

Chapter 1

Introduction

Constitution of the Committee

1.1 On August 19, 1998, Dr. Bimal Jalan, Governor, Reserve Bank of India, constituted an *Informal Advisory Committee on Ways and Means Advances (WMA)*, consisting of Shri B.P.R.Vithal, Member, Tenth Finance Commission, as the Chairman; Dr. Ashok Lahiri, Director, National Institute of Public Finance and Policy (NIPFP) as a member; and Smt. Usha Thorat, Chief General Manager, Internal Debt Management Cell, Reserve Bank of India as the Member Secretary. Dr. R.K. Pattnaik, Director and Shri M.G. Kelkar, Assistant Manager of the Internal Debt Management Cell, Reserve Bank of India were the resource persons.

1.2 The Committee was asked to look into the existing scheme of WMA to State Governments and to consider rationalisation – if warranted revision – of limits, keeping in view the needs of the State Governments as also the issues relating to fiscal and monetary management. While appointing the Committee, the Governor desired that the Committee might hold discussions with State Governments, Central Government and officers of the Reserve Bank of India to ascertain their views. It was expected that the Committee would complete the work and submit the Report within six to eight weeks.

Broad Approach of the Committee

1.3 The Committee in its first meeting at Hyderabad on August 19, 1998 discussed the existing structure of WMA to State Governments and the Central Government and the background in which the previous two revisions in 1993 and 1996 were made. The Committee also had preliminary discussions on various aspects relating to WMA and overdrafts, particularly, (a) the underlying fiscal stress, (b) difficulties in measuring a genuine temporary mismatch between receipts and payments as opposed to a deficit problem, (c) the asymmetry between the Central and the State Governments in respect of WMA limits, (d) feasibility of a ceiling on overdrafts, and (e) monetary implications of a revision in WMA limits.

1.4 The Committee met the Finance Secretaries of the State Governments (States) and officials of the Government of India (Centre), the Reserve Bank of India (RBI) and the Planning Commission. The schedule of these meetings is set out in *Annexure 1.1*. A detailed questionnaire prepared and circulated to the States in order to facilitate the discussions with the Finance Secretaries of States is contained in *Annexure 1.2*. A summary of the discussions with the Finance Secretaries is at *Annexure 1.3*.

1.5 The RBI is a banker to both the Centre and the States and is compensated in terms of interest-free minimum balances maintained with it for the services it provides. In view of its responsibility for the conduct of monetary policy, the RBI is also required to ensure that both Centre and States operate within hard budget constraint. However, in this regard there is an asymmetry between the two, in terms of mobilising resources, particularly in respect of borrowings by the States in view of Article 293 of the Constitution. As a banker, the RBI has to provide reasonable amount of temporary advances to both to tide over their liquidity problems. The reconciliation of these conflicting needs of providing adequate temporary financing and of continuing a regime where fiscal discipline is maintained, as well as the difficulties of

distinguishing between a temporary liquidity problem and a structural deficit problem, are the challenges, the RBI has to face while dealing with WMA.

Structure of the Report

1.6 The structure of the Report is as follows: *Chapter 2* gives the existing system of WMA, overdrafts and investment of surplus funds along with a historical review of the successive revisions in the WMA limits since 1937. *Chapter 3* analyses the trends in WMA and recourse to overdrafts by the States during fiscal 1997-98 and 1998-99 (April-October), and *Chapter 4* presents the recommendations.