GOVERNMENT OF ODISHA

REVIEW OF COMPLIANCE

TO

ODISHA FISCAL RESPONSIBILITY & BUDGET MANAGEMENT ACT, 2005

2013-14

By

National Institute of Public Finance and Policy,
New Delhi

March, 2015

FINANCE DEPARTMENT

C O N T E N T S

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P R E F A C E

In terms of the provisions of Sub-section (2-a) of section 8 of Odisha Fiscal Responsibility and Budget Management Act, 2005 (Odisha FRBM Act, 2005), the State Government are required to entrust an agency, independent of the State Government interference, to make a review of compliance to the provisions of the Act and submit a report and cause it to be laid before the State Legislature.

In compliance with the said provisions of Odisha FRBM Act, 2005, the task of independent review of State's finances for the year 2013-14 was assigned to the National Institute of Public Finance and Policy (NIPFP), New Delhi, a national level institute engaged in the study and research in public finance and public policy. It is an independent non-Government Institution engaged in the pursuit of research in public economics and policies.

NIPFP assigned the task to Dr. Tapas Sen, Professor and Dr. Pratap Ranjan Jena, Associate Professor of the institute. In course of the review, the two experts visited Bhubaneswar and had interaction with senior officials of the State Government. The National Institute of Public Finance and Policy submitted the review report on 25th March, 2015.

I deem it to be a privilege to lay the report in the Legislative Assembly.

Bhubaneswar

March, 2015

(**Shri Pradip Kumar Amat**)
Minister, Finance

1. Introduction

The Odisha Fiscal Responsibility and Budget Management Act (FRBM), 2005 provides for an independent review/monitoring of compliance of the implementation of the FRBM Act. This is considered to be a desirable feature of the FRBM Act designed to improve the credibility and transparency of the fiscal management of the Government. An independent review of fiscal policy and fiscal rule achievements gives more credibility to the outcome of the fiscal policy. It helps in providing an unbiased assessment of Government's compliance with the provisions of the fiscal rules and reasons for deviations. An independent review has remained as an important element of public financial management requirements for effective fiscal responsibility legislation. The Act provides an institutional process to assess the fiscal management of the State Government keeping in view the statutory fiscal targets and fiscal management principles enshrined in the FRBM Act.

The State Government entrusted the responsibility of reviewing the compliance of the Act for the year 2013-14 to the National Institute of Public Finance and Policy (NIPFP), New Delhi. This review report evaluates the fiscal trends achieved during the year 2013-14 as against the budget projections contained in the rolling fiscal targets worked out in the Medium Term Fiscal Policy (MTFP) presented along with the budget. The report also assesses the desired fiscal management principles contained in the FRBM Act of the State to achieve the fiscal targets and transparency measures.

The report has analyzed the macroeconomic outlook and recent trends of finances of the State Government including revenue generation, expenditure framework, and the debt burden. The fiscal targets and achievements for the year 2013-14 are reviewed and an assessment has been done regarding the desired fiscal management principles. The report includes assessment regarding the sector priorities and expenditure pattern for the year 2013-14, including utilization of budgeted amount under revenue and capital heads. The Department of Finance, Government of Odisha, provided data and information on State Finances for this study and gave an overall perspective on the issues relating to State fiscal management. The study also benefited from the inputs provided by the spending departments.

The report is organized as follows. Section 2 provides an overall assessment of macroeconomic outlook and sectoral composition of GSDP. The section 3 contains analysis on state finances in recent years. Compliance of the State Government to the fiscal targets and fiscal management principles under the Odisha FRBM Act are covered in section 4. Issues related to revenue mobilization and expenditure pattern for the year 2013-14 as compared to the budget provisions are analyzed in Section 5. Concluding observations are contained in Section 6.

2. Macroeconomic Outlook

The growth profile of the State economy, given in Table 1, shows volatility since 2004-05. It has experienced a slowdown after 2007-08. The growth rate of the GSDP at constant prices declined from close to 11 per cent in 2007-08 to 7.75 per cent in 2008-09 and further plummeted to a low of 4.55 per cent in 2009-10. Although the State economy performed better in 2010-11, with a growth rate of 8.01 percent, it reverted to a slowdown after that. The growth rate has come down sharply to 1.82 percent in 2013-14. The nominal growth of the GSDP for the year 2013-14 was 8.66 percent as against 13.89 percent in the previous year.

The growth of the economy is an indicator to understand the revenue generation effort of the State Government. The recent decline in growth rate makes it difficult to increase the tax revenue. The composition of the State GSDP reveals that, the share of service sector has increased over the years. The share of service sector has gone up from 42.39 percent in 2004-05 to 50.62 percent in 2013-14. The manufacturing sector, which was showing a growing trend until 2007-08, has declined since then. The share of manufacturing sector has come down from about 30 percent in 2007-08 to 26.41 percent in 2013-14. The share of agriculture sector also has declined during this period. While agriculture sector is usually out of the tax net, the decline in manufacturing sector has repercussions for the success in improving the tax effort. Some of the sectors included in the service sector like transport and transactions in real estate provide a tax base to the Government. However, collection of service tax is in the hand of the Central government, out of which the State gets a share.

Table 1

Composition of GSDP (Constant Prices)

(Percent)

