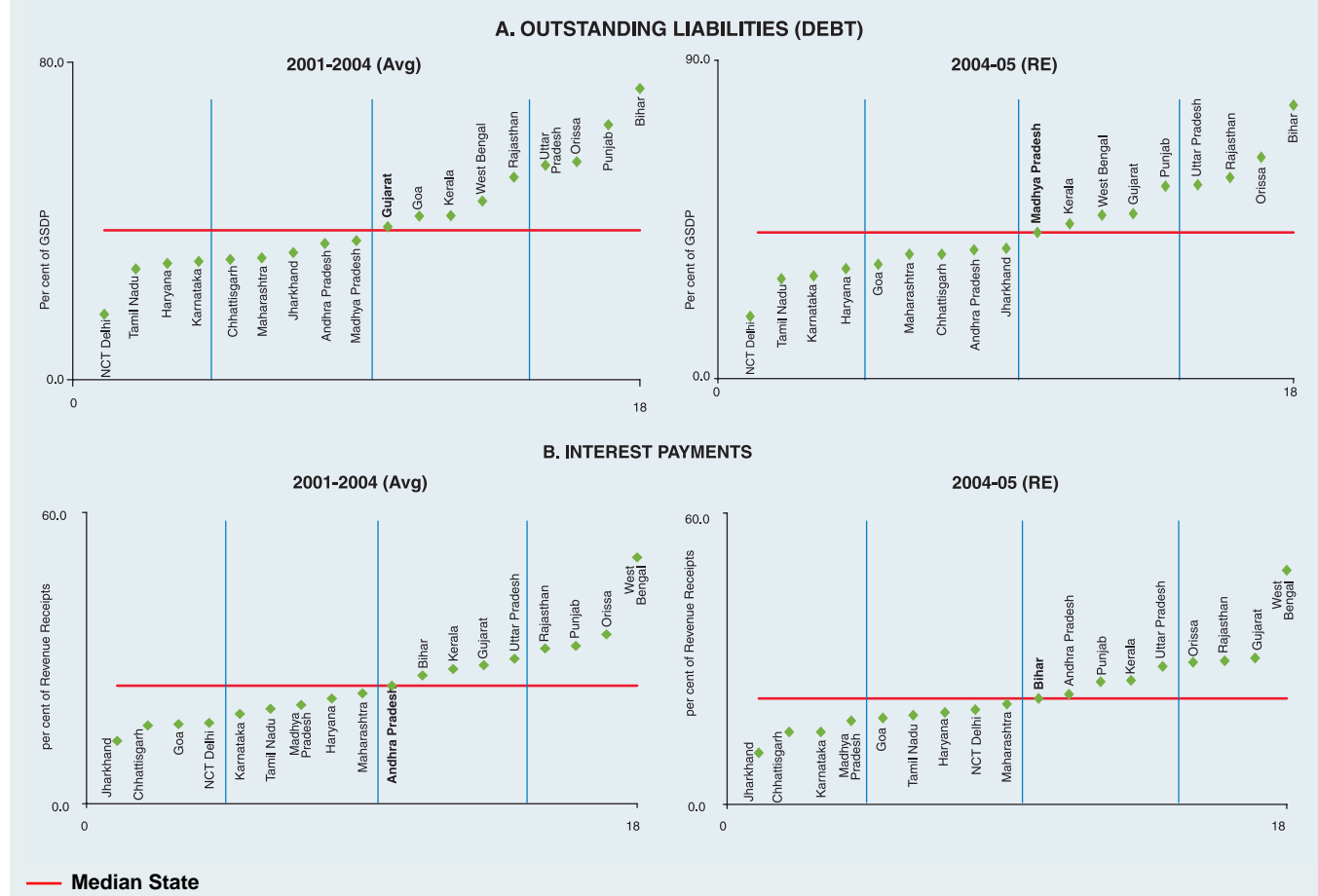
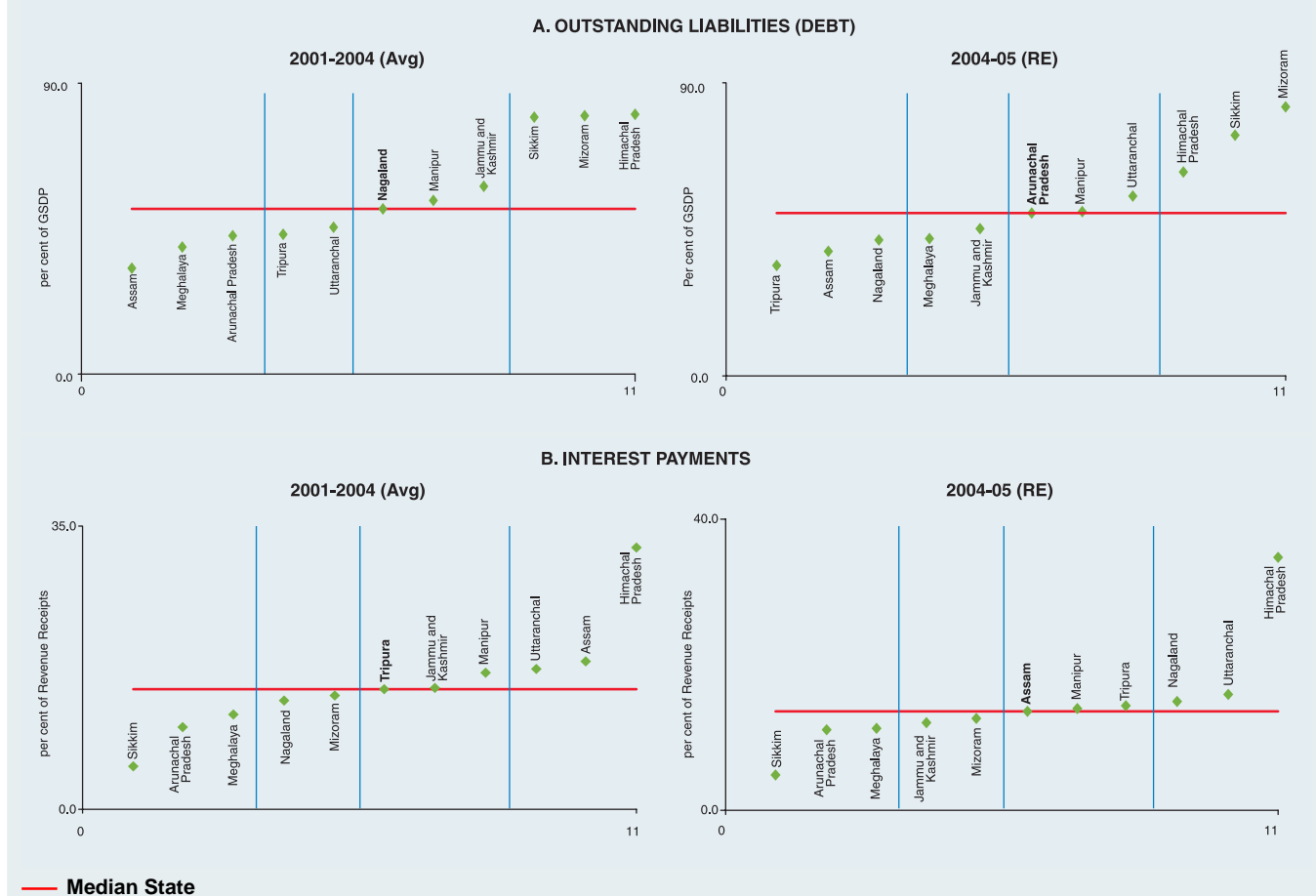


Chart 27 : Quartile Position of Special Category States - Outstanding Liabilities

persistently worst States (Charts 27 A & B).

The States are substantially varied in their debt burden as well as on their servicing. Addressing the debt problem of States would require a proper estimation of their debt levels which has been a new aspect of this Study.

VII. CONCLUDING OBSERVATIONS

The fiscal position of the State Governments during 2005-06 would to a large extent, be shaped by the recommendations of the TFC, implementation of VAT by majority of States and progressive enactment of FRL by the State Governments. The budget estimates of 2005-06 indicate the strong commitments of State Governments to carry on the fiscal correction and consolidation process. There are some important issues, which need to be addressed by the State

Governments in the milieu of fiscal correction and consolidation. The process of fiscal correction should be durable and sustainable. As recommended by TFC, the State Governments may consider to follow a holistic approach to fiscal restructuring, emphasising revenue augmentation, compression and rationalisation of expenditure and containment of debt at sustainable levels. In this connection, progressive enactment of FRL by the State Governments would provide the statutory framework for augmenting fiscal discipline and to carry out fiscal correction in a realistic time-bound manner.

