

CHAPTER - XI

FISCAL IMBALANCES: DIMENSIONS, ISSUES AND IMPLICATIONS

Correcting fiscal imbalances today is the single most important task of the State Governments in the face of galloping revenue deficits and burgeoning public debts. A number of measures towards this end have already been initiated by different States, particularly after the MoU signed with the Central Government and the recommendation of the Eleventh Finance Commission, which has recommended debt relief linked to fiscal performance. It is true that there is no second opinion for the need of correcting fiscal imbalances of the States, as the increasing imbalance would hamper the development of the States. However, in order to correct the fiscal imbalances there is a need to discuss the issues linked to the problem. The present chapter makes an attempt to find the magnitude of the fiscal problem faced Orissa and discusses various issues to address the problem.

MAGNITUDE OF THE PROBLEM

Orissa is currently undergoing a situation of severe financial crunch. It has moved from a revenue-surplus State in 1983-84 to a revenue-deficit State. The revenue account of the State is progressively deteriorating over the years. This is basically due to rapid increase in revenue expenditure than in revenue receipts. The revenue deficit of the State has increased from Rs.73.74 crore in 1984-85 to Rs.2573.57 crore in 1999-00, which then declined to Rs.1926.76 crore in 2000-01 (Table 11.1). Its share in the NSDP has gone up from 1.42 per cent in 1984-85 to 8.46 per cent in 1999-00 and 5.63 per cent in 2000-01. Like the revenue deficit, the fiscal deficit of the State is also increasing at a galloping rate. From only Rs.269.04 crore in the year 1980-81, the fiscal deficit has reached to a level of Rs.8055.57 crore in 1999-00, which again increased to Rs.9228.53 crore in 2000-01. The revenue deficit as a percentage of fiscal deficit has gone up from 7.44 per cent in 1984-85 to 38.76 per cent in 1998-99 and then declined to 20.88 per cent in 2000-01, indicating that the revenue deficit, not the fiscal deficit, is the major headache of the State.

Table - 11.1**Revenue Deficit and Fiscal Deficit**

(Rs. in Crore)

Year	Revenue Receipts	Revenue Exp.	Revenue Surplus(+)/ Deficits(-)	NSDP (Current Prices)	Revenue Deficit as % of NSDP	Fiscal Deficit	Rev. Deficit as % of Fiscal Def.
1980-81	621.35	546.85	74.50	3442.69	--	269.04	-
1985-86	940.84	1000.93	-60.09	6225.73	0.97	733.49	8.19
1990-91	2170.94	2190.53	-19.59	9664.28	0.20	1515.12	1.29
1995-96	3890.71	4697.81	-807.10	21462.79	3.76	2071.49	38.96
1996-97	4286.76	5117.25	-830.49	20635.89	4.02	3811.36	21.79
1997-98	4632.03	5536.48	-904.45	24104.98	3.75	4687.69	19.29
1998-99	4554.40	6816.90	-2262.50	27086.62	8.35	5837.34	38.76
1999-2000	5884.64	8458.51	-2573.87	30437.07	8.46	8055.57	31.95
2000-01	6907.23	8833.99	-1926.76	34201.95	5.63	9228.53	20.88

Note: NSDP from 1980-81 to 1997-98 are old series figures and the rest are projected figures.

Source: Orissa Budget (2001-02) at a Glance, Finance Department, Govt. of Orissa;

For NSDP, Economic Survey of Orissa, various issues.

The revenue deficit of Orissa has not only increased at a rapid rate over time, but also has remained higher than many other States. During the year 1997-98, the revenue deficit of Orissa was more than all the major low-income States, except Uttar Pradesh (Table 11.2). Considering the share of revenue deficit in NSDP, Orissa with a share of 3.75 per cent was the second highest among the 14 major States. Uttar Pradesh was the only State with higher proportion of revenue deficit than Orissa. All the other major States have lower proportion of revenue deficit compared to Orissa. This is a major cause of concern as far as the finance of Orissa is concerned.

Table - 11.2

Fiscal Position of 14 Major States (1997-98)

State	Revenue Deficit (Rs. in Crore)	NSDP at Current Prices (Rs. in Crore)	Revenue Deficit as % of NSDP
Low Income States			
Bihar	263.90	46219.40	0.57
Madhya Pradesh	469.30	61018.78	0.77
Orissa	904.50	24104.98	3.75
Rajasthan	581.80	46346.20	1.26
Uttar Pradesh	4623.90	113104.80	4.09
Middle Income States			
Andhra Pradesh	703.20	78705.41	0.89
Karnataka	276.80	57952.00	0.48
Kerala	1122.90	38002.42	2.95
Tamil Nadu	1363.90	77302.27	1.76
West Bengal	2294.10	80664.76	2.84
High Income States			
Gujarat	1017.80	725335.34	0.14
Haryana	719.40	36274.60	1.98
Maharashtra	2579.90	164576.71	1.57
Punjab	1483.90	44789.13	3.31

Source: *State Finances: A Study of Budgets of 1999-00*, R.B.I., Jan. 2000.

The galloping revenue deficit of Orissa is due to the fact that revenue expenditure is increasing at a faster rate than the revenue receipts. Over a period of 20 years from 1980-81 to 1999-2000, the revenue expenditure grew at an annual compound rate of 15.40 per cent as compared to the growth of revenue receipts at 13.37 per cent (Table 11.3). While the growth rate of revenue expenditure has increased marginally from 14.66 per cent in the 1980s to 15.03 per cent in the 1990s, the growth of revenue receipts has declined drastically from 12.83 per cent per annum in the 1980s to 10.58 per cent in the 1990s. Hence, both the higher growth of revenue expenditure as compared to the revenue receipts and the slow down in the growth of revenue receipts are responsible for the fiscal imbalance in the State.

