# A Study of the State Budget: Collection and Allocation in India post COVID-19

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## Introduction

Revenue refers to the money received or earned by the government. These can be capital receipts or revenue receipts. Revenue Receipts are those receipts that need not be paid again to the payee from the government and do not impact the liabilities of the government.

Although the constitution provides state governments with expenditure responsibilities, a significant proportion of the State's revenue sources lie with the Union Government. States' revenues largely come from indirect taxes on transport fuel, vehicle sales, alcohol, real estate transactions, and electricity. In contrast, the Union government largely relies on direct taxes on personal and corporate income, manufacturing, and imports.

Four new changes to India's fiscal structure has put State finances in an insecure situation.
These are (i) the introduction of GST (ii) restructuring of Centrally Sponsored Schemes (iii) the need to adjust to other fiscal shocks and (iv) the institution of the 15th Finance Commission and the submission of its first interim report in February 2020.

Goods and Services Tax (GST) is an indirect tax (or consumption tax) used in India on the supply of goods and services. It is a comprehensive, multistage, destination-based tax: comprehensive because it has subsumed almost all the indirect taxes except a few state taxes. The tax is imposed on every stage of production, but is meant to be refunded to all parties in the various stages of production other than the final consume. a shortfall in tax collection below this estimated level is paid as GST compensation to the States by the Union. However, the compensation is expended from the collections made through a GST Compensation Cess - an additional levy on goods that attract 28 per cent GST.

The restructuring of CSS in order to accommodate the increase in tax devolution to States to 42 per cent from 32 per cent recommended by the 14th Finance Commission was another reason. In October 2015, for several schemes including the National Health Mission, Rashtriya Swasthya Bima Yojana, National Rural Drinking Water Programme, Pradhan Mantri Awas Yojana, and the Samagra Shiksha, the Union government changed the funding pattern from 75:25 to 60:40 for General Category States, while the share remains unchanged at 90:10 for the North-Eastern and Himalayan States. Hence, part of the autonomy given to States in the form of increased devolution has been curtailed by the rise in States' contribution towards CSSs. Many Ministries have been asked to restrict their overall expenditure to 20 per cent of the Budget Estimates (BEs) for the year; several others may spend only up to 15 per cent of the BEs. Budget Estimates (BEs) are the estimates put forth by the government for any department or scheme under various major heads for the upcoming financial year.

Even before COVID-19, the state finances had to adjust to other fiscal shocks constraining their finances. Under the scheme, States were to take over 75 per cent of the DISCOM debt as on September 30, 2015 50 per cent in FY 2015-16 and 25 per cent in FY 2016-17. Finally, FY 2020-21 also saw the institution of the 15th Finance Commission and the submission of its first interim report in February 2020. Key aspects of the report dealt with an adjustment in the formula for devolution of taxes from the Union to the States, provision of Grants-in-Aid (GIA), proposal for sector-specific and performance-based grants, and recognition of challenges in GST implementation.

I have studied the revenue and expenditure performance of 17 States to unpack the status of State finances prior to the outbreak of COVID- 19 with a view to envision the fiscal impact from the pandemic, and discuss possible ways forward for the States. In the rest of the paper, I would explain the methodology, undertake a discussion on different components of State revenue receipts and discuss state expenditures. That would be followed by a conclusion and a bibliography

## Methodology

The present study on State finances assesses the flow of resources to State governments and their utilisation. My sample focuses on 17 States that have released their State budgets in the public domain for the current financial year, FY 2020-21. The 17 States include Assam, Bihar, Chhattisgarh, Gujarat, Haryana, Jharkhand, Karnataka, Kerala, Maharashtra, Mizoram, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, Uttarakhand, and West Bengal.