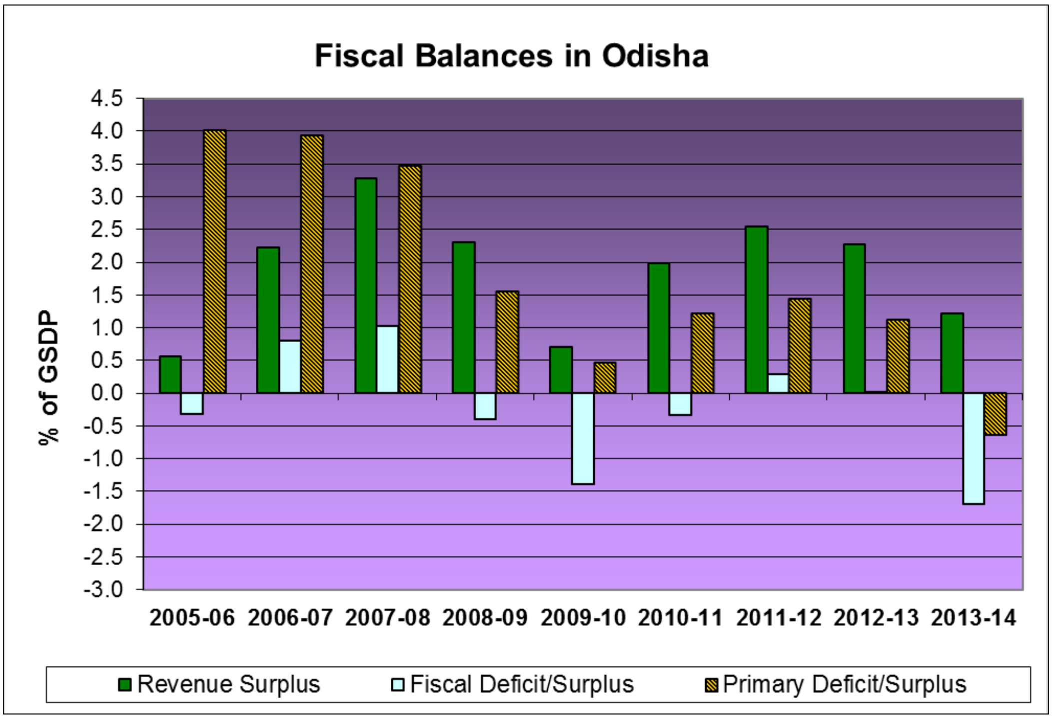
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Primary Sector	**31.03**	**30.72**	**28.99**	**27.30**	**26.31**	**26.95**	**24.98**	**23.69**	**24.66**	**22.97**
Agriculture	23.49	22.97	20.75	19.57	18.50	19.07	17.99	17.20	18.39	16.30
Mining	7.54	7.76	8.24	7.72	7.81	7.88	6.99	6.49	6.26	6.67
Secondary Sector	**26.58**	**25.38**	**27.40**	**30.01**	**29.05**	**26.44**	**27.36**	**27.72**	**26.46**	**26.41**
Manufacturing	12.05	11.70	13.12	15.74	16.56	14.77	14.40	13.97	13.00	13.04
Construction	10.41	10.11	10.32	10.12	9.61	9.58	10.17	11.13	10.59	10.39
Electricity & Water supply	4.11	3.58	3.96	4.15	2.88	2.09	2.79	2.62	2.87	2.98
Tertiary Sector	**42.39**	**43.89**	**43.61**	**42.70**	**44.64**	**46.61**	**47.66**	**48.59**	**48.89**	**50.62**
Transport	7.54	8.17	8.33	8.13	8.60	8.89	9.40	9.68	9.96	10.59
Trade, Hotel and Restaurant	10.68	11.57	12.45	12.29	12.42	12.95	13.42	13.87	13.59	13.37
Banking & Insurance	3.24	3.53	3.74	3.97	4.31	4.76	5.55	6.01	6.55	7.21
Real Estate	6.51	6.55	6.19	5.91	5.84	5.78	5.65	5.78	5.95	6.22
Public Admn	4.71	4.16	3.90	3.65	4.22	4.08	3.78	3.66	3.66	3.52
Other Services	9.71	9.91	9.00	8.74	9.25	10.15	9.85	9.59	9.18	9.71
GSDP Growth		**5.68**	**12.85**	**10.94**	**7.75**	**4.55**	**8.01**	**3.98**	**3.76**	**1.82**

Source: Central Statistical Unit, GoI

3. Overview of State Finances

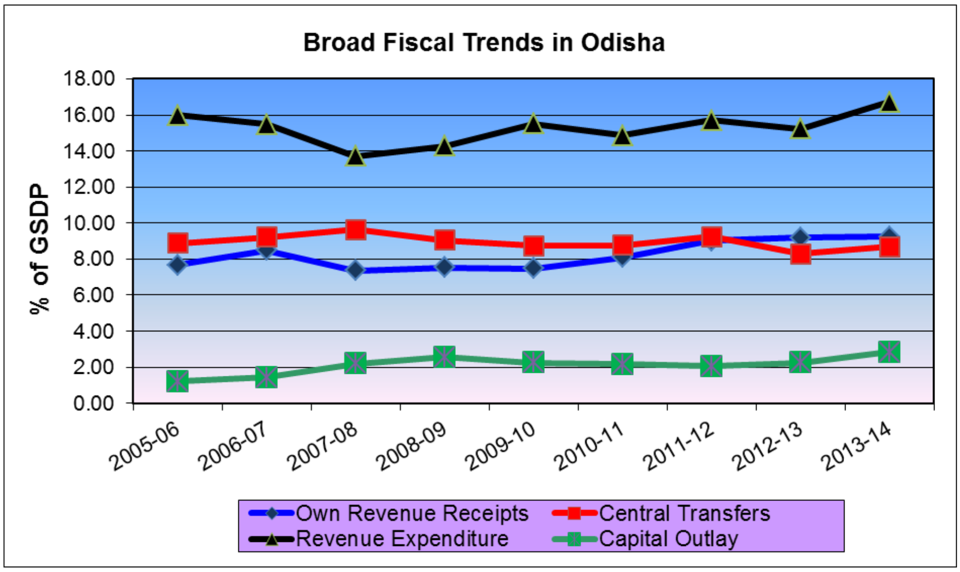
State finances in Odisha have exhibited healthy bottom lines since 2005-06 with revenue account surpluses and either fiscal surpluses or fiscal deficits within 2 percent of GSDP. The state also had primary surpluses since 2005-06 till 2012-13, which changed to a small deficit in 2013-14 (Figure 1). Even so, the overall fiscal balances should not cause any worry for the Government of Odisha. However, the surpluses/deficits can result in a variety of ways, with different combinations of underlying fiscal variables, all of which may not have the same implications for the prospects of the State and its citizens. To get a reasonable idea of the implications of the observed fiscal stance, it is usually necessary to look into the expenditure and revenue trends both in broad terms as also in some amount of detail.

Figure 1



To begin with, Figure 2 depicts the trends in own revenue receipts, central transfers, revenue expenditures and capital outlay (on general, social and economic services together). It shows that the State kept its revenue expenditures tightly controlled at 16 percent or below of GSDP throughout the reference period except in the last year (2013-14) when it shows significant increase. Similarly, capital outlay has been around 2 percent of GSDP except in 2013-14, when it increased noticeably. Own revenue receipts of the state comprising tax and non-tax sources exhibit a small increase after 2009-10; this small increase managed to make it the larger revenue source as compared to central transfers in 2011-12, though only marginally. This was facilitated by a small reduction in central transfers (shared taxes and grants) received by the Government of Odisha during 2012-13 and 2013-14 (Figure 2). Thus, despite a marginal increase in the state's own revenues during 2013-14, noticeable increases in both revenue and capital expenditures reduced the revenue surplus and enlarged the fiscal and primary deficits. One may add that even with the increases in both revenue and capital expenditures the state remains within the prescribed limits for the deficits. The rising expenditure levels may represent a legitimate strategy employed by the State Government of exploiting the fiscal space created by fiscal prudence of the previous years.

Figure 2



It is a little surprising that even during a period of fiscal consolidation own revenues of the state did not increase more than they actually did, failing to reach even 10 percent of GSDP. Since the effort would usually be directed towards tax revenues to achieve greater revenue mobilization, a disaggregation of tax revenue collections could be useful to identify successes and failures. Table 2 provides the necessary figures of tax revenue collections from individual taxes as a ratio of GSDP.

Table 2
Own Tax Revenues in Odisha

(% of GSDP)

	2009-10	2010-11	2011-12	2012-13	2013-14
Sales Tax (VAT)	3.23	3.32	3.45	3.72	3.86
State Excise	0.44	0.52	0.55	0.63	0.60
Stamp Duty & Regn Fees	0.33	0.22	0.21	0.23	0.22
Entry Tax	0.43	0.50	0.56	0.59	0.53
Motor Vehicle Tax	0.35	0.38	0.37	0.36	0.30
Electricity Duty	0.25	0.28	0.23	0.25	0.24
Land Revenue	0.23	0.18	0.20	0.24	0.17
Profession Tax	0.08	0.08	0.07	0.06	0.05
Other Taxes	0.03	0.03	0.03	0.03	0.03

It can be seen that despite uncertainties regarding introduction of GST, sales tax collections have been steadily improving as a percentage of GSDP; similarly, entry tax collections have been gradually improving, though the ratio dropped a little in 2013-14. The case of state excise is similar to that of entry tax, but with greater buoyancy. Stamp duty and registration fees, however, show poor buoyancy along with motor vehicle tax, dragging the aggregate tax buoyancy down. Also, the individual taxes with relatively low revenue significance – electricity duty, land revenue and profession tax – exhibit poor buoyancy. Clearly, some attention needs to be paid to these five taxes to identify the causes of low buoyancy and take remedial measures.