Table - 11.3**Annual Compound Growth of Revenue Receipts and Revenue Expenditure**

(In %)

Period	Revenue Receipts	Revenue Expenditure
1980-81 to 1989-90	12.83	14.66
1990-91 to 1999-2000	10.58	15.03
1980-81 to 1999-2000	13.37	15.40

Note: Growth rates have been estimated by using the semi-logarithmic model $y = ab^t$, where y is revenue/expenditure and t is time period. The growth rate is given by $(b-1) \times 100$.

Source: Calculated from the data available in *Orissa Budget (2001-02) at a Glance*, Finance Department, Govt. of Orissa.

Given the poor flow of revenue receipts as compared to the revenue expenditure, the entire burden of adjustment of this imbalance has fallen on capital and maintenance expenditure. That means, the entire revenue expenditure of the plan sector and the part of the revenue expenditure of the non-plan sector are being funded from receipts in the capital account. This is a dangerous situation, as this will lead to sluggish growth in capital expenditure and will ultimately result in slowdown of the economic growth.

The higher revenue deficit forces the State Government to resort to higher borrowing, which means higher debt servicing liabilities. This will lead to more revenue expenditure, which will again give rise to higher revenue deficits. The entire theory acts like a vicious circle and will inevitably lead to a situation of debt trap.

Since the State Government is unable to finance its expenditure it has resorted to excessive borrowing. As a matter of fact, the debt burden of the State has increased tremendously over the years. The outstanding debt of the State has grown by more than fifteen-fold from Rs.1177 crore in 1980-81 to Rs.18099.79 crore in 1999-00 and again to Rs.24495.05 crore in 2001-02 (RE) (Table 11.4). In per capita terms, the debt has increased more than ten times from Rs.445.85 in 1980-81 to Rs.6692.64 in 2001-02 (RE). It has increased at a significantly higher rate in the 1990s as compared to the 1980s. This is primarily because the revenue deficits are more prominent in the 1990s than the 1980s. During the period 1980-81 to 2001-02 (RE), the share of outstanding debt in NSDP has increased from 34.19 per cent to 63.74 per cent.

Table -11.4**Debt Profile**

Year	Outstanding Debt (Rs. in Crore)	Outstanding Debt as % of NSDP	Per Capita Debt (Rs.)	Int. Pay/ Borrowing	Debt Serv./ Borrowing	Debt Serv. as % of Rev.Exp	Debt Serv. as % of Total Debt
1980-81	1177.06	34.19	445.85	0.23	0.77	30.30	14.08
1985-86	2270.42	36.47	761.88	0.26	0.59	28.24	12.45
1990-91	4538.58	46.96	1431.73	0.35	0.71	34.41	16.61
1995-96	9219.91	42.96	2695.88	0.49	0.82	33.26	16.94
1996-97	10493.75	50.85	3024.14	0.56	0.90	34.00	16.58
1997-98	12387.50	51.39	3519.18	0.48	0.78	38.22	17.08
1998-99	14751.14	54.46	4143.58	0.42	0.75	39.12	18.08
1999-00	18099.79	59.47	5013.79	0.28	0.52	26.62	12.44
2000-01	21001.90	61.41	5738.22	0.51	0.86	43.71	18.38
2001-02 (RE)	24495.05	63.74	6692.64	0.62	0.90	42.86	17.89

Note: (1) The Outstanding debt, interest payment, borrowing and debt servicing include provident fund.

(2) See Table 11.1

Source: *White Paper on State Finances*, Finance Department, Govt. of Orissa, March 2001.

Due to the enormous increase in the borrowing, the government has to repay more debt. At the same time, in order to repay the debt an increasing amount of borrowing is required. Looking at the ratio of debt servicing to borrowing (Table 11.4), we find that more than 80 per cent of the borrowing is utilised for debt repayment during most part of the 90s. Out of the total borrowings, a significant proportion is utilised for interest payments. During 1996-97, about 56 per cent of the total borrowing were used for financing interest payment, leaving a very small proportion of borrowing for repayment of loan. This figure has increased to around 62 per cent in 2001-02 (RE).

Though the State Government utilises a higher proportion of the borrowings towards debt repayment, yet a significantly higher percentage of the total debt is still to be paid. The data shows that during 1999-00, about 12.44 per cent of the total debt of the State were repaid. Furthermore, the ratio of outstanding debt to NSDP has been increasing faster than the ratio of debt repayment to total debt, which indicates that the debt burden of the State has been increasing rapidly year after year. The share of debt repayment in the total revenue

expenditure has fluctuated between 21 per cent to 39 per cent during the period 1980-81 to 1999-2000, which increased to around 44 per cent in 2000-01. This indicates that a significant percentage of the State's revenue expenditure goes towards debt repayment. The State depends mostly on borrowings to repay its loans and interest payments. This is a very delicate and dangerous situation and will ultimately lead to debt trap. Therefore, it is of utmost importance that the State Government should take steps to control its increasing borrowing. Otherwise the State will move towards complete financial disarray and bankruptcy.

