Table 3.4 : Sources of Tax Revenue

	2007-8	2008-9	2009-10	2010-11	2011-12 (BE)	2011-12 (P)	2012-13 (BE)
				(₹ crore)			
Direct (a)	**295938**	**319859**	**367648**	**438477**	**525151**	**489312**	**564337**
Personal income tax	102644	106046	122475	139069	164526	165276	189866
Corporation tax	192911	213395	244725	298688	359990	323250	373227
Indirect(b)	**279031**	**269433**	**244737**	**344530**	**397250**	**392273**	**504423**
Customs	104119	99879	83324	135813	151700	149489	186694
Excise	123611	108613	102991	137701	163550	145205	193729
Service tax	51301	60941	58422	71016	82000	97579	124000
Gross tax revenue #	**593147**	**605299**	**624528**	**793072**	**932440**	**890622**	**1077611**
			Tax revenue as a percentage of gross tax revenue				
Direct (a)	49.9	52.8	58.9	55.3	56.3	54.9	52.4
Personal income tax	17.3	17.5	19.6	17.5	17.6	18.6	17.6
Corporation tax	32.5	35.3	39.2	37.7	38.6	36.3	34.6
Indirect(b)	47.0	44.5	39.2	43.4	42.6	44.0	46.8
Customs	17.6	16.5	13.3	17.1	16.3	16.8	17.3
Excise	20.8	17.9	16.5	17.4	17.5	16.3	18.0
Service tax	8.6	10.1	9.4	9.0	8.8	11.0	11.5
			Tax revenue as a percentage of gross domestic product				
Direct(a)	5.9	5.7	5.7	5.6	5.8	5.5	5.6
Personal income tax	2.1	1.9	1.9	1.8	1.8	1.8	1.9
Corporation tax	3.9	3.8	3.8	3.8	4.0	3.6	3.7
Indirect(b)	5.6	4.8	3.8	4.4	4.4	4.4	5.0
Customs	2.1	1.8	1.3	1.7	1.7	1.7	1.9
Excise	2.5	1.9	1.6	1.8	1.8	1.6	1.9
Service tax	1.0	1.1	0.9	0.9	0.9	1.1	1.2
Gross tax revenue #	11.9	10.8	9.6	10.2	10.4	9.9	10.7

Sources : Union Budget documents and Controller General of Accounts.

\# includes taxes referred in (a) & (b) and taxes of Union Territories and 'other' taxes.

Notes: 1. Direct taxes also includes taxes pertaining to expenditure, interest, wealth, gift, and estate duty.
2. The ratios to GDP at current market prices are based on the CSO's National Accounts 2004-5 series.

the age of 60 years has been enhanced from ₹ 1,80,000 to ₹ 2 lakh. The income slab for 20 per cent tax rate has been broadened for all individual taxpayers irrespective of their age and will now be applicable to total income between ₹ 5 lakh and ₹ 10 lakh instead of the earlier slab of ₹ 5 lakh and ₹ 8 lakh. The tax rate of 30 per cent will now be applicable to total income exceeding ₹ 10 lakh. Securities transaction tax on certain transactions in specified securities has been reduced from the existing 0.125 per cent to 0.1 per cent.

3.15 The two specific measures aimed at expanding the direct tax base in the Budget for 2012-13 were the introduction of the provisions of GAAR in the Income Tax Act and extending the provisions of alternate minimum tax (AMT) to all non-company assessees. In an environment of moderate rates of tax, it is necessary that the correct tax base be subject to tax in the face of aggressive tax planning and use of opaque low tax jurisdictions for residence as well as for sourcing capital. The need for making statutory provisions for codifying the doctrine of 'substance over form' has been realized by introducing the chapter on GAAR. However, in view of the apprehensions raised about the Rules and the recommendations of the Shome Committee, the provisions have been deferred.