Central transfers have roughly doubled between 2007-08 and 2013-14 in absolute terms, but as percentage of GSDP, there has been some fall, particularly in 2012-13 and 2013-14. Share in central taxes constitutes the larger part of central transfers, but such shares and total grants have broadly moved together. Within grants, however, non-plan grants have increased faster than plan grants. Overall, central transfers have not kept pace with the increase in own revenues of the state, reducing the transfer dependency of the state over the years.

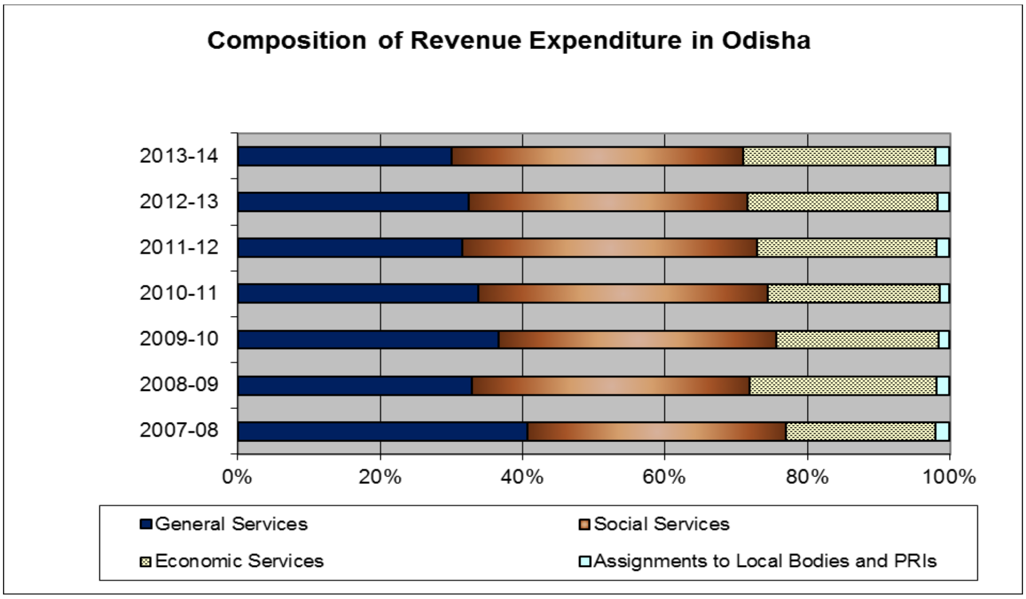
Table 3

Central Transfers to Odisha

(Rs. Crore)

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Share in Central Taxes	7846.50	8279.96	8518.65	10496.87	12229.09	13964.94	15247.09
Grants-in-aid from central government	4611.02	5158.70	5717.02	6806.25	8152.19	6859.73	8429.42
Non-plan grants	1152.47	1242.00	1629.35	2111.39	2561.48	1505.49	2729.19
Grants for state plan schemes	2231.59	2632.53	2776.74	3279.21	3853.22	3483.61	3429.46
Block grants	2003.85	2393.06	2393.55	3041.05	3451.77	3219.57	3095.50
Grants for central plan schemes	115.62	119.41	167.11	192.01	108.60	183.00	121.67
Grants for centrally sponsored schemes	1111.34	1164.76	1143.83	1223.64	1628.89	1687.63	2149.11

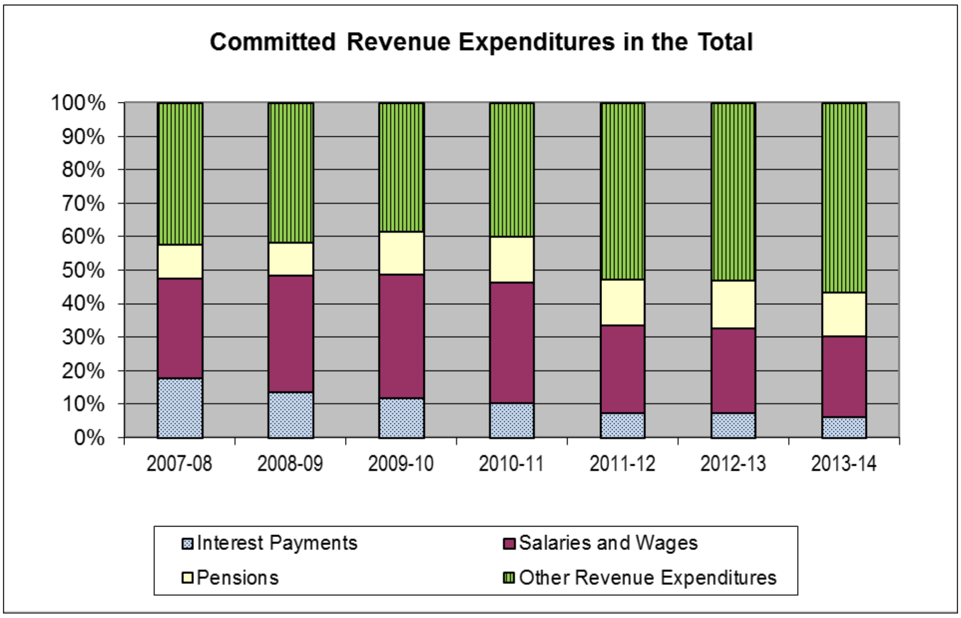
Figure 3



Public expenditures are dominated by revenue expenditures in Odisha, in line with the general trend in India. Total revenue expenditures have generally remained within a band of 14-16 percent of GSDP, in 2013-14, the upper limit was breached and revenue expenditures stood at 16.7 percent of GSDP. The composition of revenue expenditures have improved in recent years in the sense that the share of less directly productive general services has shrunk and those of social and economic services have increased, as can be seen from Figure 3 . This should translate into greater value of public expenditure for the citizens of the state.