UNDERLYING CAUSES OF IMBALANCE AND TRENDS IN REVENUE RECEIPTS AND REVENUE EXPENDITURE

Trends in Revenue Receipts

The existence of huge revenue deficits of the State Government is mainly because of the inability of the government to raise more revenue. The revenue receipts of the State Government have increased from Rs.621.35 crore in the year 1980-81 to Rs.5884.64 crore in 1999-00. The State receives its revenue from two sources: (1) own revenue (Tax and Non-tax Revenue) and (2) Central transfer (Shared tax and Grants). If we look at the composition of revenue receipts in Orissa, we find that out of the total revenue receipts, the share of Central transfer is higher than the share of State's own revenue (Table 11.5). While the share of Central transfer remains between 55 to 60 per cent over the period 1980-81 to 1999-2000, the share of own revenue remains between 40 to 45 per cent during the same period. This indicates that the receipts from the State's own revenue source is lower than the Central transfers.

Within the own revenue, the share of tax revenue remains significantly higher than the share of non-tax revenue in 1999-2000, though in 1980-81 it was more or less the same (Table 11.5). That means the share of tax revenue has increased rapidly from 1980-81 to 1999-2000, while the share of non-tax revenue has declined significantly during the same period. Considering the different items of Central transfers, it is found that the share of grants has been losing its importance over time than that of the shared tax. This is a great concern for a poor State like Orissa. One of the reasons for this could be that the State is unable to provide the matching grants.

Table - 11.5**Composition of Total Revenue Receipts of Orissa****(in %)**

	1980-81	1985-86	1990-91	1995-96	1999-00
1. Own Revenue	42.83	44.27	40.07	45.12	41.13
Tax	21.26 (49.63)	30.39 (68.64)	30.81 (76.88)	28.97 (64.21)	28.96 (70.40)
Non-tax	21.57 (50.37)	13.88 (31.36)	9.26 (23.12)	16.15 (35.79)	12.17 (29.60)
2. Central Transfer	57.17	55.73	59.93	54.88	58.87
Shared Tax	25.75 (45.04)	29.29 (52.55)	31.97 (53.35)	33.03 (60.18)	29.71 (50.47)
Grants	31.14 (54.96)	26.44 (47.45)	27.96 (46.65)	21.86 (39.82)	29.15 (49.53)
3. Total Revenue	100.00	100.00	100.00	100.00	100.00

Note: (1) Figures in parentheses are percentage share of their respective totals.

(2) Central sales tax is included in own sources of revenue.

Source: Calculated from the data available in *Orissa Budget (2001-02) at a Glance*, Finance Department, Govt. of Orissa.

Table -11.6**Annual Compound Growth of Revenue Receipts****(in %)**

	1980-81 to 1999-00	1980-81 to 1989-90	1990-91 to 1999-00
1. Own Revenue	13.88	13.65	11.88
Tax	15.19	18.15	11.9
Non-tax	11.76	6.89	12.12
2. Central Transfer	13.16	13.34	9.66
Shared Tax	14.7	15.94	10.71
Grants	11.4	10.96	7.9
3. Total Revenue	13.44	13.43	10.53

Note: (1) For Calculation of Growth Rate, see Table 11.3

(2) Central sales tax is included in own sources of revenue.

Source: Calculated from the data available in *Orissa Budget (2001-02) at a Glance*, Finance Department, Govt. of Orissa.

Considering the annual growth of different items of revenue receipts, Table 11.6 shows that the State's total revenue grows at an annual compound rate of 13.44 per cent during the period 1980-81 to 1999-2000. However, the growth of State's own revenue is found to be higher than the growth of Central transfer to Orissa. Considering the total revenue between the period 1980s and 1990s, it is observed that the growth rate has decelerated in the latter period. The

annual growth rate of 13.43 per cent in the 1980s has declined to 10.53 per cent in the 1990s. This is also found to be true in case of both own revenue and Central transfers. But the deceleration in case of Central transfers is significantly higher than that of State's own revenue.

Since tax revenue constitutes the bulk of the share of State's own revenue, the State's dependence on tax revenue is greater. Among the own tax revenue, sales tax has emerged as the dominating source of revenue, which contributes almost 64 per cent of the State's own tax revenue in 1999-2000, up from 50.18 per cent in 1980-81 (Table 11.7).

Table - 11.7

Composition of State's Own Tax Revenue

(Rs. in Crore)

Own Tax	1980-81	1985-86	1990-91	1995-96	1999-00
Sales Tax*	56.40 (50.18)	109.90 (44.42)	336.70 (51.73)	716.10 (63.53)	1061.74 (64.02)
Excise Duty	9.20 (8.18)	21.60 (8.73)	45.60 (7.01)	73.40 (6.51)	114.82 (6.92)
Motor Vehicles Tax	9.70 (8.63)	25.30 (10.23)	52.30 (8.03)	107.50 (9.54)	155.53 (9.38)
Stamps & Reg.	7.80 (6.94)	17.30 (6.99)	30.90 (4.75)	63.10 (5.60)	102.00 (6.15)
Elec. Duty	16.90 (15.04)	49.80 (20.13)	98.80 (15.18)	121.30 (10.76)	127.21 (7.67)
Land Revenue	7.10 (6.32)	15.90 (6.43)	81.90 (12.58)	39.50 (3.50)	50.46 (3.04)
Others	5.30 (4.72)	7.60 (3.07)	4.70 (0.72)	6.30 (0.56)	46.51 (2.80)
Total Own Tax*	112.40 (100.00)	247.40 (100.00)	650.90 (100.00)	1127.20 (100.00)	1658.27 (100.00)

Note: (1) Figures in Parentheses are Percentage share of their respective totals.