3.16 Besides the above, in order to widen the tax base, the provisions regarding AMT have been extended to all non-company assessees and it is provided that a person other than a company that has claimed deduction under any section (other than section 80P) included in Chapter VI-A under the heading 'C – Deductions in respect of certain incomes' or under section 10AA, shall be liable to pay AMT at the rate of 18.5 per cent. In order to bring about greater certainty and to reduce litigation in matters related to transfer pricing and international taxation, the advance pricing agreement (APA) scheme has been notified. APA is an agreement in advance between a taxpayer and the revenue department on an appropriate transfer-pricing methodology for a set of transactions over a fixed period of time in the future. APAs therefore offer better assurance on transfer-pricing methods and are conducive for providing certainty and unanimity of approach.

3.17 The modernization of the business processes of the tax administration through extensive use of information technology is continuing, viz. along with e-filing of income tax returns, various forms, audit reports, and statements of tax deduction at source have been made compatible with electronic filing and computerized centralized processing. These measures would enable tax administration to function in a more efficient and automated environment.

Indirect Taxes

3.18 The Budget for 2012-13 estimated revenue from indirect taxes to grow by 26.7 per cent over

Box 3.1 : Sector-Specific Proposals in Central Excise

1. **CEMENT:** The excise duty structure on cement manufactured and cleared in packaged form rationalized. The graded retail selling price (RSP) slabs for the purpose of charging of duty on cement manufactured and cleared in packaged form done away with. The duty rates on cement and cement clinkers revised as follows:

Description	Revised rate of duty
1. Cement manufactured and cleared in packaged form:-	
(a) from mini cement plants	6% + ₹ 120 per tonne
(b) from other than mini cement plants	12% + ₹ 120 per tonne
2. Cement cleared other than in packaged form.	12%
3. Cement clinker	12%

Cement also notified under section 4A, that is RSP-based assessment with an abatement of 30 per cent on RSP.

2. **PRECIOUS METALS:** (i) Excise duty on gold jewellery sold from export-oriented units (EOUs) into domestic tariff area (DTA) increased from 5 per cent to 10 per cent; (ii) Excise duty on refined gold increased from 1.5 per cent to 3 per cent; (iii) Excise duty on gold produced from copper smelting increased from 2 per cent to 3 per cent; (iv) Excise duty on silver produced from copper smelting reduced from 6 per cent to 4 per cent; (v) Gold coins of 99.5 per cent and above purity and silver coins of 99.9 per cent and above purity manufactured out of duty paid gold fully exempted from excise duty; (vi) Articles of gold /silver jewellery exempted from excise duty.

3. **MASS CONSUMPTION ITEMS:** (i) Refills and inks used for the manufacture of writing instruments of value not exceeding ₹ 200 per piece fully exempted from excise duty subject to actual user condition;(ii) Exemption limit on footwear enhanced from ₹ 250 per pair to ₹ 500 per pair. Footwear above ₹ 500 per pair to attract excise duty of 12 per cent; (iii) Excise duty on iodine reduced from 10 per cent to 6 per cent.

4. **ENVIRONMENT-FRIENDLY GOODS:** (i) Excise duty reduced from 10 per cent to 6 per cent on battery packs supplied to manufacturers of electric vehicles for use as spares and original equipment manufacturers subject to end-use condition; (ii) Excise duty reduced from 10 per cent to 6 per cent on specific parts of hybrid vehicles supplied to manufacturers of hybrid vehicles subject to end-use condition; (iii) Excise duty on LED lamps reduced to 6 per cent.

5. **PETROLEUM:** The rate of cess leviable on indigenous petroleum crude oil under the Oil Industry (Development) Act 1974 increased from ₹ 2500 per metric tonne to ₹ 4500 per metric tonne.

6. **TEXTILES:** For the purpose of charging excise duty on ready-made garments bearing a brand name or sold under a brand name, the level of abatement from RSP increased from 55 per cent to 70 per cent.