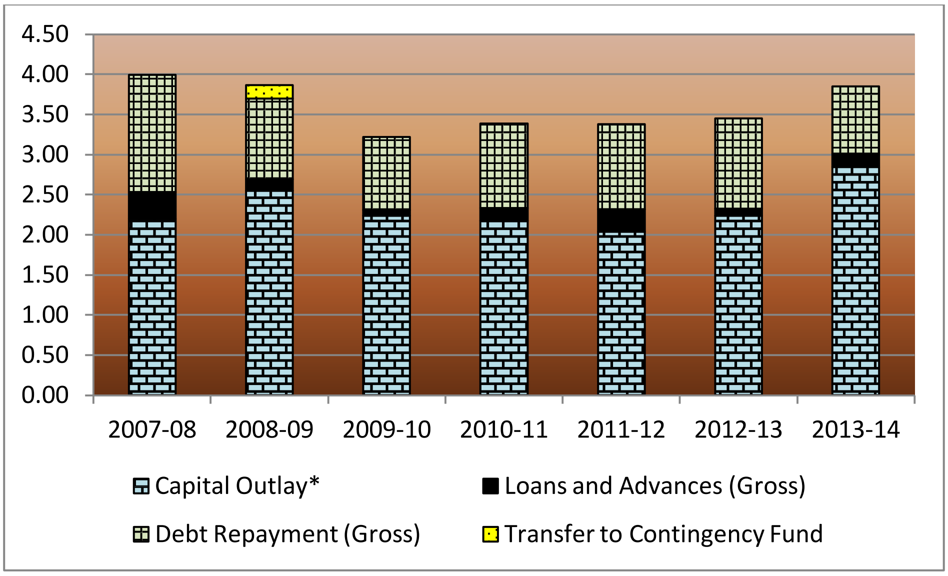
Composition of revenue expenditures has also improved in another way. There is a part of such expenditures that are contractual, committed and pre-determined in nature. The higher the share of such committed expenditures in the total, the less is the discretionary expenditure on providing public services and also, the lower the degree of flexibility available to the government in determining allocation of public expenditures. Since one can observe a substantial reduction in the share of committed revenue expenditures in the total since 2007-08 from almost 60 percent to around 45 percent in 2013-14 (Figure 4), it ought to impart greater flexibility to public expenditure policy in the state.

Figure 4



Capital expenditures, and particularly capital outlay on various services (general, social and economic), have remained low in the state at below 4 percent of GSDP. Public capital expenditures of the right kind have a major role to play in stimulating the rate of growth of the state economy in order to narrow the gap between Odisha and the more developed States, but that role cannot be successfully discharged at such low levels. Within capital expenditures, capital outlay contributes to growth more directly and it is a somewhat positive development that the share of capital outlay has registered an increase in recent years; the increase in 2013-14 is particularly noticeable (Figure 5). However, the level has to be pushed up much higher for a significant growth dividend to be reaped. For this purpose, it would be legitimate to exploit the slack available in fiscal deficit (the gap between the maximum permissible and the actual) to the hilt, and finance identified public investments with high social returns with higher debt, provided the investment projects also meet financial feasibility constraints with adequate rates of return to service the additional debt. This would not hurt fiscal sustainability; problems are caused when debt is incurred to finance revenue expenditures or capital expenditures with inadequate rates of return.

Figure 5: Composition of Capital Expenditure



In terms of indebtedness, the position of Government of Odisha has improved significantly over the years (Table 4). Taking all types of liabilities, the total stock decreased from more than 33 percent of GSDP in 2007-08 to less than half of the same in 2013-14, with indebtedness falling consistently every year throughout the period. Among the various components of total liabilities, the slowest reduction is seen for NSSF loans, although each of the components has registered substantial reduction. The closing level of aggregate indebtedness is well below the level prescribed as prudent by the 13th Finance Commission.

Table 4

Liabilities of Government of Odisha

(% of GSDP)

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
NSSF	5.23	4.59	4.56	4.28	3.85	3.42	3.29
Net Loans from Centre	6.50	5.71	5.05	3.84	3.30	2.87	2.65
Other Public Debt	8.07	6.70	5.98	4.83	4.01	2.99	2.60
State Provident Funds	8.30	7.53	7.56	6.86	6.33	5.84	5.62
Other Liabilities	5.15	5.00	4.84	3.47	4.21	2.29	2.36
Total	33.23	29.53	27.99	23.28	21.70	17.41	16.53

4. Assessment of Compliance to the Provisions made in the State FRBM Act

4.1 Fiscal Achievements and Compliance to the FRBM Act Targets: 2013-14

The review report is required to assess the progress of the State Government in complying with the statutory fiscal targets made in the FRBM Act and review the fiscal management principles enshrined in the Act to conduct the fiscal policy for the year 2013-14. The major objectives of the FRBM Act have been to incentivize fiscal management in order to eliminate the revenue deficit, reduce the fiscal deficit to prescribed level, and contain the debt level at a sustainable level. The major provisions of the Odisha FRBM Act are as follows;

- Present a Medium Term Fiscal Plan (MTFP)
- Undertake appropriate fiscal management principles indicated in the Act to achieve the targets
- Achieve fiscal targets relating to deficit, stock of debt, interest payment, and salary level
- Take suitable measures to ensure greater transparency in the fiscal operation.

Among these provisions, presenting the MTFP in the State legislature and achieving the fiscal targets stipulated in the FRBM Act are statutory requirements. The fiscal transparency measures are stipulated in the rules to the FRBM Act. These are disclosures on fiscal operations and data and information to be given along with the budget to ensure greater transparency. Fiscal management principles enshrined in the

FRBM Act are guiding principles to conduct the fiscal policy in the State to facilitate achievement of the required fiscal targets.

The medium term fiscal plan statement as part of the Medium term Fiscal Policy (MTFP) provides the fiscal stance of the State Government with respect to fiscal targets for the ensuing year, revenue generation efforts, expenditure plan and consequent borrowing requirements. The objective of MTFP is to provide the fiscal plan of the Government to raise the revenues, resource allocation priorities, and borrowing plan for the ensuing year in a transparent way. This statement contains three-year rolling targets for revenue deficit, fiscal deficit, and the debt-GSDP ratio – for the ensuing year, and for two subsequent years. Thus, the first year of the MTFP projections is the budget estimates for the year 2013-14. The MTFP was presented in the assembly along with the budget documents.

The Government of Odisha, as per the FRBM Act, is required to achieve the following mandatory fiscal targets;

1. Attaining zero revenue deficit;
2. Containing the fiscal deficit to 3 per cent of GSDP;
3. Limiting the debt-GSDP ratio to the level fixed by the Central Finance Commission, *viz.* 29.8 percent for the year 2013-14;
4. Keeping the interest payment as percentage of revenue receipts to 15 per cent to maintain sustainable level of debt stock;
5. Limiting the debt stock to three hundred percent of the total revenue receipt of the State;
6. Limiting the ratio of salary to State’s own revenue to 80 per cent; and
7. Limiting the ratio of non-interest committed revenue expenditure to State’s own plus mandated revenues to 55 per cent.

The improvement in fiscal situation in recent years has enabled the State Government to achieve better fiscal outcomes. The fiscal targets specified in the FRBM Act and the outcomes for the year 2013-14 are given in Table 5. The State managed to generate revenue surplus of 1.22 percent and limited the fiscal deficit to 1.70 percent relative to GSDP as against FRBM Act requirements of reducing the revenue deficit to nil and limiting the fiscal deficit to 3 percent. Outstanding debt burden of the State declined substantially to 14.16 per cent relative to GSDP as compared to the prescribed ceiling of 29.8 percent. The debt burden target was fixed by the 13th Finance Commission, which form the benchmark for fiscal management in the State FRBM Act. The interest payment as percentage of revenue receipts, which was 5.9 percent of total revenue receipt remained lower than the prescribed limit of 15 percent. The ratio of debt stock to total revenue receipts at 79 percent was much below the prescribed ceiling of 300 percent. Ratio of salary payments to State's own revenue stipulated to be contained at 80 percent stands at 43.55 percent in 2013.14. Ratio of non-interest committed revenue expenditure to own and mandated revenue at 41.81 percent in 2013-14 remains below the prescribed maximum of 55 percent. The fiscal outcomes for the year 2013-14 reveal that the State Government has achieved the numerical fiscal targets stipulated in the FRBM Act.