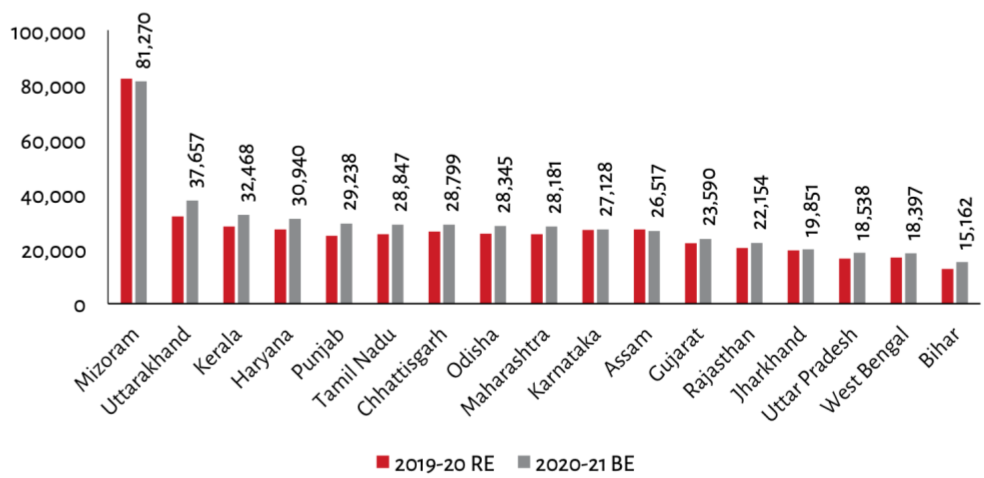
The data is sourced from State government websites and the documents uploaded on them. These may include press releases and press information bureau. Budget Estimates (BEs) are the estimates put forth by the government for any department or scheme under various major heads for the upcoming financial year. During the year, based on an estimation of expenditures, States compute Revised Estimates (REs). These REs can be either lower than the BEs if actual expenditure till October or anticipated expenditure till March is expected to be less than originally budgeted or higher if the grants budgeted at the start of the year fall short of expenditure requirements. In the latter case, demands for additional grants are placed in front of the Parliament which are then looked into and passed by the Parliament during the financial year itself.

Actuals represent the actual expenditures by the government in a given financial year. Since actual expenditures can be assessed only after the financial year has passed and are audited by the Comptroller and Auditor General (CAG), these figures are released by the government with a time lag of two years.

## Per-capita revenue receipts

Per-capita revenues receipts or the revenue receipt generated per person in a State is calculated as the total revenue of a State divided by the population of that State. For population figures, we have used the recent projections by the Technical Group on Population Projections published by the Ministry of Health and Family Welfare.5
For the States analysed here, the average revenue per- capita for FY 2020-21 BE is ₹29,240. There are, however, significant differences across States. Mizoram has the highest per-capita revenue among the States analysed with ₹81,270, followed by Uttarakhand with ₹37,657, Kerala with ₹32,468, and Haryana ₹30,940. In contrast, per-capita revenues of Bihar were ₹12,662 for FY 2019- 20 RE and ₹15,162 for FY 2020-21 BE.

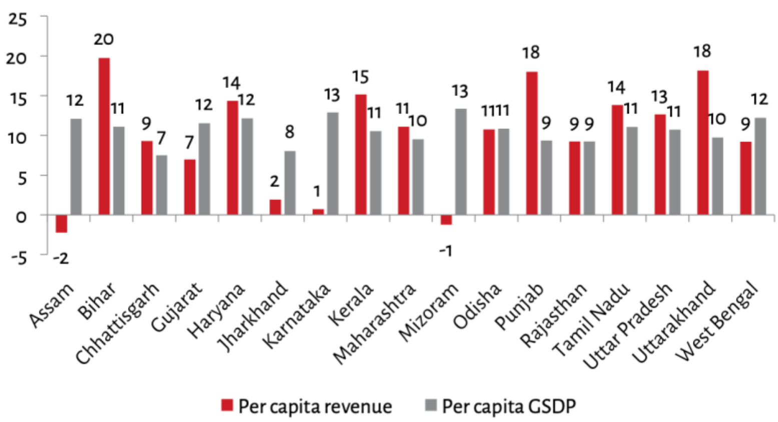
**Figure 1: Total Revenue Receipts Per-Capita for FY 2019-20 RE and FY 2020-21 BE**




Between FY 2019-20 RE and FY 2020-21 BE, on average, per-capita revenue receipts were expected to grow at a rate of 8 per cent. States with a higher expected growth rate included Bihar (20 per cent), Punjab (18 per cent), and Uttarakhand (18 per cent). In contrast, growth rates were expected to be less than 10 per cent in Karnataka, Jharkhand, Gujarat, Chhattisgarh, Rajasthan, and West Bengal. Worryingly, States such as Assam and Mizoram indicate a negative growth in per-capita revenue receipts.