Several weaknesses have persisted in State finances over the years and are manifested in sluggish non-tax revenue, downwardly rigid non-developmental expenditure and low allocation in respect of social sectors such as health and

education. It may be mentioned that the State Governments have a major responsibility as regards provisions in respect of social sectors such as education and health and economic infrastructure such as roads, waterworks and power. In order to make the process of fiscal consolidation durable and sustainable it is important to recognise that adequate investment in economic infrastructure and spending on social services are essential. With the State Governments facing resource gaps, a desirable path to fiscal correction lies through fiscal empowerment *i.e.*, by expanding the scope and size of revenue flows into the budgets. In this context, augmenting resource mobilisation from non-tax revenue through appropriate user charges, cost recovery from social and economic services and restructuring of State PSUs assume importance.

The State Governments may consider a prudent public expenditure strategy by arresting the rising share of non-plan non-developmental expenditure. The State

Governments have been making efforts to restrict the share of non-developmental committed expenditure by opting for DSS and introducing new pension scheme based on defined contributions. A closer examination to arrest unproductive expenditure and rationalisation of subsidies may be useful.

With regard to financing of deficit, the State Governments have the options to be guided by their requirements and creditworthiness to tap different sources of funding *viz.*, market borrowings, securities issued to NSSF and others. In order to be able to borrow from the market in an environment of market discipline, it is essential that the State Governments attempt to improve the financial position. In this context, it may be emphasised that the strategy of imposing fiscal discipline as recommended by TFC as well as the statutory frameworks of FRLs enacted by several States would lay the foundation for the process of fiscal correction and consolidation in the medium term.