Table 5

FRBM Act Targets and Fiscal Achievements during 2013-14

Percent

	Targets	Achievements
Revenue deficit % of GSDP	0	1.22
Fiscal deficit % of GSDP	-3	-1.70
Total debt stock % of GSDP	29.8	14.16
Interest payments % of revenue receipts	15	5.9
Ratio of debt stock to total revenue receipts	300	79.0
Ratio of salary to State's own revenue	80	43.55
Ratio of non-interest committed revenue expenditure to State's own and mandated revenue	55	41.81

The State government has been showing improved fiscal performance in terms of generating substantial revenue surplus, limiting the deficit and debt burden relative to GSDP consistently for several years now. The fiscal performance in 2013-14 continues the achievements of earlier years. The reduction in fiscal deficit and debt burden, significant as they are, raises the question regarding the necessity of the adjustment to such a magnitude. The fiscal correction in previous two years even made the State fiscally surplus; this means a situation where the revenue surplus was more than the capital expenditure. Although, in 2013-14, the fiscal deficit has gone up to the level of 1.70 percent to the GSDP, it remains much lower than the permissible level of 3 percent. The large fiscal space should have been used to push the Government spending, particularly in capital expenditure.

4.2 Fiscal Management Principles

The FRBM Act of the State enunciates a set of fiscal management principles involving debt management and borrowing, tax policy, expenditure policy, and budgetary and other institutional measures. The fiscal management principles are prescribed to help the State Government to achieve the statutory targets. These principles are usually common to the economic policies pursued by the Governments at any level and can be properly assessed only over a reasonably long period with continuous monitoring of relevant fiscal data. Improving efficiency in tax system, pursuing expenditure policies to provide economic growth and poverty reduction, and stabilizing debt burden to achieve fiscal consolidation are policies that form the core of any Government's economic policies. However, it is necessary to assess the recent fiscal policies of the State government keeping these stated principles under consideration.

Debt Management

The overall objective of any Government's debt management policy is to meet financing needs at the lowest possible long-term borrowing costs and to keep the total debt within sustainable levels. The debt management principles of the FRBM Act require the State Government to maintain debt at a prudent level, manage guarantees and other contingent liabilities prudently, and use borrowed funds for productive purposes and create capital assets. The debt stock putting an intergenerational burden ceased to be concern for the State as the debt-GSDP ratio of the State has declined sharply from 43.81 percent in 2004-05 to 14.16 percent in 2013-14. The State Government, over the years, reduced dependence on borrowing to finance State Plan, swapped high cost loans in the past, and prepaid and followed a buy back policy for high cost loans. These measures reduced the interest burden of the State. The State Government also has not resorted to market borrowing to contain net addition to the debt stock for last many years.

The FRBM Act, through the fiscal management principles, calls upon the Government to restrict the guarantee and other contingent liabilities to a specified level and manage it prudently. The guarantees, not part of the conventional debt burden, become the liability in the event of default by borrowing organizations. The State Government has been following the recommendations of the Technical Committee of Finance Secretaries (supported by the Reserve Bank of India), 2002-03, to fix a ceiling on guarantees. There is a limit of 100 per cent of the State revenue receipts of the second preceding year to fix the total outstanding government guarantees. The outstanding guarantee as percentage of revenue receipt net of grant-in-aid has been reduced to 5.31 per cent by 2013-14 (Table 6). The State also constituted a guarantee redemption fund during the year 2002-03 with the objective of meeting the payment obligations arising out of possible default in discharging the debt servicing obligations relating to the loans guaranteed by Government.

Table 6
Outstanding Guarantees

Year	Guarantee Outstanding at the end of the year (Rs. Lakh)	Guarantee Outstanding % of Revenue Receipts less Grants for the 2nd Preceding year	Guarantee as % of GSDP
2004-05	3823.25	57.59	4.92
2005-06	3496.19	45.26	4.11
2006-07	2647.55	27.87	2.60
2007-08	2168.43	19.00	1.68
2008-09	1386.4	9.32	0.93
2009-10	1026.94	5.92	0.63
2010-11	2066.25	10.62	1.05
2011-12	2510.43	12.12	1.14
2012-13	2251.23	8.50	0.90
2013-14	1705.27	5.31	0.62

Source: Finance Account, GoO, Relevant Years

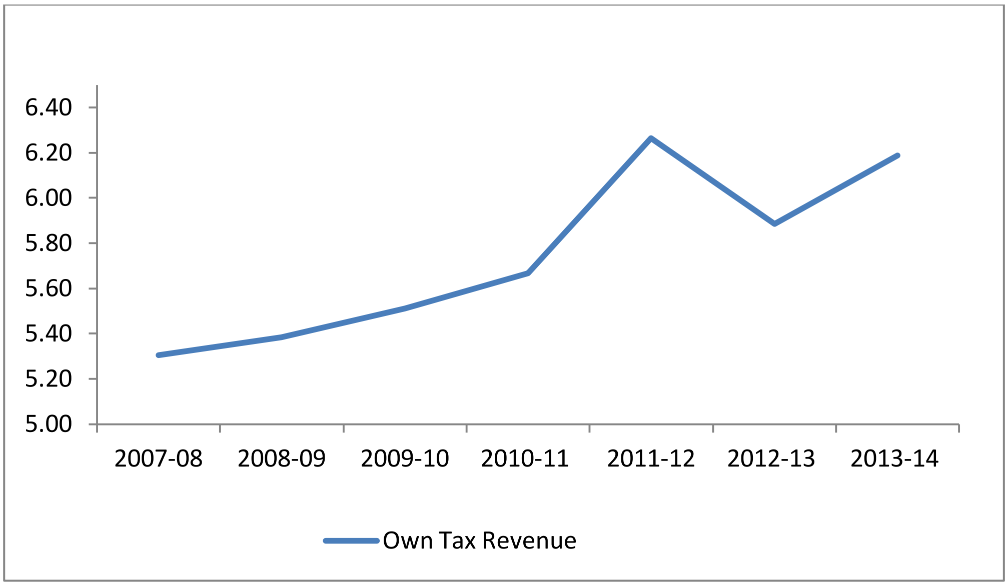
Although the statutory requirement of using borrowed funds exclusively for creating capital assets is satisfied as generating revenue surplus consistently over the years helped to limit the borrowing for capital outlay only, the low-borrowing regime raises concerns in the context of a fiscal policy enabling growth and development. Indeed, borrowing is carried out to finance the deficit arising due to capital outlay and any deficit in the revenue account. A revenue surplus provides greater fiscal space to the Government to increase the capital outlay and keep the debt burden sustainable. Between the years 2007-08 and 2012-13, the capital outlay as percentage of GSDP has remained unchanged at the very low level of 2.20 percent. In 2013-14, there was a marginal change in capital outlay to 2.84 percent relative to GSDP. Given that the fiscal deficit has remained very low as compared to the permissible limit of 3 percent of GSDP, the State Government should go for higher capital outlay. Not resorting to borrowing for markets and reducing net addition to borrowing should not be the benchmark for a development oriented fiscal policy in the face of availability of large fiscal space.