(2) * Central Sales Tax is not included.

Source: *Orissa Budget in Brief*, (Various Issues), Directorate of Economics and Statistics, Govt. of Orissa; *Finance Accounts*, (Various issues), Govt. of Orissa.

Though there are other sources of tax revenue like excise duty, stamp duties and registration fees, motor vehicles tax, electricity duty, etc their contribution towards State's own revenue is low. Apart from sales tax and motor vehicles tax, the percentage share of all other sources of tax has declined in 1999-00 from 1980-81.

Looking at the different items of own tax revenue (Table 11.8), we find that sales tax has the highest annual growth rate over the period 1980-81 to 1999-2000. This is followed by motor vehicles tax. On the other hand, electricity duty has the lowest growth rate. Comparing their growth rate between the 1980s and the 1990s, we find that the growth rate of all the different sources of tax revenue has declined in the latter period. Even the growth rate of sales tax and motor vehicles tax has declined in the 1990s. The data show that there is a drastic decline in the growth rate of electricity duty during the 1990s against the 1980s. The electricity duty grew at an annual compound rate of 13.84 per cent during the 1980s, which declined significantly to 3.15 per cent during the 1990s. The deceleration in the growth of different items of tax revenue has contributed to the increasing fiscal imbalances in the State.

Table 11.8

Annual Compound Growth of Different Items of Own Tax Revenue

(In %)

Own tax revenue	1980-81 to 1999-00	1980-81 to 1989-90	1990-91 to 1999-00
Sales Tax	17.09	18.98	14.18
Excise Duty	14.51	16.30	10.50
Motor Vehicle Tax	16.48	19.15	13.08
Stamps & Reg.	14.07	15.52	13.93
Elec. Duty	10.98	13.84	3.15

Note: (1) For calculation of growth rate, see Table 11.3

(2) Central sales tax is not included in own sales tax revenue.

Source: Same as Table 11.7.

Trends in Revenue Expenditure

Expenditure of the State can be broadly divided into two parts: Revenue expenditure and Capital expenditure. Revenue expenditure includes purchase of goods and services for current operation against cash or credit, salary of the employees, interest payments etc. Capital expenditure, on the other hand, includes purchase of goods and services for fixed capital formation. Higher revenue expenditure pushes the economy towards debt trap and low economic growth, whereas higher capital expenditure leads to higher income and employment generation and higher economic growth.

The State of Orissa is currently passing through a situation of higher revenue expenditure. The revenue expenditure is growing at a rate higher than the growth of total expenditure (Table 11.9). The capital expenditure on the other hand, is growing at a lower rate. The revenue expenditure during the last 20 years has grown at an annual compound rate of 15.40 per cent, whereas capital expenditure grew at only 9.66 per cent during the same period. This shows that revenue expenditure is growing faster than capital expenditure. Further, revenue expenditure has grown at a higher rate in the 1990s than the 1980s. On the other hand, the growth rate of capital expenditure has slowed down in the 1990s as compared to the 1980s. This shows that the State is being pushed towards debt trap and low economic growth.

Table - 11.9

Annual Compound Growth of Expenditure

(In per cent)

	1980-81 to 1999-00	1980-81 to 1989-90	1990-91 to 1999-00
Revenue Expenditure	15.40	14.66	15.03
Capital Expenditure	9.66	12.43	5.24
Total Expenditure	14.46	14.14	13.58

Note: For calculation of growth rate, see Table 11.3

Source: *R.B.I Bulletin; Finance Accounts, Govt. of Orissa.*

Looking at the total expenditure as percentage of NSDP it is found from Table 11.10 that total expenditure has increased from 21.34 per cent in 1980-81 to 30.42 per cent in 1999-2000. A break up of the total expenditure shows that revenue expenditure constitutes a significantly higher proportion of NSDP, while capital expenditure constitutes a very small proportion of NSDP and has declined significantly from 1980-81 to 1999-2000.

Table - 11.10

Total Expenditure as Percentage of NSDP

	1980-81	1985-86	1990-91	1995-96	1999-00
Revenue Expenditure	15.89	16.08	22.67	21.89	27.79
Capital Expenditure	5.46	4.13	5.70	2.08	2.63
Total Expenditure	21.34	20.21	28.37	23.97	30.42

Source: *R.B.I Bulletin; Finance Accounts, Govt. of Orissa.*

Revenue expenditure has a dominant share in the State's total expenditure. During 1980-81 the share of revenue expenditure was 74.44 per cent, which increased to 91.37 per cent in 1999-00 (Table 11.11). The same is true in all the different functional categories like general, social and economic services. In general and social services, almost all the expenditures are revenue expenditure, leaving an insignificant share for capital expenditure. On the other hand, a major portion of the share in economic services sector is revenue expenditure and it is increasing over the years. This indicates that even in the economic services sector, there is a rising trend in revenue expenditure, which is a cause of great concern.

Table-11.11
Functional Composition of Revenue Expenditure in Total Expenditure

(Rs. in Crore)					
Year	General Services	Social Services	Economic Services	Others	Total Rev. Expenditure
1980-81	134.10 (100.00)	240.50 (94.39)	168.50 (49.27)	3.70	546.90 (74.44)
1985-86	282.50 (97.99)	431.40 (95.27)	280.20 (54.92)	6.80	1000.90 (79.56)
1990-91	682.00 (98.74)	842.20 (95.16)	648.10 (56.47)	18.20	2190.50 (79.90)
1995-96	1603.20 (99.19)	1834.70 (97.13)	1247.10 (76.67)	12.90	4697.90 (91.31)
1999-00	2888.11 (99.47)	4002.10 (98.83)	1548.02 (67.77)	20.59	8458.82 (91.37)

Note: Figures in the brackets Indicate Percentage Share of total Expenditure under Different Heads of Expenditure.