7. **MISCELLANEOUS:** (i) Full exemption from excise duty provided to food preparations containing fruits and vegetables falling under Chapter 20, which are prepared in a hotel, restaurant, or retail outlet, whether or not such food is consumed in such hotels/restaurants/retail outlets; (ii) The composite rate applicable to automobile chassis converted into an ad valorem rate and fixed at 14 per cent for diesel driven buses, lorries, and trucks; (iii) Excise duty on parts of mobile phones, other than those cleared to a manufacturer of mobile phones, reduced from 10 per cent to 2 per cent, provided no Cenvat credit is taken; (iv) Excise duty reduced from 10 per cent to 6 per cent on matches manufactured by semi-mechanized units and processed food products of soy; (v) Full exemption from excise duty withdrawn from mega/ultra mega power projects except 113 specified projects.

2011-12 (RE) on the strength of assumed economic recovery. In so far as union excise duties are concerned, the BE 2012-13 envisaged a growth of 29.1 per cent in revenue over 2011-12 (RE). An increase in the effective rate of excise duty on non-petroleum products from 10 per cent earlier to 12 per cent in BE 2012-13 and a pickup in the manufacturing sector were the bases for these assumptions. The Budget for 2012-13 also made the following other changes: raised the concessional rate of excise duty on non-petroleum products from 5 per cent to 6 per cent; increased the lower rate on non-petroleum products without Cenvat Credit from 1 per cent to 2 per cent with the exception of coal and fertilizers; enhanced the rate of excise duty from 22 per cent to 24 per cent and from '22 per cent+ ₹ 15,000 per vehicle' to 27 per cent on certain categories of automobiles; increased the rates of specific excise duty on cigarettes (both filter and non-filter) of length exceeding 65mm; raised the excise duty on cigars, cheroots, and cigarillos to '12 per cent or ₹ 1,370 per thousand, whichever is higher'; increased the basic excise duty on hand-rolled *bidis* from ₹ 8 to ₹ 10 per thousand and on machine-rolled bidis from ₹19 to ₹ 21 per thousand (See Box 3.1 for sector-specific details).

3.19 In so far as revenue from customs is concerned, the Budget for 2012-13 envisaged a growth of 22.0 per cent over 2011-12 (RE). The two important general reductions in customs duties were the exemption of education cess and secondary and higher education cess from the CVD portion of customs duty so as to avoid computation of such cesses twice; the duty-free allowance under the baggage rules has been increased for adult passengers of Indian origin from ₹ 25,000 to ₹ 35,000 (returning after stay abroad of more than three days) and from ₹ 12,000 to ₹ 15,000 (returning after stay abroad of three days or less). Continuing with the practice of sectoral changes in duty rates, Budget 2012-13 announced many sector-specific measures (Box 3.2).

Box 3.2 : Sector-specific changes in Customs:

1. **AGRICULTURE/AGRO PROCESSING/PLANTATION SECTOR:** (i) Basic customs duty on sugarcane planter, root or tuber crop-harvesting machine and rotary tiller and weeder and parts and components for their manufacture reduced from 7.5 per cent to 2.5 per cent; (ii) At present, project import status available for installation of mechanized handling systems and pallet racking systems in mandis or warehouses for foodgrains and sugar, with concessional rate of basic customs duty of 5 per cent. Such systems also exempt from additional duty of customs (CVD) and special additional duty of customs (SAD). The same dispensation extended to such systems installed in mandis or warehouses for horticultural produce; (iii) Project import status granted to greenhouses set up for protected cultivation of horticulture and floriculture produce with concessional basic customs duty of 5 per cent; (iv) Basic customs duty reduced from 10 per cent/7.5 per cent to 5 per cent (until March 2014) on specified coffee plantation and processing machinery; (v) Basic customs duty reduced from 10 per cent to 5 per cent (until March 2014) on coffee brewing and vending machines (commercial type). Basic customs duty also reduced to 2.5 per cent on parts required for manufacture of such coffee- brewing and -vending machines; (vi) Basic customs duty reduced on specified soluble fertilizers and liquid fertilizers, other than urea, from 7.5 per cent to 5 per cent and from 5 per cent to 2.5 per cent respectively.