Tax Policy and Administration

The FRBM Act requires the State Government to maintain stability and predictability in the level of tax burden, avoiding incentives, concessions and exemptions, and pursuing the tax policy with due regard to economic efficiency and compliance cost. These form the core of the tax policy of any Government. The own tax revenue as percentage of GSDP shows a smooth rising curve since 2007-08, with a single spike in 2011-12 due to rise in sales tax. There have not been many changes in tax rate of individual State taxes. The VAT regime, introduced in 2005, has stabilized in terms of rate and base structure in the State. The introduction of GST, which has remained uncertain, will bring in changes in the tax system as some of the State taxes like entertainment tax, luxury tax, and entry tax will be subsumed in it along with the VAT. However, every effort needs to be made to improve the tax-GSDP ratio, which has remained at relatively low level compared to many other States of India.

Figure 6

Own tax Revenue as Percentage of GSDP



Economic efficiency in tax system implies that the Government should collect sufficient revenue to carry out its functional responsibilities without distorting market behavior and basic economic decisions of people relative to saving and consumption. The introduction of VAT and stabilization of the rate structure in the State has reduced any discretionary changes in the tax policy. The Government has made efforts to modernize the tax administration and introduced electronic payment taxes, e-filing of returns and generation of Waybills and statutory forms on electronic mode. These are expected to reduce compliance cost. The Government has largely refrained from offering concessions and exemptions that distort the tax system.

The FRBM Act also calls upon the Government to raise non-tax revenue with due regard to cost recovery and equity. The non-tax revenue of the State has evolved as a major source of State revenue as its share in total revenue receipts has steadily increased from about 24 per cent in 2004-05 to 33 percent in 2013-14. About 65 percent of the nontax revenue of the State comes from royalties on mining and quarrying activities. The Central Government takes decisions regarding the royalty rates. The power sector has been privatized in the State and the Government is not a big player in the provision of public transport facility. Thus, subsidy in these two important sectors has been low. The scope for reducing subsidy and improving cost recovery from other services provided by the Government in the social and economic sectors seems to be limited. However, the Government should make efforts to improve cost recovery in economic sectors by improving the quality of the service provided. There has been no major change in the policy of the Government to increase cost recovery from services under social and economic sectors in 2013-14.

Institutional Measures to Improve Quality of Expenditure

The FRBM Act incorporates fiscal management principles relating to improving institutional aspect and processes to improve quality of public expenditure. These include getting value for money from use of public resources, maintaining physical assets, increasing transparency, minimizing fiscal risks associated with public sector undertakings (PSUs), realistic budget formulation to minimize the deviations during the course of the year, and an appropriate cash management practice. The Government has taken several initiatives to improve the quality of public expenditure. These include introducing outcome budget, introducing cash management system, formulating annual maintenance plan, and computerization of treasury activities and integrated financial management system (IFMS).

The Government has introduced outcome budget in number of departments to link outlays to outcomes. Producing desired results from the utilization of public money is the key to the idea of getting best value for money. There are many concerns with regard to the outcome budget introduced in the State. Developing a set of realistic performance information for the programmes, costing the activities, and utilizing the performance information in the programme formation and resource allocation decisions are important ones in this context. If the outcome budget remains an *ex post facto* activity, it will have no major impact in the budget management system and will continue as a routine activity. It is advisable for the State government to assess independently whether the performance information contained in the individual outcome budgets is relevant and adequate, and whether a better integration of the performance indicators with the decisions relating to programme formulation and resource allocation is called for.

The State Government introduced cash management system in 2010-11 to maintain an even pace throughout the year and remove the spikes in the expenditure towards the end of the fiscal year. A sound cash management system helps drawing an effective borrowing calendar and improves predictability of fund flows to spending agencies. The State Government introduced the cash management system initially for 10 departments, which were extended to 18 departments by 2012-13. This system, while giving operational flexibility to the departments, puts a ceiling on spending limit in each quarter and in the last month of the fiscal year. Expenditure during the month of March should not exceed 15 per cent of the budget, and expenditure during the last quarter of the financial year should be within 40 per cent of the budget. The introduction of cash management system has improved utilization of the budgetary allocation and reduced the tendency of ‘March Rush’ considerably. The Comptroller and Auditor General, in their report on state finances for Odisha, observed some cases of higher expenditure exceeding the cash management limit. The State Government should take steps to remove this tendency and ensure that the limit set for the last quarter of the financial years is adhered to by the departments.

The State Government has introduced an Annual Maintenance Plan for the administrative departments for better utilization of the budgeted provision for Operation & Maintenance. The plan indicates the criteria to be followed for allocation of budgeted provision among the functional and administrative units, routine and periodic maintenance, and monitoring and oversight arrangement.

The treasury computerization and IFMS system being worked out by the Government is expected to provide a comprehensive electronic system to facilitate capture of the financial activities of the State Government. The system adopts a life cycle approach, which would envisage accommodating all the processes from preparing estimates to audit. It will help the Finance Department in managing the resources for the state. This system has been designed to provide services to various users such as the finance department, spending departments, field offices, AG (O) and treasuries. A fully operational IFMS will have several other features to integrate the financial transactions relating employees through HRMS, plan finance monitoring system for monitoring of Central schemes, the VLC system for receipt of online accounts, and the RBI for advising electronic payments and receiving scrolls for electronic payments and receipts.

Fiscal transparency measures enunciated in the FRBM Act requires the State Government to minimize the secrecy and disclose data and information relating to the fiscal operations. The Act specifies that the Government should provide information with regard to changes in accounting standards, budgetary documents, and new policies, detailed accounts of fiscal variables, details of employees and salary payments, and revenue, and expenditure details. While the State governments has made most of the information accessible to the general public, some of the information like estimated yearly pension liability and statement showing tax concession and exemptions have not been provided yet. The State Government should furnish this information along with the budget documents in the interest of greater transparency espoused by the FRBM Act.

Other Budget Management Features

To improve budget credibility and preserve the sanctity of the budget voted in the State Legislature the FRBM Act limits the number of supplementary demands to be presented in a financial year to one. The Act also stipulates presenting accompanying statement indicating availability of resources for this supplementary demand through curtailment of expenditure to offset any fiscal impact on fiscal targets to be achieved as envisaged in the Act. Although the State Government managed to limit the budget amendments by presenting a single supplementary budget during the year and managed to meet the fiscal targets as specified in the Act, there are many cases of deviations from the budget estimates. It is important for the State Government to respect the spirit of this provision of the Act and minimize the deviations of actual spending from the budget estimates.

5. Budget Credibility: Projections and Outturns

This section compares the aggregate fiscal outturns for the year 2013-14 to the budget estimates to assess the budget credibility. One of the important fiscal management principles enunciated in the FRBM Act was to formulate the budget in a realistic manner giving due regard to the general economic outlook and realistic revenue projections to minimize deviations during the course of the year. The ability to raise the projected revenue and implement the budgeted expenditure is an important factor that shows the ability of the Government to deliver the public services as enunciated in the Government policies. Table 7 shows the fiscal variables as projected in the budget for the year 2013-14 and the achievements for the year. The fiscal indicators for both the budget estimates and budget outturns are shown as percentages of the GSDP at current prices.

The fiscal outcomes for the year 2013-14 - revenue deficit, fiscal deficit, and debt-GSDP ratio, show that the State Government managed to improve considerably over the budget estimates. The revenue surplus of 1.22 percent relative to GSDP was higher than that of the budget estimate of 0.70 percent, a 0.52 percentage point improvement. Similarly, the fiscal deficit of 1.70 percent relative to GSDP was achieved over the projected level of 2.18 percent. The revenue expenditure has declined by 1.38 percentage points relative to GSDP due to compression of general services as compared to the budget estimates. The aggregate receipts, however, declined by 0.86 percentage points, largely due to decline in central transfers. While own tax revenue fell by 0.26 percentage points, own non-tax revenue registered an increase of 0.57 percentage points as compared to the budget estimates. The capital expenditure utilization, falling short marginally by 0.03 percentage points, seems to be an improvement over the previous years.