A comparison with growth in per-capita GSDP indicates that the expected increase in per capita revenue receipts was higher than the expected increase in GSDP for nine out of the 17 States analysed. These include Bihar, Chhattisgarh, Haryana, Kerala, Maharashtra, Punjab, Tamil Nadu. Uttar Pradesh and Uttarakhand. Past analysis of revenue receipt estimations of States, however, indicate that there are differences between the revenue receipts estimated and the actual revenue received or earned. In FY 2018-19 for instance, seven out of the 17 States - including Gujarat, Karnataka, Maharashtra, Odisha, Tamil Nadu, Uttar Pradesh, and West Bengal - had reported BEs to be 5 per cent higher than the Actuals for the year. In fact, Mizoram was the only State to report higher Actuals than BEs by 2 per cent.

**Figure 2: Growth Rate of Per-Capita Revenue Receipts in Comparison to Growth Rate of Per-Capita GSDP between FY 2019-20 RE and FY 2020-21 BE**

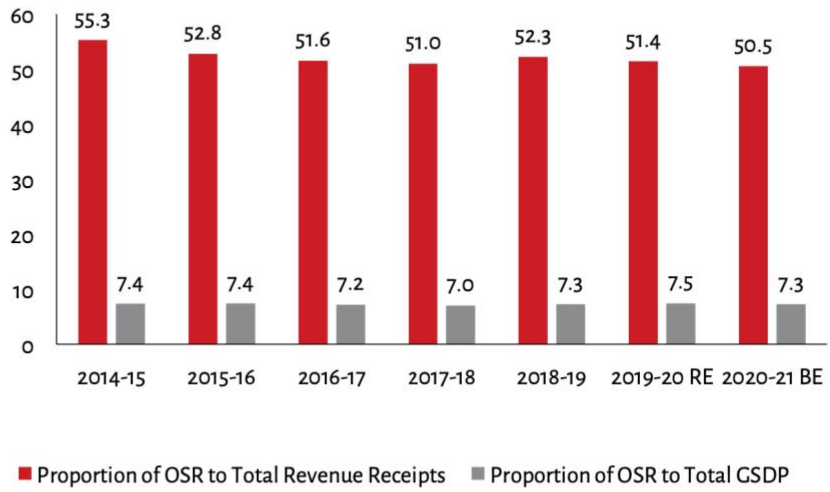



Broadly, revenue receipts of States comprise revenue from own sources and transfers from the Union government, including devolution of taxes and Grants- in-Aid. This distinction on the nature of revenue receipts gains importance because although State governments do not have much influence over Union form a significant share of total receipts enjoy relatively more flexibility in financing their development needs

## Own Source Revenues

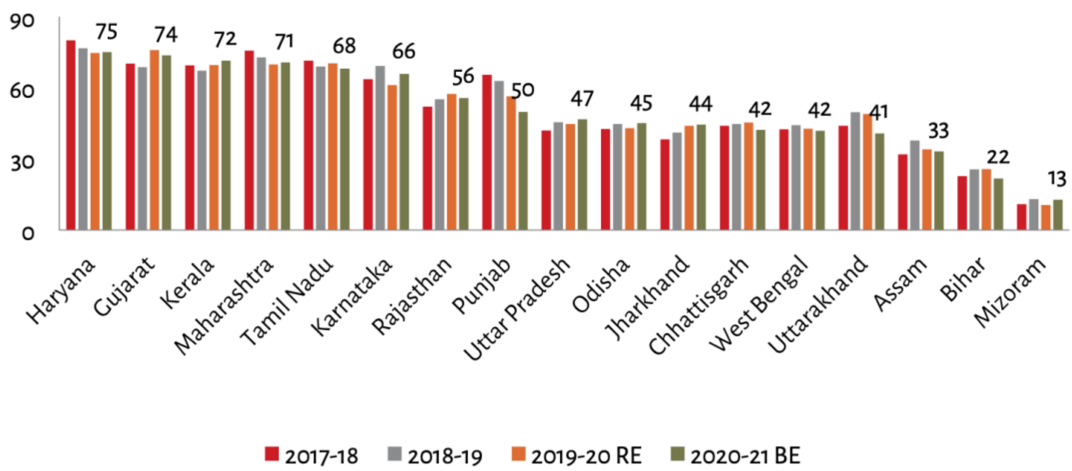
Own Source Revenues (OSR) comprise the tax and non- tax receipts of State governments. States‟ own tax revenue comes overwhelmingly from indirect taxes as the power to impose direct taxes rests with the Union government. Following the implementation of the GST - barring a few exceptions like petroleum products, property tax, and alcohol excise - indirect taxes have, to a large degree, been subsumed under the GST regime. Non-tax revenue, on the other hand is the recurring income earned by the State governments other than taxes, such as interest payments (received on loans given by the State government to Railways, or to other States, etc.), and dividends and profits received from the public sector companies. Additionally, various services provided by the government, such as police and defence, social and community services, and economic services also yield revenue for the government. From the perspective of States, the analysis illustrates that while around half of States‟ revenue is derived from OSR, it has seen a marginal decline over the years, indicating their increasing fiscal dependence on the Union government. For instance, in FY 2014-15, on average, OSR accounted for 55 per cent of total revenue receipts. However, FY 2020-21 BE, witnessed the lowest proportion of OSR out of total revenues at 50.5 per cent - over 4 percentage points lower than in FY 2014-15. transfers, the States where revenues from own sources