2. **AUTOMOBILES:** Basic customs duty on completely built units (CBUs) of large cars/ MUVs/ SUVs permitted for import without type approval (value exceeding US $ 40,000 and engine capacity exceeding 3000 cc for petrol and 2500 cc for diesel) increased from 60 per cent to 75 per cent.

3. **METALS:** (i) Basic customs duty on coating material for manufacture of electrical steel reduced from 10 per cent to 5 per cent subject to actual user condition; (ii) Basic customs duty on ammonium meta-vanadate used in the manufacture of ferro-vanadium reduced from 7.5 per cent to 2.5 per cent; (iii) Nickel oxide/ hydroxide and nickel ore/ concentrate fully exempted from basic customs duty; (iv) Exemption from SAD currently available to CRGO steel restricted to prime quality of such steel; (v) Basic customs duty on flat rolled products (HR and CR) of non-alloy steel increased from 5 per cent to 7.5 per cent.

4. **PRECIOUS METALS:** (i) Basic customs duty on standard gold bars and platinum increased from 2 per cent to 4 per cent; (ii) Basic customs duty on non-standard gold increased from 5 per cent to 10 per cent; (iii) Additional customs duty on gold ore/concentrate and bars for refining increased from 1 per cent to 2 per cent; (iv) Basic customs duty of 2 per cent imposed on cut and polished coloured gemstones.

5. **CAPITAL GOODS/INFRASTRUCTURE:** (i) Basic customs duty on capital goods, plant, and equipment imported for setting up or substantial expansion of iron ore pellet plants or iron ore beneficiation plants reduced from 7.5 per cent to 2.5 per cent; (ii) Full exemption from basic customs duty until March 2015 provided for initial setting up and substantial expansion of fertilizer projects; (iii) Steam coal fully exempted from basic customs duty. CVD reduced from 5 per cent to 1 per cent on such coal (valid up to 31.3.2014); (iv) Natural gas/liquefied natural gas imported for power generation by a power generation company fully exempted from basic customs duty; (v) Full exemption from

(Contd...)

Box 3.2 : Sector-specific changes in Customs: (Contd..)

basic customs duty provided to uranium concentrate, sintered natural uranium dioxide, sintered uranium dioxide pellets for generation of nuclear power; (vi) Full exemption from basic customs duty, CVD and SAD extended to equipment imported for road construction projects awarded by metropolitan development authorities; (vii) Full exemption from basic customs duty and CVD presently available to tunnel boring machines and parts for hydel and road projects extended to all infrastructure projects without end-use condition; (viii) Full exemption from basic customs duty and CVD extended to tunnel excavation and specified lining equipment also; (ix) Full exemption from basic customs duty extended to coalmining projects; (x) Basic customs duty for machinery and instruments for surveying and prospecting reduced and unified at 2.5 per cent; (xi) Basic customs duty on railway safety (train protection and warning system) equipment and railway track-laying machines reduced from 10 per cent to 7.5 per cent.

6. **AIRCRAFT AND SHIPS:** (i) Full exemption from basic customs duty and CVD provided to new and retreaded aircraft tyres; (ii) Full exemption from basic customs duty and CVD extended to parts of aircraft and testing equipment for maintenance and repair of aircraft imported by maintenance, repair, and overhaul (MRO) units; (iii) Customs duties on foreign-going vessels on conversion for coastal trade now to be charged on proportionate basis depending on the period for which they operate as coastal vessels in India; (iv) Full exemption from SAD extended to import of dredgers.

7. **ENVIRONMENT PROTECTION:** (i) Equipment for setting up of solar projects fully exempted from SAD; (ii) Concessional rate of 5 per cent basic customs duty extended to raw materials for the manufacture of intermediates, parts, and sub-parts of blades for rotors for wind energy generators; (iii) Full exemption from basic customs duty extended to tri band phosphor for use in the manufacture of compact fluorescent lamps; (iv) Full exemption from basic customs duty and SAD along with 6 per cent CVD available to specified parts for the manufacture of hybrid vehicles extended to some additional parts; (v) The customs duty regime of 6 per cent CVD and nil SAD extended to lithium ion batteries for the manufacture of battery packs for supply to electric or hybrid vehicle manufacturers.