Table 7

Budget Estimates and Outturns for the year 2013-14

(Percentage of GSDP)

	2013-14 (BE)	2013-14 Actual	Difference	Diff. % BE
Revenues	18.79	17.93	-0.86	-4.59
Own Tax Revenues	6.45	6.19	-0.26	-4.05
Own Non-Tax Revenues	2.50	3.07	0.57	22.76
Central Transfers	9.84	8.67	-1.17	-11.88
Tax Devolution	5.83	5.59	-0.24	-4.13
Grants	4.02	3.09	-0.93	-23.13
Revenue Expenditure	18.09	16.71	-1.38	-7.65
General Services	6.63	5.02	-1.61	-24.23
Social Services	6.61	6.86	0.25	3.75
Economic Services	4.52	4.51	-0.01	-0.30
Assignment to Local Bodies	0.33	0.33	0.00	-0.39
Capital Expenditure	2.88	2.92	0.04	1.44
Capital Outlay	2.87	2.84	-0.03	-1.07
Net Lending	0.00	0.08	0.07	2046.32
Revenue Deficit	-0.70	-1.22	-0.52	74.79
Fiscal Deficit	2.18	1.70	-0.48	-22.06
Primary Deficit	0.16	0.64	0.48	299.23
Outstanding Debt	16.69	14.16	-2.53	-15.13

Source: Basic data – Finance Accounts and Budget Document for the year 2013-14, GoO
GSDP data used are of 2004-05 series

The actual debt-GSDP ratio of 14.16 percent in 2013-14 was lower than the budget estimate of 16.69 percent relative to GSDP. The actual borrowing during the year both from the market and from the central Government has been less than what has been planned for in the budget estimates. The net debt incurred during the year was Rs.686.10 crores, as against the budget estimate of Rs.4985.60. This has helped reducing the debt burden relative to GSDP. Table 8 shows the debt receipts and repayments from various sources during 2013-14.

Table 8

Borrowings and Repayments: 2013-14

(Rs. Lakh)

	Budget Estimates	Actual	Difference
Public Debt Receipts			
Internal Debt	608495	173966	-434529
Loans Advances from Central Government	71934	55060	-16874
Public Debt	680429	229026	-451403
Small Savings and Provident Fund	325047	333233	8186
Total	1005476	562259	-443217
Debt Repayments			
Internal Debt	227541	177531	-50010
Loans Advances from Central Government	54328	51790	-2538
Public Debt	281869	229321	-52548
Small Savings and Provident Fund	225047	264327	39280
Total	506916	493648	-13268

Source: Finance Accounts and Budget Document for the year 2013-14, GoO

The State Government managed to achieve higher revenue surplus and reduced the fiscal deficit and debt stock as compared to the budget estimates. The fiscal outcomes of the year 2013-14, however, remained much below the permissible limits imposed by the FRBM Act. The fiscal space available to the Government has not been utilized properly, as the capital expenditure continues to remain low. However, during the fiscal year 2013-14, the State government has attempted to improve the capital outlay as compared to the last two years. During 2011-12 and 2012-13, the revenue surplus, as percentage of GSDP, was much higher and fiscal deficit was much lower. This trend of raising capital expenditure should gain momentum and the Government should not shy away from borrowing from market. The government should reverse the policy of not borrowing from the market, when the revenue surplus is substantial and the fiscal deficit is lower than the FRBM Act ceiling.

5.1 Disaggregated Analysis of Revenue Receipts

Data on detailed sources of revenue shown in Table 9 reveal that the actual own tax revenue fell short of the budget estimate in 2013-14. The actual collection of taxes like sales tax, taxes on vehicles, land revenue, stamps and registration fees, profession tax, and other taxes has declined as compared to the budget estimates. Lower realization of tax revenue as compared to the budget estimates raises questions on efficiency of projection methodology and assumptions taken on macroeconomic conditions. The actual collection from land revenue fell short of the budget estimates by 52 percent. The planned levy of stamp duty on renewal of license fees on mining lease was stayed by the judiciary, because of which the projected revenue could not be realized. However, compared to the previous year, the own tax revenue has grown at about 12 percent.

Table 9
Revenue Realization

	2012-13	2013-14 (BE)	2013-14	Diff.	% Change over Budget	% Change Over 2012-13
Revenues	4393691	5129898	4894685	-235213	-4.59	11.40
Own Tax Revenues	1503413	1760500	1689158	-71342	-4.05	12.35
Sales Tax	968468	1109500	1072855	-36645	-3.30	10.78
State Excise Duties	149864	172500	178013	5513	3.20	18.78
Motor Vehicle Tax	74619	90000	85967	-4033	-4.48	15.21
Goods and Passengers tax	134254	150000	161345	11345	7.56	20.18
Electricity Duty	59048	64000	67011	3011	4.71	13.49
Land revenue	42021	90000	43126	-46874	-52.08	2.63
Stamp Duty and Regi. Fees	54488	62000	60548	-1452	-2.34	11.12
Profession tax	13599	16000	14970	-1030	-6.44	10.08
Other Taxes	7052	6500	5322	-1178	-18.12	-24.53
Own Non-Tax Revenues	807803	682500	837860	155360	22.76	3.72
Interest Receipts	58825	30000	124118	94118	313.73	111.00
Dividends and Profits	56453	23000	45240	22240	96.70	-19.86
General Services	36342	12870	28790	15920	123.70	-20.78
Miscellaneous General Services of which	22560	1100	12650	11550	1050.01	-43.93
Social Services	19058	14180	20713	6533	46.07	8.68
Education, Sports, Art & Culture	8910	1663	7586	5923	356.18	-14.85
Economic Services	637125	602450	618999	16549	2.75	-2.84
Forestry and Wildlife	18892	3022	9511	6489	214.78	-49.66
Major Irrigation	29114	8500	30846	22346	262.90	5.95
Medium Irrigation	9645	28400	12785	-15615	-54.98	32.55
Mining Royalties	569570	551500	551880	380	0.07	-3.11
Roads and Bridges	5912	7200	6907	-293	-4.07	16.83
Central Transfers	2082475	2686898	2367666	-319232	-11.88	13.69
Tax Devolution	1396501	1590388	1524725	-65663	-4.13	9.18
Grants	685973	1096510	842942	-253568	-23.13	22.88

Actual receipts from own non-tax revenue increased by 22.76 percent over the budget estimates during the year 2013-14. While both the own tax revenue and central transfers declined over their budget projections, it was because of the performance of the non-tax revenues that the State managed reduced the severity of the decline of total revenue. Some of the sources of non-tax revenue seem to have been under projected at budget estimate level, which actually ended up with larger realization. This practice should be discouraged and an unbiased estimate of revenue sources should be included at the budget estimate level.