Annex 1: Major Policy Initiatives of State Budget 2005-06

State	Fiscal	Institutional	Sectoral
1. Andhra Pradesh	<ul style="list-style-type: none"> Steps will be taken to strengthen institutional measures against corruption to prevent leakage from revenue resources side and expenditure side. Introduce a contributory pension scheme. Fifty thousand new pensions will be additionally sanctioned during 2005-06 for the disabled persons. The pension amount will be increased from Rs.75 per month to Rs.100 from the year 2005-06. 	<ul style="list-style-type: none"> The Assembly Constituency Development Programme will be revived and an amount of Rs.50 lakhs is allocated for the purpose to each Assembly constituency. 	<ul style="list-style-type: none"> Infrastructure relating to revenue earning departments will be further strengthened. Introduced a new scheme A.P. Small Scale Industries Revival scheme to address the problems of small scale industries sector. The A.P. Urban Reforms and Municipal Services Project will be taken up with World Bank assistance in order to finance the infrastructure needs like roads, drains, water supply, street lighting and solid waste management etc. in the urban areas. The Hussain Sagar Lake would be restored with the assistance from Japan Bank for International Co-operation.
2. Arunachal Pradesh	<ul style="list-style-type: none"> MLA Local Area Development Fund has been enhanced. 	<ul style="list-style-type: none"> From April 1, 2005, 50% dearness allowance will be merged with basic pay for State Government employees. 	
3. Assam	<ul style="list-style-type: none"> Levy of entry tax on mekhela-chadors coming from outside the State. Set up a Tax Reform Commission A Bill for liquidation of arrear dues to be placed. The arrears pertain to demanded tax, penalty and interest with rebate in interest and waiver in penalty. Set up a Cell in Assam Administrative College to advise Government on tax-policy impact. Entry tax on crude oil reduced from 4 per cent to 2 per cent on all refineries. 	<ul style="list-style-type: none"> Adopted a Roads Maintenance Policy. Constituted a Standing Committee on employment generation. Setting up of Autonomous Councils and elections to Bodoland Territorial Council have been planned. Introduced the District Development Plan in the State similar to the national programme of Rashtriya Sama Vikash Yojana, Reserved 30 per cent of the vacancies in the State Government for women. 	<ul style="list-style-type: none"> Introduce a new scheme named "Anandram Barooah Award" for students who pass Class X Board examination in first division. New incentive schemes for students in the age groups of 3 to 6 years and 6 to 10 years. Establish a University in Guwahati and introduce several courses in other institutions. Set up 3 new medical colleges across Assam. Propose to create new Development Authorities for urban areas surrounding Guwahati to ensure planned and proper development of these areas.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> • Raised excise duties and fees relating to liquor trade and also introduce other fees. • Enhance Motor Vehicles Tax lease by imposing additional tax. • Introduction of Profile Registration Fee, Registration of Mono Cartoons and excise duty on BIO products. 	<ul style="list-style-type: none"> • Raise 2 new India Reserve Battalions. • Modern Municipal Law in line with those in other parts of the country to strengthen the urban local bodies to be enacted. • A new scheme Mukhya Mantrir Jeevanjyoti Veema Achani from this financial year to provide for health and accident risk insurance coverage to the entire population to be launched. 	
4. Bihar	<i>Vote-on-account</i> budget placed in the Parliament		
5. Chhattisgarh	<ul style="list-style-type: none"> • Recruitment of 22,000 teaching staff. • Wages and salary expenses are to be restricted to 32 per cent of revenue receipts. • Contributory Pension Scheme has been implemented from November 1, 2004 to contain establishment expenses. • Bill is proposed to be introduced to amend Indian Stamp Act, 1899 to mobilise additional resources. 	<ul style="list-style-type: none"> • Radical reform in Public Distribution System (PDS) is proposed by involving varied agencies such as private parties, co-operative societies, village panchayats, Women Self-Help Group, etc. • Constitution of 'Food Security Fund' to ensure the availability of essential goods to malnourished and famine affected people living at far off places. • Introduce E-Tendering in all construction relating Departments to have transparency in Governance. 	<ul style="list-style-type: none"> • Greater emphasis on Human Resource Development is proposed under which, setting up of Model Schools, making Mid-day Meal Scheme more attractive, implementation of Below Poverty Line (BPL) Scholarship and BPL Book Bank Scheme, starting E-Class Room and Vocational Education in select colleges, setting up Youth Hostels, development and strengthening of Health related infrastructures, Special facilities for the spread of education among SC/ST, etc. are proposed. • Constitution of Bio-Fuel Development Authority to encourage an alternative source of power.
6. Goa			<ul style="list-style-type: none"> • Build a Convention Centre to boost the tourism sector which has been approved by the Planning Commission. • Upgrade medical facilities in Goa Medical College and add super-specialities. • Set up a state-of-the-art Institute of Hotel Management with private sector participation.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
			<ul style="list-style-type: none"> Set up a expressway from Mormugao port.
7. Gujarat	<ul style="list-style-type: none"> Reduction in electricity charges across large sections of consumers. 	<ul style="list-style-type: none"> Establish "Patients Welfare Committees". State Government has declared 'Urban Development Year 2005' identifying certain key areas such as sanitation, drinking water, sewerage management, etc. Create a 'Gujarat Urban Infrastructure Fund'. 	<ul style="list-style-type: none"> Pragatipath Yojana under which nine long distance high speed corridors will be prepared. Vikaspeth Yojana will improve State highways in a modern way. Kisanpath Yojana will be introduced for development and modernisation of roads.
8. Haryana	<ul style="list-style-type: none"> Various incentive based schemes to be introduced for gender sensitisation, financial assistance for birth to second girl child, pension for families with only girl child. 	<ul style="list-style-type: none"> Constituted a Committee to address the sensitive issue of pending power dues from farmers. Will set up an Overseas Employment Bureau and constitute an Empowered Committee to take decisions about providing information and assistance in the matter of overseas placements. A Committee under Chief Minister constituted to mobilise additional resources. Announced a New Industrial Policy, 2005 with the basic objectives to provide balanced industrial growth with special emphasis to backward areas, creating quality infrastructure, generating new employment opportunities and providing investor friendly environment. Launched a new scheme Rajiv Gandhi Scholarship for Excellence in Education to reward brilliant students in Government schools. A High Powered Committee set up to find ways and means to promote sports and to improve the skills of the sportspersons of the State. 	<ul style="list-style-type: none"> Construct Kundli-Manesar - Palwal Expressway on BOT basis. Set up a Government College for Women. Set up a Women Cooperative Development Bank exclusively to be managed and run by women. Set up a Special Economic Zone in Gurgaon to boost exports. Set up Central Institute of Plastic and Engineering Technology in collaboration with Govt. of India.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
9. Himachal Pradesh	<ul style="list-style-type: none"> Proposal to assign the royalty on minor minerals and collection of fees on minor forest produce to the <i>Gram Panchayats</i> for improving their resource base. Increase in electricity duty for all categories of consumers and additional duty for extremely power intensive industries. Special road tax to be raised. Rationalisation in the water rates for irrigation. Rationalisation of rates of urban water supply and private connections in rural water supply. Levy of sewerage fees linked to water bills and one time connection fees. Imposition of Profession Tax covering all salaried employees. Imposition of "Certain Goods Carried by Road Tax" on packaged drinking water and pharmaceuticals products. 	<ul style="list-style-type: none"> Frame a Technical Education Policy for private sector participation and investment. Set up a series of partnerships under a plan called 'Partnership HP' to undertake a series of infrastructural projects. The list includes several expressways, IT Park, Special Development Zone, Special Economic Zone, educational institutes, etc. The Government would announce its own Hydro Power Policy. Suitable amendments to the H.P. <i>Panchayati Raj</i> Act to increase effectiveness of the panchayats. The Third State Finance Commission is to be constituted which will go into the question of strengthening the resource base of PRIs. Set up a Core Group under the Chief Secretary to look into the issues of host schemes with identical outputs, subsidies and norms for social services, administrative infrastructure and decentralisation. Set up a Public Tariff Commission for various services like transport, education, health, water, irrigation, etc. 	<ul style="list-style-type: none"> Open 3 new colleges besides 200 middle schools. Several new housing colonies to be built and satellite townships proposed.
10. Jammu & Kashmir	<ul style="list-style-type: none"> Propose an amnesty scheme from interest and penalty blended with self assessment for all categories of dealers registered with Dept. of Sales Tax for the accounting years 1999-00 to 2004-05. 	<ul style="list-style-type: none"> A Reconstruction Plan presented by the Chief Minister to address specific socio-economic problems arising out of militancy. 	<ul style="list-style-type: none"> ADB's J&K Multisector Infrastructure Rehabilitation project would focus on roads and bridges.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Area-wise valuation of real estate as would comprise the minimum benchmark value for registration and payment of Stamp Duty. To extend tax holiday for hotels, restaurants and like arrangements of lodge for the tourists. Improve recoveries in the power sector by going for a well planned and sustained enforcement drive of recoveries – past and present. Increase water and irrigation rates to bring it in line with expenditures over the next 3 years. Create an institution along the lines of an Asset Reconstruction Company at the State level with participation from the Union Government for taking over the infected assets of the private and public sector. 	<ul style="list-style-type: none"> Put in place an institutional arrangement, Economic Reconstruction Agency, which will be implementing agency for all externally aided projects. Set up a Special Group under the Economic Advisor to work out the modalities of administrative responsibilities and framing of rules that govern borrowings of municipalities and other local bodies. 	<ul style="list-style-type: none"> Japanese Bank of Industrial Cooperation is likely to finance a complete overhaul of the drainage and sewerage system for greater Srinagar and Jammu. Earmarking funds for identified 900 schemes that have been on the works for some time and require Rs.50 lakh or less for completion. A project is being formulated for getting external funding to finance the spill over cost of buildings of health sector. Work on Srinagar-Leh transmission line, which will help ensure grid connectivity to the districts of Kargil and Leh, will be started. A major programme for development of model villages will be launched. An Integrated Development Project for the two capital cities of Jammu and Srinagar is being prepared.
11. Jharkhand	<ul style="list-style-type: none"> Computerisation of registration offices, transport department, commercial tax department and treasuries will be completed. Defined Contributory Pension Scheme for those who have joined services after December 2004 has been implemented. Action will be taken on the enactment of FRL after due consideration of all aspects relating to fiscal. 	<ul style="list-style-type: none"> Jharkhand Agency for Promotion of Information Technology (JAP-IT) has been set-up to execute E-governance and also for other schemes relating to information technology. 	<ul style="list-style-type: none"> Education for women up to post graduation level will be free. Proposal for setting-up Dairy Technology College, Cattle and Fish Research Institute and Agro-Export Zone.
12. Karnataka	<ul style="list-style-type: none"> Waive off interest and penal interest on cooperative loans availed by farmers from Cooperative banks. 	<ul style="list-style-type: none"> Set up a Fiscal Policy and Analysis Cell with the objective of tax analysis, revenue forecasting, expenditure review, project appraisal and debt management. 	<ul style="list-style-type: none"> Open 6 new medical colleges in six cities. Open 114 new high schools in backward taluks. Open 2 degree colleges.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> No registration charges for availing agricultural loans. Introduce an insurance scheme viz.; 'Karnataka Janashree Vima Yojana' for sheep and shepherds. Levy a toll for some roads under Karnataka State Highways Act to take up their improvement. Free power upto a limit to certain category of customers. Also under Dalit Basti Scheme provide free power to large number of households. Tax amnesty scheme 'Karasamadhana Scheme' as a last chance for those who would like to clear their arrears. Levy a Special Entry Tax for certain items and also on items for which neighbouring States may not implement VAT. 	<ul style="list-style-type: none"> Establish 'Karnataka School Quality Assessment Organisation' to ensure quality in primary schools. Provide Rs.50 lakh to undertake development works in the constituency of each member of the Karnataka Assembly. Set up Karnataka State Industrial Development Council under the Chairmanship of the Chief Minister to facilitate accelerated industrial development of all regions and sectors. 'Kaigarika Vikasa' scheme would be launched for intensive industrialization of 39 most backward taluks. Introduce a 'Purchase-Provider' model between Government and ESCOMS in power sector. 'Karnataka Sustainable Forest management and Bio-Diversity Conservation Project' will be undertaken with financial assistance from Japan Bank for International Cooperation. 	<ul style="list-style-type: none"> Initiate a new programme 'Kugrama-Sugrama' for integrated development targeted towards most backward villages. A new scheme 'Namma Hola – Namma Tota' for labourers to undertake cultivation of garden crops. 'Kaushalya' scheme for training unemployed women will be implemented to cover scheduled caste, scheduled tribe and backward class women. Establish 'Kuvempu Samskrithika Kendra' to support translation of works of Rastra Kavi Kuvempu and other eminent writers. New scheme of 'Suvarna Karnataka – Pravasi Thana' under which at 50 locations basic wayside facilities would be provided. Product specific Special Economic Zones for textiles and IT, 11 Science & Technology Parks and 4 Clusters across the State would be set up. Develop a High-Tech city near Hosur - Sarjapur.
13. Kerala	<ul style="list-style-type: none"> Prudential Financial Management scheme to ensure that the amount cleared by the Government will be paid by the treasuries without delay. Open several new sub treasuries for the accessibility of rural people and pensioners. Increase the amount for Regional development Fund Scheme for MLAs. 	<ul style="list-style-type: none"> A Milk Products Manufacturing Centre to be set up. Launch a crop insurance scheme for agricultural products and a Risk Fund Scheme to write off debt liabilities of farmers who die during the repayment period. Constitute a Consumer Welfare Fund to utilise the fund from Central Government's Consumer Welfare Fund. 	<ul style="list-style-type: none"> New innovative scheme "Nagarathil Oru Nattinpuram" will be launched for promotion of agriculture in urban households. Pashugramam scheme will be implemented in 15 Grama Panchayats. New Scheme "Habitat Forestry" to promote planting of trees in private land.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Levy of Luxury Tax on rent received by certain premises such as hotels, clubs, etc. Stamp Duty (8.5%) and surcharge (5%) raised to pre-December 2003 rates. 	<ul style="list-style-type: none"> 'Suraksha' and 'Karunaya' housing schemes proposed for the economically backward homeless people. New Programme 'Sutharya Keralam' for redressal of public grievances. Kerala Sustainable Urban Development Project with assistance from ADB is being designed to provide financial and technical assistance to 5 Municipal Corporations to expand urban infrastructure, implement poverty alleviation measures and improve governance. 	<ul style="list-style-type: none"> Development of a Deepwater International Container Trans-shipment Terminal at Vizhinjam. KSEB proposes to commission several sub-stations of varying capacities in order to improve the voltage profile and reliability of the transmission and distribution networks.
14. Madhya Pradesh	<ul style="list-style-type: none"> Computerisation of Treasury system to execute effectively fiscal discipline. Deposit of revenue receipts in treasuries through E-banking facility will be introduced and accordingly cyber-treasury facility will be made available. All registry offices are being computerised and they will also be interconnected to contain fraudulent activities and help in raising additional resources. Decision has been made to implement Defined Contributory Pension Scheme for those who have joined services after January 1, 2005. Decision has been made to set-up Guarantee Redemption Fund (GRF) to avoid default in honouring guaranteed loans, if guarantee is invoked. Receipts of guarantee fee by the Government would be deposited every year in this Fund. 		<ul style="list-style-type: none"> Setting up of Madhya Pradesh Road Development Corporation to accelerate road development work. Financial assistance from ADB is also proposed to be sought in this regard.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