Source: *R.B.I Bulletin*; and *Finance Accounts Govt. of Orissa*.

In the social services sector, education is the single most service sector, which constitutes almost half of the total revenue expenditure. Almost all the expenditure in education sector is revenue expenditure, leaving an insignificant share for capital expenditure (Table 11.12). This is also true in the case of social welfare and security. In case of medical and sanitation, though there is some provision for capital expenditure, still the share of revenue expenditure in total expenditure varies between 92 per cent to 96 per cent. In housing and urban development, there is a significant increase in the share of revenue expenditure over time. The share has increased from 63.25 per cent in 1980-81 to 91.15 per cent in 1999-00. Hence, almost all the major items of social service sector constitute more than 90 per cent revenue expenditure. This significant share of revenue expenditure leaves ground for very low share of capital expenditure. This not only reduces the quality of social services but also helps increasing fiscal imbalance.

Table -11.12**Composition of Major Items of Revenue Expenditure on Social Services Sector****(Rs. in Crore)**

Items of Social Services	1980-81	1985-86	1990-91	1995-96	1999-00
Education	107.10 (98.93)	203.43 (96.61)	451.70 (97.80)	942.60 (99.65)	1930.37 (99.55)
Medical & Sanitation	54.91 (93.51)	109.12 (95.53)	175.40 (92.56)	365.30 (91.67)	647.59 (95.95)
Social Welfare & Security	26.01 (99.20)	90.94 (98.33)	122.30 (97.56)	372.70 (99.19)	218.01 (100.00)
Housing & Urban Dev.	10.55 (63.25)	16.65 (72.30)	25.10 (61.87)	42.00 (74.09)	89.98 (91.15)
Total Expenditure on Social Services	240.50 (94.39)	431.40 (95.27)	842.20 (95.16)	1834.70 (97.18)	4002.10 (98.83)

Note: Figures in the brackets indicate percentage share of total expenditure under Different Heads of Expenditure.

Source: *R.B.I Bulletin*; and *Finance Accounts Govt. of Orissa*.

Similarly, in the economic services sector, the share of revenue expenditure is increasing over the years. The major item of economic services sector is agriculture and allied sector, where the share of revenue expenditure has increased rapidly from 1980-81 to 1999-2000 (Table 11.13). During 1999-00, the share has reached to a level of more than 90 per cent, thus making less than 10 per cent of the total expenditure available for capital formation. Similar is the case of industry and mining sector. In the case of transport and communication, there is fluctuation in the share of revenue expenditure. Still it has a significant share. The only exception is the energy, irrigation and flood control sector, where the share of revenue expenditure is low, thereby giving place for capital expenditure. This shows that in different items of economic services sector, revenue expenditure has a major share, as a result of which the share of total revenue expenditure is increasing over time, leaving a declining share for capital formation and development of the economy.

Table - 11.13**Composition of Major Items of Revenue Expenditure on Economic Services Sector****(Rs. in Crore)**

Items of Economic services	1980-81	1985-86	1990-91	1995-96	1999-00
Agriculture & Allied Sector	84.55 (63.51)	158.62 (83.66)	272.1 (94.85)	426 (93.76)	539.84 (90.41)
Industry & Mining	6.21 (56.00)	14.55 (39.20)	34.3 (45.30)	64.9 (97.81)	75.26 N.A
Energy, irrigation & Flood Control	29.06 (21.48)	25.02 (14.96)	68.4 N.A	404.4 N.A	105.93 (17.84)
Transport & Communication	26.31 (65.79)	23.74 (40.55)	50.4 (38.16)	116.3 (43.76)	143.63 (52.15)
Total Expenditure on Economic Services	168.5 (49.27)	280.2 (54.92)	648.1 (56.47)	1247.1 (76.67)	1548.02 (67.77)

Note: Figures in the brackets indicate percentage share of total expenditure under Different Heads of Expenditure.

Source: *R.B.I Bulletin*; and *Finance Accounts Govt. of Orissa*.

MAJOR ISSUES OF FISCAL IMBALANCES IN ORISSA

A number of issues can be raised on the emerging fiscal imbalance in the State. These issues are highly significant and need immediate attention, otherwise the problem will go out of control of the State Government. Some of the major issues concerning the fiscal problem in Orissa are discussed below.

Higher Expenditure on Salary, Pension and Interest

The idea that emoluments of an employee are related to the capacity to pay by his employer is progressively vitiated. The option now is that either you do not employ or if you employ, you have to pay according to considerations other than your capacity to pay (Vithal 1992).

Ever increasing wage bill has become a serious cause of concern for most of the states in the country and Orissa is no exception. The share of salary of the State Government employees in the State's total revenue expenditure has increased tremendously over the last two decades and has become unsustainable. Table 11.14 shows that the total salary and pension bill was only Rs.158.07 crore in the year 1980-81, which was 28.90 per cent of the total revenue expenditure. This has increased to Rs.5147.20 crore (50.34 per cent of revenue expenditure) in the year 2001-02 (RE). The share was 56.83 per cent in 1998-99, when the State

Government implemented the new pay scale as recommended by the Fifth Pay Commission. This is a major cause of concern for the State and a major reason for the current imbalance. To add to the woes, the interest bill of the State Government has gone up significantly during the past two decades. The percentage share of interest in the total revenue expenditure was only 9.25 during the year 1980-81. But in the year 2001-02 (RE), the figure has gone up to 29.54 per cent. The salary, pension and interest payments taken together constitute a staggering 79.88 per cent of the State's total revenue expenditure in the year 2001-02 (RE). This indicates that almost 68 per cent of the total revenue expenditure are meant for these unproductive expenses, leaving very little for other productive expenses, which reflects in low economic growth.