Figure 3: Proportion of OSR to Total Revenue Receipts and GSDP




A State-wise analysis of the same for our 17 States indicates that as per FY 2020-21 BE, the States with a higher share of OSR out of total revenue receipts were Haryana (75 per cent), Gujarat (74 per cent), Kerala (72 per cent), and Maharashtra (71 per cent). In contrast, fiscally poorer States such as Mizoram, Bihar, Assam, Uttarakhand, West Bengal, and Chhattisgarh are more dependent on transfers from the Union government, with low share of own tax and non- tax revenues.

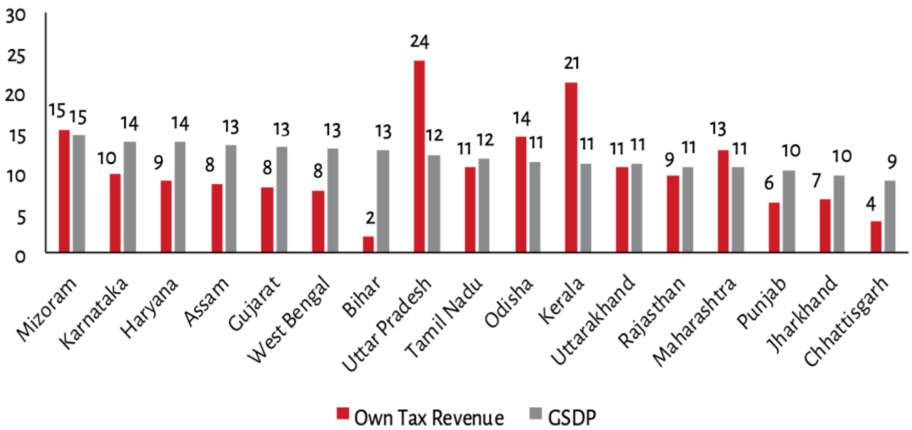
Figure 4: Own State Resources out of Total Revenue Receipts




## Growth Rate of Own Tax and Non-Tax Revenue in Comparison with GSDP

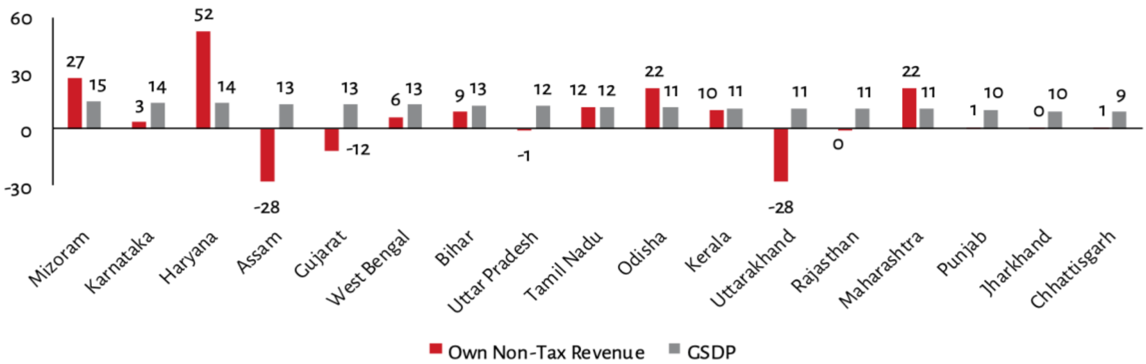
A comparison with GSDP growth rate indicates that four of the 17 States analysed - namely Uttar Pradesh (24 per cent), Kerala (21 per cent), Maharashtra (13 per cent), and Odisha (14 per cent) - expected a higher growth of own tax revenue in comparison with the growth rate of GSDP. Assuming that while the quantum may decrease but the trend continues, these States may have the potential to increase their tax-to- GSDP ratio, giving them relatively greater fiscal room.