15. Maharashtra	<ul style="list-style-type: none"> Will declare a tax holiday of stamp duty for housing loan upto a certain amount as well as reduction for a higher amount level. Tax holiday of stamp duty on all educational loan documents executed by students for pursuing studies within the country. Endeavour to introduce VAT based stamp duty system for two stages <i>i.e.</i> Development Agreements and Conveyance related to property development. Create 3 separate funds to manage servicing of off-budget debts, distressed assets, and future guarantees on behalf of the Government of Maharashtra. Each Fund will have a Lead Institution as a Fund Manager. An amnesty scheme for tax on motor trailers used for agriculture under which the entire interest arrears will be waived if the pending taxes are paid in full by end June 2005. Introduce a system of monthly cash flows for Departments to make the process of withdrawing funds from Treasury for approved expenditures automatic. Form an Unorganised Workers Authority Fund. A State level Authority for unorganised workers would help in solving their problems. 	<ul style="list-style-type: none"> Set up a Trust to manage the liabilities of the State Government to financial institutions and non-Governmental entities. Committee constituted under the Finance Minister for reviewing the release of funds and expenditure incurred out of the outlays made available for removal of backlogs. Referral Centres are being established at the Divisional Head Quarters to provide super speciality services. Valmiki Ambedkar Awas Yojana announced with a view to upgrade the living standard of slum dwellers in urban areas, who are below the poverty line and members of the economically weaker sections of society. Set up a Consultative Committee of Trade and Industry to deliberate on operational problems and issues regarding VAT and recommend appropriate solutions. Set up a system known as Computerised Stamp Duty Administration System through a computer-based network which will authorise designated banks and financial institutions to sell stamps and provide information. 	<ul style="list-style-type: none"> Initiate steps to revitalise the Maharashtra State Road Transport Corporation to make it financially viable. Restructuring of Maharashtra State Electricity Board into a holding company, a generation company, a transmission company and a distribution company. Ambitious scheme to provide constructed houses to population below poverty line. Under this scheme, those deprived of the benefits of Indira Awas Yojana would get financial assistance in rural areas. Establish zoo, safari park and eco tourism project of international standards near Nagpur to promote tourism and appoint international standard consultants. The Maharashtra Industrial Development Corporation will establish garment parks on the leased lands of Maharashtra State Textile Corporation at several places.
16. Manipur	No new initiatives enumerated in the Budget 2005-06 of Manipur.		
17. Meghalaya	<ul style="list-style-type: none"> Imposition of limited water user charges on water available for irrigation. 		<ul style="list-style-type: none"> A new Shillong Township Project has been planned to decongest Shillong urban agglomerate.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
18. Mizoram	<ul style="list-style-type: none"> Steps for introduction of Entry Tax, Luxury Tax on hotels and lodging houses and other luxury houses. 		<ul style="list-style-type: none"> To promote organic farming, purchase of 120 tonnes of organic manures, bio-fertilisers and soil amendments for distribution to farmers at 50 per cent subsidy. Set up a Bamboo Technology Park and several CFC for handloom and handicrafts. Implement urban water supply schemes in certain towns under Accelerated Urban Water Supply Programme. Develop permanent exhibition infrastructure with Govt. of India funding. Construct a cancer hospital and nursing college. Proposed to construct 3 important new roads linking important points in the State with financial assistance from NABARD. Several new tourism sector projects will be taken up at various places. Proposal for new ITI at Champai and Women ITI at Aizwal. Proposal to build a State Museum, Cultural Complex, District Library buildings and State Library building.
19. Nagaland	<ul style="list-style-type: none"> Set up a Special Purpose Vehicle to borrow funds to meet critical infrastructure requirements and productive plan schemes. Set up an Independent Pricing Tribunal and Regulatory Authority for the State for rendering justice in determining the due rates of costs/prices of goods and services delivered to the people. 	<ul style="list-style-type: none"> Propose to bring in measures to improve the enforcement of prohibition by communitisation and authorising the local bodies to enforce the law and the rules. 'The State Sports Policy' will be adopted by the State Government and also the 'The Nagaland Youth Policy'. 	<ul style="list-style-type: none"> Adopt the principle of contract farming to enable farmers to produce more with assured market and minimum assured price. Govt. of India to set up a Central Institute of Horticulture. Self employment opportunities will be provided to unemployed veterinary doctors under Entrepreneurship Development Programme.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Set up a Pension Fund Regulatory and Development Authority to manage pension funds to rationalise the pension payment in future as being adopted by the Central Government and by a few States. 	<ul style="list-style-type: none"> Set up a Budget Cell to monitor and keep the accounts of the State's finances. Set up a special cell in the Finance Department to tackle the problems and grievances of the entrepreneurs as well as to provide all round guidance to them. 	<ul style="list-style-type: none"> New projects of constructing transmission lines and sub-stations.
20. Orissa	<ul style="list-style-type: none"> State Culture Fund has been created by the Government in the Dept. of Culture for promoting and propagating the art and culture of the State. Zero based investment review to ensure completion of the projects which are languishing for years. 	<ul style="list-style-type: none"> Framing of a special rule for self employment. Western Orissa Development Council has been constituted with a view to accelerating the pace of development. Tenure of Orissa Health System Development Project being implemented with assistance of World Bank is being extended for one more year. 	<ul style="list-style-type: none"> A new scheme "Swayamsidha" with funding from Govt. of India is implemented for empowerment of women. Dept. of Information Technology proposed 2 self employment schemes viz.; Information Kiosks and Business Process Outsourcing Complex.
21. Punjab	<ul style="list-style-type: none"> Seeking Structural Adjustment Loan facility from World Bank for providing requisite fiscal space for sustaining the development process. Introduce contributory based pension scheme to cover new Government employees. Also cover them with new health insurance scheme on shared-premium basis. Set up a Municipal Development Fund under the Punjab Accelerated Infrastructure Development Programme to fund urban infrastructure projects. To facilitate transformation of agriculture in the State, it is proposed to set up Agri-Diversification, Infrastructure, Research and Development Fund (ADIRF), which would be capitalised by a levy on diesel and petrol. 	<ul style="list-style-type: none"> Project Urban Water Supply, Sewerage, Sewage Treatment and Solid Waste Management is posed for World Bank assistance. Unbundling of Punjab State Electricity Board as part of road map for reforms. Set up a Medical Education Board for improving quality and for enforcing standards in respect of medical institutions. Human Resource Development by improving the provisioning and quality of health and education through alternate delivery systems. A new scheme – "Balri Rakhrak Yojna" – has been formulated, under which incentives will be provided to the people adopting terminal methods of family welfare after birth of one or two girl children. 	<ul style="list-style-type: none"> Introduce mid-day meal programme in all the Government schools. Proposed 2 major projects to Govt. of India, viz.; Strengthening of Primary Health Care Services for multilateral funding and an Integrated Reproductive, Child Health & Family Planning Programme under vertical funding by Govt. of India. Gas-based thermal plant of 1000 MW is proposed near Doraha. Set up a University of Animal Sciences to spearhead research in animal husbandry, veterinary science and dairy technology. Adopt the 'Golden Rozgar Bus Scheme' for the benefit of unemployed youth, ex-servicemen, roadways employees, and terrorist victims.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Further reduce the rate of interest on crop loans by atleast 1 per cent from the existing 11 per cent to align the rates charged by commercial bank for similar loans. The self-financed health insurance scheme "Sanjivni" for the members of the Primary Cooperative Societies will be operative from this year. Setting up of the Village Development Fund under the Punjab Accelerated Infrastructure Programme for tackling the problem of sewage and sanitation covering 1500 villages in 2 years. Create a 'Dedicated Social Security Fund' to ensure timely payment of pensions to the aged, widows, destitute, disabled and dependent/orphans in the future. Create a "Agricultural Diversification Research & Development Fund" to redirect research and development programmes towards development of superior varieties of alternative crops, improved agricultural practices and appropriate post harvest practices. 	<ul style="list-style-type: none"> Enact a law for providing statutory backing to various industrial approvals under a Single Window Service. Set up an Investment Commission for promoting investment in agriculture, infrastructure, industry and services sector on the lines of the National Investment Commission. Set up a Farmers' Commission to provide a forum for farmers to voice their grievances and also guide the various policies in agriculture and allied sectors. Preparation of a road map for empowerment of the <i>Panchayati Raj</i> Institutions. New survey to be carried out by an independent agency for the enumeration of BPL families with enlarged definition for providing them a better quality of life. A dedicated Social Security Fund has already been set up to finance various social security and welfare schemes which will be operative from April 2005. As an implementation strategy, all important proposals made in the Budget would be reviewed by a group of Ministers under the Chairmanship of Chief Minister, every quarter. A new scheme "Drug De-addiction will be launched to create awareness regarding drug abuse among youth. 	<ul style="list-style-type: none"> Launch the "Information and Communication Technology" project in selected Government schools to train teachers for enhancement of teaching learning process.
22. Rajasthan	<ul style="list-style-type: none"> 7,200 school teachers, 4,000 constables and 456 college lecturers will be recruited. 	<ul style="list-style-type: none"> Road Infrastructure Development Company of Rajasthan has been set up to mobilise resources for the development of roads. 	<ul style="list-style-type: none"> Mid-day Meal Scheme is to be made attractive and nutritious for the children.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Implementation of VAT is to be kept in abeyance. Simplification and rationalisation of tax administration. Amendments in Sales Tax Act are proposed to execute tax returns through electronic media/internet. Rajasthan Relief Fund is to be set-up to meet out natural calamity and for an immediate commencement of relief work for the affected ones. 	<ul style="list-style-type: none"> Rajasthan Finance and Development Corporation has been set-up to strengthen finances of urban bodies and to help in accelerating urban development. 	<ul style="list-style-type: none"> All important crops are to be included under Crop Insurance Scheme. Plan has been made to set-up Knowledge Corridor and Knowledge Park to create employment avenues in Information Technology Sector. Livelihood Mission has been constituted to identify potential areas of new employment to harness the available resources in a better way and also recommend programme for their overall development. Establish an Institute of Foreign Languages in the State.
23. Sikkim	<ul style="list-style-type: none"> Broaden the State's internal resource base by introducing new avenues of taxation. Create a special fund to attain the goal of making Sikkim a Total organic State by 2009. The fund will be jointly conducted by the Department of Agriculture and Department of Science and Technology. Sponsor Sikkim Research Fellowships in 7 eminent Universities primarily for Sikkim students and build intellectual capacity in the State. Establish the State Illness Assistance Fund with Central Govt. matching 50% contribution and will provide monetary assistance to BPL patients in need of specialised treatment. Appoint the Sikkim State Human Rights Commission and also set aside a separate fund for its functioning. 	<ul style="list-style-type: none"> The ADB-approved Technical Assistance on Capacity Building for Fiscal reforms in Sikkim is aimed at designing effective methods to improve the State's finances and to build the necessary capacity to implement and sustain these measures. Setting up a unit in the Department of Personnel for the promotion of employment abroad. A policy to facilitate development of one model tourism village each in all the constituencies. Set up urban local bodies in select townships. Chief Ministers Self Employment Scheme Phase II to encourage the youths to take up all kinds of productive activities. 	<ul style="list-style-type: none"> Establish colleges and a Science college to make higher education widely and easily accessible. Introduce Sikkim Youth Technologists Programme primarily for those entrepreneurial youths who would like to upgrade their technical and technological skills in specific fields.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Introduce a Career Development Fund to be used by all graduates unemployed students/youth of Sikkim as an one time assistance for coaching in India. Wherever feasible, user charges will be introduced while ensuring qualitative improvement in the standard of services. 		
24. Tamil Nadu	<ul style="list-style-type: none"> Extend 50% subsidy for small and marginal farmers taking up drip and sprinkler irrigation systems. Pension Scheme for the benefit of construction workers would be implemented. Pension scheme for the benefit of workers in other unorganised sectors proposed. A new scheme of interest subsidy to be introduced as an incentive to processing units which adopt clean technology. It will be available to small and medium enterprises. Launch the Tamil Nadu Empowerment and Poverty Reduction Project funded by the World Bank under which each selected village will establish a Village Livelihood Fund to provide support to poor families. Pension scheme with lump sum benefit for the employees working in non-pensionable service such as organisers, anganwadi workers, helpers and cooks working in Noon Meal scheme and ICDS projects. 	<ul style="list-style-type: none"> A Special Task Force to be constituted so that plans to tackle the difficult problem of pollution of rivers by industrial can be implemented with full participation by industry groups. A new programme to upgrade thatched and kutcha houses to provide better shelter to the rural population is proposed. Launch a new programme of providing free house-sites for the rural poor by acquiring necessary land. The Tamil Nadu Road Infrastructure Development Corporation is being established to mobilise resources for the Comprehensive Road Infrastructure Development Programme. A State Action Plan has been evolved to rehabilitate child labour in the State and the Government has sanctioned formation of State Level and District Level Child Labour rehabilitation cum Welfare Societies. 	<ul style="list-style-type: none"> Establish a new Agri-Export Zone for cashew. The World Bank approved the Water Resources Consolidation Project-1 for implementation under which 17 major basins have been formed for integrated management of the available water resources. Undertake a new programme of deepening and reconstructing irrigation tanks under the control of PWD to ensure that each tank functions as a proper reservoir. Phase-II of the Tamil Nadu Afforestation Project financed by Japanese Bank of International Cooperation will be implemented. A special programme under the Comprehensive Road development Programme to improve existing Panchayat Union Roads will be launched. The Tamil Nadu Rural Water Supply Project with assistance from the World Bank is being finalised for implementation. Desalination plant project at Chennai would be implemented shortly.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Reduction in stamp duty with monetary cap for transfer of Non Performing Assets to Asset Reconstruction Companies. 		<ul style="list-style-type: none"> A new scheme "Kasturba Gandhi Balika Vidyalaya" will be launched in blocks situated in 10 districts where female ratio is less than national average. This scheme will help in narrowing the gap between rate of male and female illiteracy.
25. Tripura	<ul style="list-style-type: none"> Creation of Guarantee Redemption Fund. Steps in the current financial year to settle outstanding liabilities of the past committed expenditure of different department in 2 instalments. 	<ul style="list-style-type: none"> Responsibility for running certain utility services will be handed over to local bodies. A high level Committee will be constituted to look into the revival of PSUs in a time bound manner. Launch a State Sector Scheme for generation of employment in the urban areas. Preparation of comprehensive master plans for <i>Nagar Panchayats</i>. A Consultative Committee is being constituted to suggest removal of bottlenecks and wrong perception besides implementation problems, if any, in implementation of the new system of VAT. A Facilitation Centre will be set up in the office of Commissioner of Taxes for redressal of grievances. 	<ul style="list-style-type: none"> Several programme being drawn up for promotion of higher education. Several important transport projects will be taken up for implementation.
26. Uttaranchal	<ul style="list-style-type: none"> Computerisation of treasuries, commercial tax department, transport department, stamp & registration and also bringing improvement in accounting standards and practices and procedures towards fiscal discipline. Implementation of self-assessment scheme for tax assesses business men having turnover up to Rs.25 lakh. 	<ul style="list-style-type: none"> Uttaranchal Transport and Traffic Advisory Committee has been set-up to develop road ways in a planned manner. Decision has been made to set-up 'Area Fund' (Rs.25 lakh per <i>Panchayat</i>) to execute developmental work at the <i>Panchayat</i> level. 	<ul style="list-style-type: none"> WIMAX computer net work system is to be implemented to have wireless connectivity in entire State and also to provide free internet facilities to all. Proposal of financing high cost bridges and roads through World Bank or ADB is under consideration. Efforts are being made to expand the coverage and increase the effectiveness of Agriculture Crop Insurance Scheme.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Contd.)