Table -11.14

Share of Wage and Interest in Revenue Expenditure and Own Revenue

Year	Salary & Pension (Rs. in Crore)	Interest (Rs. in Crore)	Total (Rs. in Crore)	Salary & Pension as % of Rev.Exp	Interest as % of Rev.Exp	G.Total as % of Rev.Exp	Salary & Pension as % of Own Rev.	Interest as % of Own Rev.	G.Total as % of Own Rev.
1980-81	158.07	50.61	208.68	28.90	9.25	38.16	64.15	20.54	84.69
1985-86	458.79	125.91	584.70	45.84	12.58	58.42	121.37	33.31	154.68
1990-91	957.31	364.67	1321.98	43.69	16.65	60.35	112.36	42.80	155.16
1995-96	1961.95	929.26	2891.21	41.77	19.78	61.54	111.76	52.94	164.70
1996-97	2316.75	1079.37	3396.12	45.27	21.09	66.36	127.03	59.18	186.21
1997-98	2940.19	1291.81	4232.00	53.11	23.33	76.44	149.81	65.82	215.63
1998-99	3874.36	1484.84	5359.20	56.83	21.78	78.62	189.49	72.62	262.11
1999-2000	4495.52	1237.77	5733.29	53.15	14.63	67.78	189.31	52.12	241.43
2000-01	4633.68	2286.88	6920.56	52.48	25.90	78.39	161.38	79.70	241.18
2001-02 (RE)	5147.20	3019.95	8167.15	50.34	29.54	79.88	155.71	91.36	247.07

Source: *White Paper on State Finances*, Finance Department, Govt. of Orissa, March 2001.

The most worrisome factor is that the State's own revenue receipt is not sufficient to meet salary and pension expenses of its employees. If we add the interest payment to it, the total expenses outweigh the State's own revenue receipts by more than twice. The interest payment has alone becomes 91.36 per cent of the State's own revenue during 2001-02 (RE). During the year 1980-81, the payments made in these heads taken together constitute 84.69 per cent of the States total own revenue receipts. But after that this has gone up tremendously, and in the year 2001-02 (RE) the total payments become 247.07 per cent of the State's total own revenue, which is absolutely unsustainable. This means that the State has to depend upon sources beyond its own revenue to finance these bills. This leads to massive borrowing and

thus the vicious circle starts. Therefore, controlling these unproductive expenses becomes the topmost task of the State Government.

Poor Cost Recovery

Another major issue is the low and declining cost recoveries in many of the services provided by the State Government. While the State Government has been spending substantial amounts on various public services over the years, there has hardly been any noticeable attempt to effect cost recoveries on many of the public services provided. In the education (higher & technical), irrigation (major, medium & minor), urban water supply & sanitation, and health sectors the recovery through user charges is very poor compared to the level of expenditure incurred by the State for the delivery of these services (Table 11.15).

Table - 11.15

Cost Recovery

(Rs. in Crore)

Year	Higher Education	Technical Education	Irrigation (major, medium & minor)	Urban Water Supply & Sanitation	Health Services	Total
1992-93						
1.Expenditure	86.15	17.99	44.24	46.79	134.28	329.45
2.Recovery	0.82	0.18	14.52	5.42	4.59	25.53
3.Rec. as % of Exp.	0.95	1.00	32.82	11.58	3.42	7.75
1996-97						
1.Expenditure	159.97	28.54	72.93	37.46	213.49	512.39
2.Recovery	0.04	0.63	8.55	9.61	6.19	25.02
3.Rec. as % of Exp.	0.03	2.21	11.72	25.65	2.90	4.88
1997-98						
1.Expenditure	174.24	26.11	63.30	25.60	230.12	519.37
2.Recovery	0.00	0.67	8.39	12.60	6.21	27.87
3.Rec. as % of Exp.	0.00	2.57	13.25	49.22	2.70	5.37
1998-99						
1.Expenditure	193.95	43.52	73.48	61.59	371.19	743.73
2.Recovery	1.01	0.64	13.61	12.20	8.06	35.52
3.Rec. as % of Exp.	0.52	1.47	18.52	19.81	2.17	4.78
1999-00						
1.Expenditure	187.61	17.88	65.80	29.20	314.65	615.14
2.Recovery	1.50	0.53	12.45	16.71	6.85	38.04
3.Rec. as % of Exp.	0.80	2.96	18.92	57.23	2.18	6.18

Source: *White Paper on State Finances*, Finance Department, Govt. of Orissa, March 2001.

Due to the lower cost recoveries, the magnitude of implicit subsidies (difference between the cost of delivery of goods and services and the recovery of the cost) provided to these services

is increasing every year and thus putting a lot of financial burden on the State. The low cost recovery is basically due to uneconomic pricing and inefficiency. Therefore, there is a greater need for the recovery of at least the maintenance cost and a part of capital cost of these services provided by the Government. At the same time, there is also a greater need for improving the quality of the services provided. At present the quality of these services is very poor. Besides, there is also huge leakage.