**Figure 7: Growth Rate of Own Tax Revenue in Comparison with GSDP for FY 2019-20 and FY 2020-21 BE**




With relatively less unpredictability in non-tax revenues, States which reported an expected higher growth rate in non- tax revenues include Haryana (52 per cent), Mizoram (27 per cent), and Odisha (22 per cent). In contrast, States such as Assam, Uttarakhand, Gujarat, and Uttar Pradesh reported negative growth rate, while Jharkhand and Rajasthan have reported no growth during the period between FY 2019-20 RE and FY 2020-21 BE. In four States - namely, Haryana, Maharashtra, Mizoram, and Odisha - own non-tax revenue has grown at a higher rate in comparison to GSDP.

**Figure 8: Growth Rate of Own Non-Tax Revenue in Comparison with GSDP for FY 2019-20 and FY 2020-21 BE**



## Conclusion

There may be a need to seriously rethink the current design of social policy financing. One way that the Union government can support this is through a redesign of CSSs as an instrument of GIA by ensuring greater flexibility to States. A note published by the Centre for Policy Research outlines the mechanics of this in detail.42 Briefly, this can be achieved by bundling together GIA through these schemes into an untied grant for States without being constrained by Central guidelines and numerous conditionalities. Funds currently budgeted for non-core COVID-19 activities (i.e., excluding health, labour, and social protection), and unspent balances available for several CSSs could be used to create this COVID grant. While the Union government has recently announced that it would not remove the State share,43 one option could be to redesign the State share as a long term zero-interest loan to be repaid when the crisis abates – probably in FY 2021-22.

To guide the mechanics of Centre-State financing and the need for a coordinated response, keeping in mind State-specific situations also calls for the establishment of a new institutional mechanism to deal with Centre- State issues. One such body could be a specially created National Empowered Emergency Disaster Council (NEED Council) comprising Chief Ministers, the Prime Minister and senior Union Ministers. The NEED Council could be supported by the National Disaster Management Authority and be responsible for creating a predictable and equitable, COVID-specific funding window (including ensuring additional resources through NRDF and SRDF) and be responsible for ensuring monitoring and reporting of expenditures.

Analysis demonstrates that following the 14th FC recommendations and the subsequent increase in States‟ share of the divisible pool of taxes, the proportion of taxes devolved to States out of their total revenues increased between 2015 and 2019.

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9. Report of the 15th Finance Commission for the Year 2020-21. November 2019. New Delhi. Retrieved via URL on 9 May 2020: <https://fincomindia.nic.in/ShowPDFContent.aspx>


State Finance Data Links

1) Assam - https://finassam.in/budget_documents/
2) Bihar - http://finance.bih.nic.in/
3) Chhattisgarh - http://finance.cg.gov.in/budget_doc/Budget.asp
4) Gujarat - https://financedepartment.gujarat.gov.in/Budget.html
5) Haryana - http://www.finhry.gov.in/State-Budget12
6) Jharkhand - https://finance-jharkhand.gov.in/budget2020.aspx
7) Karnataka - https://www.finance.karnataka.gov.in/english
8) Kerala - http://www.finance.kerala.gov.in/bdgtDcs.jsp
9) Maharashtra - https://beams.mahakosh.gov.in/Beams5/BudgetMVC/MISRPT/MistBudgetBooks.jsp?year=0
10) Mizoram - https://finance.mizoram.gov.in/
11) Odisha - https://finance.odisha.gov.in/Budget.asp?GL=Budget&PL=1&TL=1&FL=1
12) Punjab - http://pbfinance.gov.in/state-budget
13) Rajasthan - http://finance.rajasthan.gov.in/aspxfiles/statebudget.aspx
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