State	Fiscal	Institutional	Sectoral
27. Uttar Pradesh	<ul style="list-style-type: none"> Emphasis to lessen dependence on market loans/borrowings and making efforts towards enhancing own resources. This proposal is under consideration before 'Cabinet Committee for Resources' and 'Resources and Expenditure Commission'. New Insurance Scheme is being introduced for 5 lakh rickshaw pullers to benefit them in case of accidental death or getting physically handicapped. 		<ul style="list-style-type: none"> Concept of 'Gender Budgeting, is being introduced towards an effective tool for women empowerment. 2005-06 has been declared as a 'Year of completion of old/incomplete work'. Rural Development and Agri-business Centres are to be set-up under a new scheme. Decision has been made to encourage private investments in the area of housing construction to meet the target of 'Houses for All' on a priority basis. 2500 primary schools and 2200 high primary schools are to be set-up to improve education facilities in the rural areas. Chief Minister Rural-based Industries Employment Scheme is to take-off to create self-employment avenues for unemployed people of the rural areas.
28. West Bengal	<ul style="list-style-type: none"> Person holding land within ceiling limit and willing to sell part of the land to Government at market rate, which the Government would purchase for distribution, free of cost among landless agricultural labourers. Set up a definite venture capital fund to encourage small scale entrepreneurs in the area of information technology and IT enabled services. Integrate a health insurance scheme with the earlier introduced provident fund scheme for workers in the unorganised sector. 	<ul style="list-style-type: none"> A new scheme of employment generation for the urban poor under which the poor people in the urban areas can be directly engaged, without the involvement of contractors, for the purpose of improvement and maintenance of roads, drainage, etc. 	<ul style="list-style-type: none"> Introduce decentralised preventive and curative health care services in the rural areas of the State, for which <i>Gram Panchayats</i> will be linked to subsidiary health centres, <i>Panchayat Samitis</i> to block primary health centres and Zilla Parishads to district level hospitals.