The interest receipt showing a large increase as compared to the budget estimates was due to a one-time settlement of arrears against interest receivable from the GRIDCO and other discoms. This is a pure book transfer and has been shown in revenue expenditure side. In the case of miscellaneous general service, interest relief from central Finance commission was not budgeted due to its uncertainty, which was realized during the year. In the case of Education, Art & Culture, showing higher collection as compared to the budget, the income from SSA was not budgeted and was realized during the year. In the case of Forestry and Wild Life, which show large increase in revenue collection as against the budget estimates, the amount pertaining to payment to Kendu Leaf workers for previous years was not budgeted and was realized during the year 2013-14.

In the case of central transfers, the actual realization was lower than the budget projection by 11.88 percent. Both the components of central transfers, share in central taxes and grants show decline as against the budget estimates. The actual receipt of central grants fell short of the budget estimates by a whopping 23.13 percent. The Finance Department, in their submission indicated that central grants under many heads included in the budget estimates were not received or a smaller amount was received during 2013-14.

5.2 Disaggregated Analysis of Expenditure Pattern

Table 10 shows the decomposed expenditure pattern for the year 2013-14. The revenue expenditure was compressed by 7.65 percent as compared to the budget estimates. The compression in revenue expenditure was driven by decline in expenditure on general services. While the expenditure under social services was higher by 3.75 percent, the decline in economic services is minimal. In the general services, the decline was largely attributable to lower interest payment as compared to the budget estimates. The difference between budget estimates and actual interest payments should not be large as the debt stock of the previous year was already known by the time budget was prepared. From the data, it is clear that excess provision under this head during budgeting stage was the main reason for savings to the extent of 42.33 percent.

Although the aggregate social services show higher spending as compared to the budget estimates, leaving the head Social Welfare and Nutrition, all other components shows lower spending during the year. The budgeted amount for priority sectors like education, health, water supply and sanitation, welfare of SC, ST, and BC, and other social services was not fully utilized. Deviation in utilization of revenue expenditure points to weak programme management in these sectors. While the deviations from budget estimates under these heads were small, the deviation for health is rather high at 9.56 percent. The higher expenditure in the case of social security and welfare was due to payment of pensions to additional beneficiaries identified during the year and additional expenditure for welfare of the people affected by the cyclone.

Although expenditure on economic services show a marginal reduction during the year as compared to the budget estimates, the components of economic services show varying trends. While the higher expenditure in rural development was due to reorganization of accounting heads, higher expenditure in minor irrigations was due to payment of electricity duty, which was a book transfer. The variations in actual expenditure from the budget estimates indicate strengthening budget management system and proper programme formulation.

The capital expenditure utilization in the year 2013-14 has improved as compared to the previous year. While in 2012-13, about 20 percent of the budgeted amount remained unutilized, it has come down to 1.07 percent in 2013-14. The capital expenditure as percentage to GSDP has also increased from 2.24 percent in 2012-13 to 2.84 percent in 2013-14. Though inadequate, as compared to the large fiscal space available to the Government, it shows an increasing trend. Given the need for expanding infrastructural facilities in the State, proper utilization of budgeted provisions for capital expenditure should have been given emphasis. The capital expenditure in the State has been suffering from basic problems like lack of capacity in the area of project appraisal, inadequate capacity for project execution, lack of a medium term sector vision and lack of prioritization. Often, considerable time is lost in identifying suitable infrastructure projects, though funding may not be a problem.

Table 10
Expenditure Profile

	2012-13	2013-14 (BE)	2013-14	Diff.	% Change over Budget	% Change Over 2012-13
Revenue Expenditure	3823756	4939437	4561773	-377664	-7.65	19.30
General Services	1242326	1810330	1371648	-438682	-24.23	10.41
Interest Payment	280723	500786	288822	-211964	-42.33	2.89
Pension	537937	672800	593517	-79283	-11.78	10.33
Other General Services	423666	636744	489309	-147435	-23.15	15.49
Social Services	1497656	1804419	1872155	67736	3.75	25.01
Education	726307	870385	828237	-42148	-4.84	14.03
Medical and Public Health	168117	200419	181258	-19161	-9.56	7.82
Water Supply	110798	164758	158514	-6244	-3.79	43.07
Welfare of SC, ST, & BC	119010	143288	133015	-10274	-7.17	11.77
Social Welfare & Nutrition	353258	393681	541656	147975	37.59	53.33
Other Social Services	20165	31888	29476	-2412	-7.56	46.17
Economic Services	1019624	1235116	1231457	-3659	-0.30	20.78
Agriculture & Allied	410423	474332	470110	-4221	-0.89	14.54
Rural Development	217870	287097	298363	11266	3.92	36.95
Irrigation & Flood Control	104322	127799	139705	11906	9.32	33.92
Energy	1620	2612	2235	-378	-14.45	37.94
Industry and Minerals	25451	38700	30570	-8130	-21.01	20.11
Transport	156168	166347	170477	4130	2.48	9.16
Science Technology	5632	11393	6586	-4806	-42.19	16.94
General Economic Services	98138	126836	113411	-13426	-10.59	15.56
Assignment to Local Bodies	64149	89571	89220	-352	-0.39	39.08
Capital Expenditure	562218	784013	775640	-8372	-1.07	37.96

The excess cash balance position of the State Government, shown in Table 11, reveals that the cash balance has declined during the year 2013-14 as compared to the previous year. Large cash balances helped the State Government in reducing its dependence on open market borrowing and discharging some high-cost loans. Although, the cash balance position has shown some decline in 2013-14, it provides a useful cushion to the State Government. There were earlier suggestions by the 12th Finance Commission and RBI also to this effect (to utilize the existing cash balances efficiently).

Table 11

Cash Balance Position and Investments

(Rs. Lakh)

	As on 31 March 2014	As on 1 April 2013
General Cash Balance		
Deposits with the Reserve Bank	2687.15	(-2392.38
Investments held in the Cash Balance - Investment account	392702.21	734180.70
Total	395389.46	731788.41
Other Cash Balances and Investments		
Cash with Departmental Officers	2154.99	2346.57
Permanent Advances for Contingent Expenditure with Departmental Officers	32.71	31.69
Investments of Earmarked Funds	552300.00	552300.00
Total	554487.70	554678.26
Grand Total	949877.16	1286466.67

Source: Finance Accounts – 2013-14

6. Concluding Remarks

State finances of Odisha have been managed quite conservatively over the last ten years, as was perhaps called for in view of the unsustainable fiscal stance of earlier years. As such, the State has been able to meet the specific FRBM Act targets with ease, though some of the transparency requirements are yet to be met. The latter shortcomings are generally traceable to lack of an established system for generating and compiling the necessary information as also inter-departmental co-ordination rather than to willful withholding. But it is important to remember that the overarching objective of any government is to provide good governance and improve the quality of life of its citizens. In the larger picture, statutory checks and balances, of which the FRBM Act is one, are only the guideposts; a government would remain within the requirements of such statutory checks without any special effort if it was honestly and intelligently discharging its primary duty of good governance. It would be a mistake to consider the statutory checks and balances as ends in themselves.

In the specific case of Odisha, the relatively less developed status of the State widens the concept of good governance to include delivery of socio-economic development for its citizens. This requires government initiatives in several areas that would conceptually be the opposite of conservatism. The admittedly difficult task that the government then has to perform is to maintain the right balance between the opposites of conservatism and developmental initiatives, which would constitute the essence of good governance in a State like Odisha. In our specific context, this would relate to remaining within the contours of fiscal prudence as detailed by the provisions of the FRBM Act, but not allowing that to overwhelm developmental initiatives that the government owes its citizens.