Negative Contribution from Departmental Commercial Undertakings and PSUs

Poor contribution from departmental commercial undertakings is another issue that needs to be taken care of. The contributions from many of the departmental commercial undertakings are either poor or negative. At a time when the State finances are already in a mess, negative contribution from commercial undertaking poses a major threat towards the finance of the State of Orissa. Even if the contributions from some of the commercial undertakings are positive, yet these are not substantial.

Table 11.16 shows that only forest and industries are the two departmental undertakings, which makes positive contribution, while the other departmental undertakings like fisheries, irrigation, electricity and road and transport contribute negatively to the State. Leakage is an important factor in all these cases, for example in case of electricity departmental undertaking the transmission and distribution loss is 42 per cent (Government of Orissa, 2001). Besides, contribution from forest department is also declining. The net contribution from forest has come to a level of Rs.19.36 crore in 1997-98, from Rs.64.63 crore in 1990-91. However, the decline is sharp after 1994-95, when the net contribution was Rs.64.38 crore.

Among the major departments, irrigation and road and communication departments drain a significant amount from the State Exchequer. This is due to the provision of implicit subsidy as well as the existence of vast number of employees.

Table 11.16
Net Contribution from Departmental Commercial Undertakings

(Rs. in Crore)

Department	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98
Forestry	64.63	36.72	37.36	41.75	64.38	10.46	19.72	19.36
Fisheries	-80.8	-12.03	-11.21	-12.32	-10.54	-12.77	-13.9	-12.85
Irrigation	-56.21	-72.77	-82.96	-101.06	-106.59	-48.68	-171.29	-138.75
Electricity	-67.4	-27.78	-38.43	-74.5	--	-23.886	-9.15	-4.74
Industries	-10.95	19.21	--	85.7	107.26	231.18	202.73	251.81
Road & Transport	-50.38	-71.56	-84.3	-89.61	-104.88	--	--	--

Source: *RBI Bulletins*, various issues.

The overall picture suggests that the contribution from these departmental commercial undertakings has been very poor and needs to be corrected. The negative contribution reflects the lack of efficiency and transparency in these departments. Therefore, the government should try to improve efficiency and transparency so as to raise more revenue from these commercial undertakings.

The State Government can also utilise the surplus of the public sector undertakings (PSUs) for financing its plans. But the State PSUs are incurring losses. There has been continuous loss by these PSUs, which has reached to a cumulative loss of Rs.1176.07 crore by 1999-2000 (Table 11.17). It can be observed from the Table that the amount of loss has been increasing year after year. Due to the negative contribution from the PSUs the State Government has to depend on other sources like borrowing for financing the Plans.

Table - 11.17
Negative Contribution from PSUs

Year	Net Loss (Rs.in Crore)
1993-94	-61.05
1994-95	-75.28
1995-96	+82.07
1996-97	-124.44
1997-98	-121.24
1998-99	-258.92
1999-00	-207.62
Cumulative Loss up to 1999-00 (Provisional)	1176.07

Source: *White Paper on State Finances*, Finance Department, Govt. of Orissa, March 2001.

Therefore, there is a need to restructure the PSUs in order to check drain of resources from the public exchequer. Public Sector Undertakings, which are producing public goods, should be kept under full government control for consideration of equity. Such industries, which are making losses, should be rehabilitated. Public sector commercial undertakings, which are making profit, should be disinvested as private sector participation is necessary in case of such industries for consideration of efficiency. In such cases, the proportion of government share should be lower compared to the private sector. On the other hand, public sector undertakings, which are making losses, should be closed down. The money saved thus could be utilised for development purposes.

Loss of Revenue on Mining Royalty

Mining royalty is an important source of non-tax revenue in Orissa. It contributes nearly 60 per cent of the State's own non-tax revenue (Government of Orissa 2001). Therefore, the growth of non-tax revenue mostly depends on the growth of royalty from minerals. Even though the State has abundant deposit of mineral resources, the growth from this source of revenue is not encouraging due to the lack of timely revision of the rate of royalty. Since the Government of India fixes the rate of royalty, the State Government is handicapped in raising revenue from this source. From coal royalty, the govt. is losing Rs.150 crore per year. In case of other minerals, the State Government cannot impose levy since the Supreme Court has given a decision that the State Government cannot impose a cess (Government of Orissa, 2001). As a matter of fact, the State Government is losing a huge amount of revenue from this source. This adds to the increasing fiscal imbalance in the State.

Low Mobilisation of Additional Tax Revenue

One of the major issues regarding the increasing fiscal imbalance is the lower revenue generating effort on the part of the State Government. This is realised from the deceleration in the growth of tax revenue in the 1990s (Table 11.8). We can also see from Table 11.18 that there is declining tax effort on the part of the State Government during the 1990s. It can be seen from the Table that all the major tax revenues were buoyant during the 1980s. But sales tax and motor vehicles taxes were more buoyant than the aggregate tax revenue, while the electricity duty was just buoyant. All these show that with the increase in income, there was more than proportionate increase in the major sources of tax revenue in the 1980s.

Table - 11.18**Buoyancy of State's Tax Revenue (1980-81 to 1999-2000)**

Tax Revenue	1980-81 to 1989-90	1990-91 to 1999-00	Difference
Sales Tax	1.4793	1.0813	0.398
Motor Vehicles Tax	1.4985	1.0108	0.4877
Excise Duty	1.3019	0.8049	0.497
Stamps and Registration Fee	1.2382	1.0717	0.1665
Electricity Duty	1.0795	0.2534	0.8261
Total Own Tax	1.4255	0.8970	0.5285

Note: Buoyancy coefficients are estimated by regressing tax revenue on NSDP.