Annex 1: Major Policy Initiatives of State Budget 2005-06 (Concl'd.)

State	Fiscal	Institutional	Sectoral
	<ul style="list-style-type: none"> Abolish licence fee and additional licence fee and increase the excise duty of foreign liquor suitably. Reduce duty on energy produced from generating sets to provide relief to industries with captive generation plants. Tea estate would be exempted from payment of education cess and rural employment cess for a period of 3 years provided arrears upto March 31, 2004 with interest are paid. Important decision taken to pre-pay, on their own, loans of All-India financial institutions for reducing their debt burden. 		
29. NCT Delhi	<ul style="list-style-type: none"> Delhi Sales Tax on Works Contract would be abolished and dealers would pay only VAT. Drugs and medicines would be placed in the third schedule of VAT Act and would be taxed at 4 per cent. Several items such as poultry, knitting wool, footwear, tea, etc. would be subject to reduced VAT rate. Several items such as salt, bread, CNG, items under cottage industry, etc., have been exempted from VAT. 	<ul style="list-style-type: none"> Prepare the first Human Development report for Delhi with the assistance of various organisations. Establish 4 Permanent Lok Adalats for hearing of cases related to public utility services. Set up a Committee of experts to consider the levy of goods and passenger tax on transport vehicles. 	<ul style="list-style-type: none"> Introduce the Mono Rail System in areas where Metro Rail is not planned. A new measure for targeted urban renewal to upgrade the water supply and sewerage infrastructure and Members would be able to recommend works on these areas. Considering a proposal for establishment of 330 MW gas based power plant. Delhi Pollution Control Committee will set up its own monitoring stations in Delhi for better monitoring of air, noise and water pollution. Implement 2 separate programmes for street children and women in distress with NGO involvement and also set up short stay homes for women in distress. A new industrial estate is being planned for gems and jewellery sector. A Games Village is to be set up.

Annex 2: Fiscal Responsibility Legislation of States

Item/State	Karnataka	Kerala	Tamil Nadu	Punjab	Uttar Pradesh	Orissa
1	2	3	4	5	6	7
1. Year of Enactment	August 2002 (Act came into force on April 1, 2003)	September 2003 [Fiscal Responsibility Rules (FRR)] March 2005 and FRR (Amendment) May 2005)	2003 (Amended in 2005)	May 2003	February 2004	May 2005
2. Gross Fiscal Deficit (GFD)	Not more than 3 per cent of GSDP by March 2006	3.5 per cent of GSDP by 2005-06. 2 per cent of GSDP by 2006-07.	Not more than 3 per cent of GSDP by March 2008 and adhere to it thereafter	Contain annual growth rate of GFD to 2 per cent in nominal terms till GFD is below 3 per cent of GSDP	Not more than 3 per cent of GSDP by March 2009	Not more than 3 per cent of GSDP by 2009; Reducing by 1.5 per cent of GSDP every year from 2004-05
3. Revenue Deficit (RD)	Nil by March 2006	2 per cent of GSDP by 2005-06 Nil by 2006-07	Ratio of RD to Revenue Receipt below 5 per cent by March 2008; Eliminate RD by 2008-09 and adhere to it thereafter.	Reduce Revenue Deficit to Revenue Receipts by at least 5 percentage points from the previous year, until revenue balance is achieved.	Nil by March 2009	Nil by 2008-09
4. Guarantees	Not to give guarantee for any amount exceeding the limit stipulated under the Karnataka Ceiling to Government Guarantees Act, 1999	—	Cap the total outstanding guarantees to 100 per cent of the total revenue receipts in the preceding year or at 10 per cent of GSDP, whichever is lower.	Cap outstanding guarantees on long-term debt to 80 per cent of revenue receipts of the previous year and guarantees on short-term debt to be given only for working capital or food credit and	Not to give guarantee for any amount exceeding the limit stipulated under any rule or law of the State Government for the purpose.	—

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Karnataka	Kerala	Tamil Nadu	Punjab	Uttar Pradesh	Orissa
1	2	3	4	5	6	7
				fully backed by stocks.		
5. Liabilities	Not to exceed 25 per cent of GSDP by March 2015	–	–	Ratio of Debt-GSDP to be 40 per cent by 2006-07	Not to exceed 25 per cent of GSDP by March 2018	(i) Debt stock to be limited to 300 per cent of revenue receipts by 2007-08 (ii) Interest payment as ratio to revenue receipts is to be limited to 18-25 per cent.
6. Expenditure	–	–	–	–	As per the targets to be given in the Medium-Term Fiscal Restructuring Policy (MTFRP).	Not more than one Supplementary Statement of expenditure shall be presented in a financial year. No liability shall be created outside the budget provision in a financial year without the approval of the Government.
7. Medium- Term Fiscal Plan (MTFP)	MTFP would include- (i) Four year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability, (iii) strategic priorities, (iv)	MTFP would include- (i) Three year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability, (iii) overview of the fiscal policy	MTFP would include- (i) multi-year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) medium-term fiscal objectives	MTFP would include- (i) three-year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) recent economic trends and future	MTFP would include- (i) five-year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) contain medium term fiscal objectives (iv)	MTFP would include- (i) three-year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) contain medium term fiscal

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Karnataka	Kerala	Tamil Nadu	Punjab	Uttar Pradesh	Orissa
1	2	3	4	5	6	7
	evaluation of performance of prescribed fiscal indicators, (v) policies on various fiscal parameters for the ensuing year and (vi) evaluation as to how current policies are in conformity with the fiscal management principles and the objective set out in MTFP Statement.	currently in vogue a n d (iv) evaluation of current policies.	(iv) evaluation of the performance of the prescribed fiscal indicators (v) economic trends and future prospects for growth and developments and (vi) strategic priorities in the fiscal matters for the ensuing financial year, (vii) evaluation of the current policies vis-a-vis the fiscal m a n a g e m e n t principles and (viii) policies pertaining to various fiscal parameters.	prospects for growth and developments and (iv) strategic priorities in the fiscal matters for the ensuing financial year, (vii) key fiscal measures and rationale for any major deviation and (viii) policies pertaining to various fiscal parameters.	evaluation of performance based on fiscal indicators (v) recent economic trends and future prospects for growth and development and (vi) strategic priorities in the fiscal matters for the ensuing financial year, (vii) evaluation of current policies vis-à-vis fiscal m a n a g e m e n t principles and (viii) policies pertaining to various fiscal instruments.	o b j e c t i v e s (iv) evaluation of performance of fiscal indicators and (v) strategic priorities in the fiscal matters for the ensuing financial year and (vi) evaluation of current policies vis-à-vis fiscal m a n a g e m e n t principles and (vii) policies pertaining to various fiscal instruments.
8. Compliance	<p>Half-yearly review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target.</p> <p>GFD and RD may exceed the limits on grounds of unforeseen demands due to national security or natural calamities. The excess beyond limits</p>	<p>Public Expenditure Review Committee would submit a review report during the month of November every year, giving full account of each item where the deviation from the fiscal target has occurred during the previous year.</p>	<p>Independent external body to carry out periodic review for the compliance of the provisions of the Act.</p> <p>GFD and RD may exceed the limits on grounds of u n f o r e s e e n demands due to national security or natural calamity.</p> <p>The excess beyond limits arising due to</p>	<p>Quarterly review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target.</p> <p>GFD and RD may exceed the limits on unforeseen grounds due to national security or natural calamity. The net fiscal cost of the</p>	<p>Half-yearly review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target.</p> <p>GFD and RD may exceed the limits on grounds of u n f o r e s e e n demands due to national security or natural calamity.</p>	<p>(i) Review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target (ii) GFD and RD may exceed the limits on grounds of u n f o r e s e e n demands due to national security or natural calamity.</p>

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Karnataka	Kerala	Tamil Nadu	Punjab	Uttar Pradesh	Orissa
1	2	3	4	5	6	7
	arising due to natural calamities does not exceed the actual fiscal cost that can be attributed to the calamities.		natural calamities does not exceed the actual fiscal cost that can be attributed to the calamities.	calamity would be the ceiling for extent of non-compliance.		
9. Pension	—	—	—	—	—	—
10. Fiscal Transparency	Specify the guiding fiscal management principles and take suitable measures to ensure greater fiscal transparency and minimize secrecy in preparation of annual budget	Measures to ensure greater transparency in the fiscal operations. Present to the Legislature several Statements on various fiscal indicators and parameters.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.
11. Others	—	—	May assign an independent external agency to carry out the periodical review for the compliance of the provisions of this Act.	—	While adhering to fiscal years, priority to protecting certain expenditure defined in the Medium Term Fiscal Restructuring Policy as 'High Priority Development Expenditure' from curtailment or may impose a recede or partial curtailment.	(i) Generate primary surplus of over 2 per cent of GSDP by March 2008 (ii) ratio of salary to State's own revenue to be reduced to 80 per cent by March 2008 (iii) ratio of non-interest committed revenue expenditure to State's own and mandated revenue to be reduced to 55 per cent by March 2008.

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Maharashtra	Rajasthan	Assam	Gujarat	Himachal Pradesh	Haryana
1	8	9	10	11	12	13
1. Year of Enactment	April 2005	May 2005	May 2005	March 2005	April 2005	July 2005
2. Gross Fiscal Deficit (GFD)	Shall specify, by rules, targets for reduction of GFD. GFD to be interpreted as expenditure on interest to revenue receipts.	3 per cent of GSDP following a path of minimum average annual reduction of 0.4 per cent of GSDP.	3 per cent of GSDP by March 2010.	Not more than 3 per cent of GSDP by March 2009.	–	Not more than 3 per cent of GSDP by March 2010.
3. Revenue Deficit (RD)	To eliminate RD by 2009 and maintain revenue surplus balance thereafter.	Nil by March 2009 with an average annual reduction of 3 per cent in RD-RR ratio.	Nil by March 2010.	Nil by March 2008.	Reduce RD-RR ratio atleast by 2 percentage points each year until revenue surplus is achieved.	Nil by 2008-09 and generate revenue surplus thereafter.
4. Guarantees	–	–	Restrict the guarantee to 50 per cent of State's own tax and non-tax revenue of the previous year or 5 per cent of GSDP of the previous year at current prices, whichever is lower.	Cap outstanding guarantees within the limit provided in the Gujarat State Guarantees Act, 1963.	Progressively reduce outstanding guarantees on long-term debt, until it can cap outstanding risk weighted guarantees at 80 per cent of total revenue receipts in the preceding year for which actuals are available as per finance accounts.	–

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Maharashtra	Rajasthan	Assam	Gujarat	Himachal Pradesh	Haryana
1	8	9	10	11	12	13
5. Liabilities	–	Outstanding Debt excluding public account and risk weighted outstanding guarantees not to exceed twice the receipts in the Consolidated Fund of the State.	Restrict total Debt stock including the Government guarantees to 45 per cent of GSDP of the previous year at current prices by March 2010.	Ratio of Debt-GSDP to be 30 per cent by March 2008.	–	Ensuring outstanding total debt including contingent liabilities to 28 per cent of GSDP by March 2010.
6. Expenditure	–	–	Restrict revenue expenditure under Annual State Plan to one-third of the Plan Outlay	–	–	–
7. Medium-Term Fiscal Plan (MTFP)	MTFP would include- (i) three-year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) contain medium term fiscal objectives (iv) evaluation of current policies vis-à-vis fiscal management principles (v) strategic priorities in the fiscal matters for the ensuing financial year, (vi)	MTFP would include- (i) setting forth fiscal objectives and strategic priorities of the Government (ii) assessment of the sustainability (iii) evaluation of performance of fiscal indicators, (iv) evaluation of current policies vis-à-vis fiscal management principles (v) strategic priorities in the fiscal matters for the ensuing	MTFP would include- (i) five year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) evaluation of performance of fiscal indicators (iv) medium term fiscal objectives (v) economic trends and future prospects for growth and developments and (vi) conformity of current policies	MTFP would include- (i) three year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) evaluation of performance of fiscal indicators vis-à-vis targets (iv) containing medium term fiscal objectives (v) conformity of current policies with the fiscal management	MTFP would include- (i) four year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) evaluation of performance of fiscal indicators vis-à-vis targets (iv) economic trends and future prospects for growth and developments and (v) strategic priorities in the fiscal matters for the	MTFP would include- (i) three year rolling target for the prescribed fiscal indicators (ii) assessment of the sustainability (iii) evaluation of the current policies vis-a-vis the fiscal management principles and (iv) strategic priorities in the fiscal matters for the ensuing financial year, (v) policies pertaining to various fiscal

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Maharashtra	Rajasthan	Assam	Gujarat	Himachal Pradesh	Haryana
1	8	9	10	11	12	13
	fiscal policies pertaining to various fiscal parameters and (vii) rationale for any major deviation.	financial year, (vi) policies pertaining to various fiscal parameters and (vii) rationale for any major deviation.	with the fiscal management principles (vii) strategic priorities in the fiscal matters for the ensuing financial year and (viii) policies pertaining to various fiscal parameters.	principles (vi) strategic priorities in the fiscal matters for the ensuing financial year, (vii) policies pertaining to various fiscal parameters and (viii) rationale for any major deviation.	ensuing financial year.	parameters and (vi) rationale for any major deviation.
8. Compliance	<p>Quarterly review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target.</p> <p>GFD and RD may exceed the targets on grounds of natural calamities or other exceptional grounds.</p>	<p>Half-yearly review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target.</p> <p>GFD and RD may exceed the limits on grounds of unforeseen demands due to national security or natural calamities.</p> <p>Constitution of Public expenditure Review Committee.</p>	<p>Yearly review of receipts and expenditure in relation to budget estimates along with remedial measures, if required.</p> <p>GFD and RD may exceed the limits on grounds of unforeseen demands arising out of internal disturbance or natural calamities or such other exceptional grounds.</p>	<p>Review of receipts and expenditure in relation to budget estimates along with remedial measures to achieve the budget target. Such review shall be placed immediately following the end of the Second quarter of the financial year.</p> <p>GFD and RD may exceed the limits on account of unforeseen circumstances or natural calamity.</p>	<p>Half-yearly review of receipts and expenditure in relation to budget estimates along with remedial measures if required.</p> <p>RD may exceed the limits on grounds of unforeseen demands due to national security or natural calamities.</p>	<p>Half-yearly review of receipts and expenditure in relation to budget estimates along with remedial measures if required.</p> <p>GFD and RD may exceed the limits on grounds of unforeseen demands arising due to internal disturbance or national security or natural calamities.</p>

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Maharashtra	Rajasthan	Assam	Gujarat	Himachal Pradesh	Haryana
1	8	9	10	11	12	13
9. Pension	–	Present to the Legislature every year estimated yearly pension liabilities worked out on actuarial basis for the next ten years.	–	Present to the Legislature every year estimated yearly pension liabilities worked out on actuarial basis for the next ten years.	–	Present to the Legislature every year estimated yearly pension liabilities worked out on actuarial basis for the next ten years.
10. Fiscal Transparency	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.	Measures to ensure greater transparency in the fiscal operations.
11. Others	–	–	Salary and wages will be contained within 60 per cent of the total tax and non-tax revenue of the Government, including devolutions from the Centre but excluding the grants under the Annual Plan from the Planning Commission and other developmental grants. Defining of offences and the penalty defined under the Act.	–	–	Set up an independent agency to review periodically the compliance of the provisions of the Act.

Annex 2: Fiscal Responsibility Legislation of States (Contd.)

Item/State	Chhattisgarh	Madhya Pradesh	Tripura	Andhra Pradesh
1	14	15	16	17
1. Year of Enactment	September 2005	August 2005	2005 June	October 2005
2. Gross Fiscal Deficit (GFD)	3 per cent of GSDP by March 2009	Bring down to 3 per cent of GSDP by March 2009	3 per cent of GSDP by March 2010	Bring down to 3 per cent of GSDP by March 2010
3. Revenue Deficit (RD)	Nil by March 2009	Nil by March 2009 and generate revenue surplus thereafter	Strive to remain revenue surplus by making a balance in revenue receipts and expenditure and build up further surplus	Nil by March 2009 and generate revenue surplus thereafter
4. Guarantees	–	Not to exceed 80 per cent of the total revenue receipts in the year preceding the current year	Limit the amount of annual incremental risk weighted guarantees to 1.0 per cent of GSDP	Limit the amount of annual incremental risk weighted guarantees to 90 per cent of total revenue receipts
5. Liabilities	–	Not to exceed 40 per cent of GSDP by 2015	Not to exceed 40 per cent of GSDP by 2010	Not to exceed 35 per cent of GSDP by March 2010
6. Expenditure	–	–	–	–
7. Medium- Term Fiscal Plan (MTFP)	MTFP would include- (i) three year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability and (iii) evaluation of current policies vis-à-vis fiscal management principles (iv) strategic priorities in the fiscal matters for the ensuing financial year, (v) policies pertaining to various fiscal parameters and (vi) rationale for any major deviation in fiscal measures.	MTFP would include- (i) five year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability, (iii) evaluation of current policies vis-à-vis fiscal management principles (iv) strategic priorities in the fiscal matters for the ensuing financial year, (v) policies pertaining to various fiscal parameters and (vi) rationale for any major deviation.	MTFP would include- (i) three year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability and (iii) evaluation of current policies vis-à-vis fiscal management principles (iv) strategic priorities in the fiscal matters for the ensuing financial year and (v) policies pertaining to various fiscal measures and (vi) rationale for any major deviation in fiscal measures.	MTFP would include- (i) three year rolling target for prescribed fiscal indicators, (ii) assessment of the sustainability and (iii) evaluation of current policies vis-à-vis fiscal management principles (iv) strategic priorities in the fiscal matters for the ensuing financial year, (v) policies pertaining to various fiscal instruments and (vi) rationale for any major deviation in fiscal measures.
8. Compliance	Quarterly review of receipts and expenditure in relation to	(i) Half-yearly review of receipts and expenditure in	(i) Quarterly review of receipts	(i) Quarterly review of receipts