The dummy variable method is used for calculating the buoyancy coefficients.

Source: 1. *Orissa Budget in Brief*, (various issues), Directorate of Economics and Statistics, Bhubaneswar.

2. Govt. of Orissa, *Economic Survey*, (various issues), Directorate of Economics and Statistics, Bhubaneswar.

But the scenario has changed in the 1990s. During this period, the aggregate tax revenue is not found to be buoyant, thereby indicating that the tax collection is less than proportionate to the increase in income. This is due to the lower elasticity¹ of tax revenue as well as the lower effort on the part of the State Government to raise additional tax revenue. The situation is more depressing in case of electricity duty, where the buoyancy coefficient is very low, indicating that the State Government is not putting much effort to raise additional revenue from this source. On the other hand, sales tax, motor vehicles tax and stamp duties and registration fees are just buoyant. But in these cases, the buoyancy coefficient has declined significantly from the 1980s. All these show that there is decline in the effort on the part of the State Government to mobilise additional tax revenue.

Increasing Arrears in Tax and Non-tax Revenue

Huge amount of arrears in both tax and non-tax revenues not only create financial burden on the state but also question the ability of the State machinery to collect these revenues. The Government of Orissa is unable to collect all the taxes that are levied in the State. The amount of arrears as on March 1997 was as high as Rs.1035.15 crore (Table 11.19). The amount of

¹ The elasticity of tax revenue is the automatic change in tax revenue, after cleansing the effect of discretionary changes, due to change in income (see Meher 1993).

arrears is found to be highest in case of sales tax, i.e., Rs.786.42 crore (76 per cent of total arrears). Apart from sales tax, the arrears of electricity duty, revenue from forest and royalty on mines and minerals are also quite high.

Table - 11.19
Tax and Non-Tax Arrears as on 31.03.1997

	(Rs. in Crore)
1. Sales Tax	786.42
2. Mines & Minerals	38.3
3. Land Revenue	12.76
4. Interest	13.51
5. Taxes & Duties on Electricity	89.17
6. Police	6.96
7. Forest	58.43
8. Taxes on Vehicles	29.6
Total Arrears	1035.15

Source: *White Paper on State Finances*, Finance Department, Govt. of Orissa, 1999.

The arrears have been increasing over time and reached to Rs.1237.48 crore in 1997-98 but declined then to Rs.1152.08 crore in 1998-99. Still it is a huge amount and it becomes more than 50 per cent of the actual collection of own tax revenue. That means, a significant proportion of revenue remains uncollected.

The increasing amount of tax and non-tax arrears is one of the reasons for lower revenue receipts. This should be reduced drastically so as to decrease the revenue deficit as well as the borrowing of the State. The peculiar situation of increasing arrears as well as increasing borrowing should be reversed through immediate and appropriate policy by State Government.

Declining Central Transfer

One of the major areas of concern is declining Central transfers to Orissa. The Central transfer in the form of shared tax and grants is on the decline over the years. It is seen that the growth rates of both the shared tax and the grants have declined drastically in the 1990s from the 1980s. In a poor State like Orissa, where the collection of own revenue is not high, declining Central transfer is a real cause of concern. Further, a significant proportion of grants is through

centrally sponsored schemes and needs matching share from the State Government. Due to the inadequate funds, the State Government is unable to qualify for most of the grants. Besides, many of the programmes have distorted the state's spending priorities and have contributed to the growth of unproductive employment (Rao 1992).

High Loan Component of Central Assistance

Since the State Government cannot provide adequate funds for financing the plan outlay, it depends almost entirely on Central assistance and other loans. But the plan assistance flowing to the State Government from the Centre has an element of 70 per cent loan and 30 per cent grant. Even in the case of additional Central assistance (ACA) under externally aided projects the same problem arises, i.e., 70 per cent loan and 30 per cent grant. Further, irrespective of the rate of interest charged by the foreign donor agencies to the Government of India (usually 0.5 per cent to 4 per cent), the loan component of the ACA carries the same rate of interest as the loan component of the normal State Plan assistance carries, i.e., 12.5 per cent per annum at present (Govt.of Orissa, 2001).

Hence, more the State receives assistance, more is the loan element. Therefore, loan burden becomes more and more heavy for Orissa.

IMPLICATION OF THE FISCAL IMBALANCES

From the foregoing discussion it is clear that the State is facing a severe financial crisis. The mounting revenue deficits accompanied by rapid increase in revenue expenditure and slow growth of revenue receipts, inadequate own revenues, declining Central assistance and negative contribution by public enterprises have kept the developmental expenditure of the State at low level. The revenue expenditure of the State has increased to such an extent that the State has to divert funds from capital account to meet expenses in revenue account, thereby ensuring low economic development. The borrowing of the State has been mounting year after year and amount of debt has reached a level where the State needs to borrow more money to clear off debts. Most of the borrowings of the State are used for repaying loans, interest and a part is used to finance the deficits. The borrowings instead of being used to finance developmental activities are used to finance non-developmental activities.

If this trend is allowed to persist then the situation would be further worsened leading to a collapse of developmental expenditure and would adversely affect the normal function of governance as well as welfare provisions in social sector. The vicious circle would continue leading to further borrowings, further interest liabilities and squeezing out whatever little scope is there for developmental expenditure. Therefore, in order to arrest this trend, there is a need to make fiscal correction without further delay.

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