Annex 2: Fiscal Responsibility Legislation of States (Concl.)

Item/State	Chattisgarh	Madhya Pradesh	Tripura	Andhra Pradesh
1	14	15	16	17
	budget estimates along with remedial measures, if required. GFD and RD may exceed the limits on grounds of unforeseen demands due to internal disturbance or natural calamities or such other exceptional grounds.	relation to budget estimates along with remedial measures, if required, (ii) An independent agency may be entrusted to review periodically the compliance of the provisions of this Act and to present such reviews in the Legislature. (iii) GFD and RD may exceed the limits on grounds of unforeseen demands due to internal disturbance or natural calamities or such other exceptional grounds.	and expenditure in relation to budget estimates along with remedial measures, if required, (ii) An independent agency may be entrusted to review periodically the compliance of the provisions of this Act and to present such reviews in the Legislature. (iii) GFD and RD may exceed the limits on grounds of unforeseen demands due to internal disturbance or natural calamities or such other exceptional grounds.	and expenditure in relation to budget estimates along with remedial measures, if required, (ii) An independent agency may be entrusted to review the compliance of the provisions of this Act and to present such reviews in the Legislature. (iii) GFD and RD may exceed the limits on grounds of unforeseen demands due to internal disturbance or natural calamities or such other exceptional grounds.
9. Pension	—	Estimating yearly pension liabilities worked out on actuarial basis or using trend growth rate for the next ten years.	Estimating yearly pension liabilities worked out on actuarial basis for the next ten years.	Estimating yearly pension liabilities worked out on actuarial basis for the next ten years.
10. Fiscal Transparency	Measures to ensure greater fiscal transparency in the fiscal operations.	Measures to ensure greater fiscal transparency in the fiscal operations.	Suitable measures to ensure greater fiscal transparency in the fiscal operations and minimise secrecy in preparation of Budget.	Measures to ensure greater fiscal transparency in the fiscal operations.
11. Others	—	—	—	—

GFD: Gross Fiscal Deficit, RD: Revenue Deficit, GSDP: Gross State Domestic Product, RR: Revenue Receipts

Fiscal transparency measures include among others the disclosure of accounting standards, policies and practices that may affect the computation of the fiscal indicators. While some States have stated to disclose the contingent liabilities created by way of guarantees, some States have indicated to present statements of Guarantee Redemption Fund, Consolidated Sinking Fund, employees in PSUs and related salaries, estimated yearly pension liabilities and details of borrowings and WMA/Overdraft availed from the Reserve Bank of India.

Explanatory Note on Data Sources and Methodology

Data Sources

This study is based on the receipts and expenditure data presented in the Budget documents of the 27 State Governments and the National Capital Territory of Delhi. For Bihar, Vote-on-Account presented in the Parliament has been incorporated. The analysis strictly conforms to the data presented in the State Budgets and the accounting classification thereof. Some supplementary information regarding Additional Resource Mobilisation (ARM) efforts and the level of guarantees (contingent liabilities) provided by States are also furnished. Some material received from the Planning Commission relating to State-wise Plan outlays are also incorporated. The analysis conforms to the accounting classification into Revenue and Capital Accounts and their bifurcation into 'Plan' and 'Non-Plan'.

The data provided in Appendix III (Capital Receipts) and Appendix IV (Capital Expenditure) in the present Study are on a gross basis for all items, including Public Account. Total Capital Receipts and Total Capital Disbursements as well as Aggregate Receipts and Aggregate Disbursements for 2003-04 (Accounts), 2004-05 (Revised Estimates) and 2005-06 (Budget Estimates) will, therefore, not be comparable with that of the previous years given in the Study.

The data for Gross State Domestic Product (GSDP) for each of the States used in this Study have been sourced from the Central Statistical Organisation (CSO) website. Wherever unavailable such data for 2004-05 and 2005-06 have been taken from the website of Ministry of Finance, Government of India. For some States for a couple of earlier years the data are estimated based on the average growth rates for previous five years.

Methodology

As set out in the Budget documents, the analysis of the expenditure data is disaggregated into developmental and non-developmental expenditure. All expenditure relating to Revenue Account, Capital Outlay and Loans and Advances are categorised into general services, social services and economic services. Broadly, the social and economic services constitute developmental expenditure, while expenditure on general services is treated as non-developmental. This re-classification is done without altering the total receipts, expenditures and overall balance presented in the budget.

With the change in data presentation of Appendix III and Appendix IV, the Overall Deficit/Surplus (Conventional Deficit/Surplus) used in the analysis is, equal to the Cash Deficit/Surplus only, which is the difference between the Closing balance and Opening balance. The increase/decrease in Cash Balance Investment Account and the increase/decrease in WMA extended by the Reserve Bank have now been included under Appendix III and Appendix IV. These 2 items in the earlier studies formed part of the financing items for the Overall Deficit/Surplus and have now been provided as Memo Items in this Study.

Methodology for Debt Statistics

The Reserve Bank, based on CAG's data series on outstanding liabilities of State Governments with a base year has been compiling a data series of outstanding liabilities of the State Governments on yearly basis by adding the budgetary flows. In this year's Study, the data series of outstanding liabilities of State Governments has been revised by broadening its composition to include reserve funds, deposits and advances and contingency funds of State Governments. The debt series has been compiled

by taking the data provided by the CAG in 'Combined Finances and Revenue Accounts of Union and State Governments in India'. In the absence of data for any particular head in the said publication, corresponding data from the State Budgets have been incorporated.

The item-wise outstanding liabilities as on end-March 2000 of the 3 bifurcated States (Bihar, Madhya Pradesh and Uttar Pradesh) have been apportioned to the respective 3 newly formed States (Jharkhand, Chhattisgarh and Uttaranchal) in their respective population ratios to facilitate research. The data provided in Appendix Tables 20 and 21 and Statements 26 to 28 on State debt position are provisional.

The State-wise market loans (Statement 33) based on which the maturity profile of outstanding State Government securities is provided at Statement 36-37 incorporates the appropriation of liability of the 3 bifurcated States to their respective newly formed States on the basis of Government of India notifications.

The Combined Finance Accounts (CFA) of Central and State Governments published by the Comptroller and Auditor General State Budgets and data from the Reserve Bank records have been utilised for Compiling the data series on debt.

Revised Coverage

The revised coverage used in the construction of the new debt series for States is as follows.

Total Outstanding Liabilities comprises of various account items under consolidated fund, public account and contingency fund.

I. Consolidated Fund

1. Public Debt
 - a) Open Market Borrowings
 - b) Borrowings from Banks and FIs
 - c) Special Securities issued to NSSF
 - d) Bonds/Debentures which are issued by the State Governments
 - e) Loans from the Centre
 - f) Others
2. Ways & Means Advances & Overdrafts from RBI

II. Public Accounts

1. State Provident Funds
2. Small Savings, Insurance and Pension Funds, Trust and Endowments, etc.
3. Deposits and Advances
4. Reserve Funds/Sinking Funds
5. Other Items in Public Accounts

III. Contingency Fund

Note:

Appendix Tables and Statements provide data for select years. State-wise data on some major fiscal indicators for the period 1980-81 to 2003-04 (BE) and State-wise detailed data on the transactions in the revenue and capital account for the period 1990-91 to 2003-04 (BE) are presented in "Handbook of Statistics on State Government Finances" published by the Reserve Bank in June 2004. This publication is also freely accessible on the Reserve Bank's website (www.rbi.org.in).