8. **HEALTH/NUTRITION:** (i) Basic customs duty reduced from 5 per cent to 2.5 per cent on iodine; (ii) Basic customs duty reduced on isolated soya protein and soya protein concentrate from 15 per cent and 30 per cent respectively to 10 per cent; (iii) Basic customs duty reduced from 10 per cent to 5 per cent on probiotics; (iv) Customs duty on six specified lifesaving drugs/vaccines and their bulk drugs reduced from 10 per cent to 5 per cent with nil CVD; (v) A concessional import duty regime of 2.5 per cent basic customs duty with 6 per cent CVD/excise duty and nil SAD prescribed for specified raw materials for the manufacture of syringes, needles, catheters, cannulas subject to actual user condition. (vi) A concessional import duty regime of 2.5 per cent basic customs duty with 6 per cent CVD and nil SAD extended to parts and components for the manufacture of blood pressure monitors and blood glucose monitoring systems (glucometers); (vii) Full exemption from basic customs duty and CVD extended to steel tube and wire, cobalt chromium tube, Hayness Alloy-25, and polypropylene mesh for the manufacture of coronary stents/coronary stent systems and artificial heart valves subject to actual user condition.

9. **TEXTILES:** (i) Basic customs duty on new shuttle-less looms, along with parts and components for their manufacture reduced from 5 per cent to nil; (ii) Basic customs duty on new automatic silk-reeling and -processing machinery and raw silk testing equipment reduced from 5 per cent to nil; (iii) The concessional rate of basic customs duty of 5 per cent restricted only to new textiles machinery; (iv) Basic customs duty on wool waste and wool tops reduced from 10 per cent and 15 per cent respectively to 5 per cent; (v) Basic customs duty on titanium dioxide reduced from 10 per cent to 7.5 per cent; (vi) Full exemption from basic customs duty extended to Aramid yarn and fabric when used in the manufacture of bulletproof helmets for supply to defence and police.

10. **ELECTRONICS/ HARDWARE:** (i) Full exemption from basic customs duty provided to LCD and LED TV panels of 19 inches and above; (ii) LEDs required for the manufacture of LED lamps exempted from SAD; (iii) The scope of full exemption from basic customs duty, CVD, and SAD extended to parts of memory cards until March 2013; (iv) Full exemption from basic customs duty currently available to copper, brass, phosphor bronze strips, and similar items imported for the manufacture of connectors withdrawn; (v) Full exemption from basic customs duty currently available to poly-laminated aluminum tape and poly-laminated steel tape if imported for the manufacture of cables and conductors for telecom use withdrawn.

11. **EXPORT PROMOTION:** (i) Basic customs duty reduced from 10 per cent to 5 per cent on marine seawater pumps with fibre impellers and automatic fish/prawn feeders for aquaculture; (ii) Basic customs duty on artemia reduced from 30 per cent to 5 per cent.

12. **PAPER:** Waste paper fully exempted from basic customs duty.

13. **SAD:** Brass scrap and timber logs fully exempted from SAD.

14. **MISCELLANEOUS:** (i) A basic customs duty of 10 per cent imposed on digital still cameras of certain specifications; (ii) Basic customs duty on boric acid increased from 5 per cent to 7.5 per cent; (iii) Basic customs duty on boiler quality tubes and pipes for the manufacture of boilers reduced from 10 per cent to 7.5 per cent subject to end-use condition; (iv) A concessional customs duty of 5 per cent basic customs duty + 6 per cent CVD+ nil SAD prescribed for imports of hydrophilic non-woven, hydrophobic non-woven, and super absorbent polymer for manufacture of adult diapers subject to actual user condition; (v) Full exemption from customs duty withdrawn from mega/ultra mega power projects except 113 specified projects.

Collection Rates

3.20 Given the large number of exemptions to the application of statutory rate of customs, the increase in value of imports does not necessarily imply similar magnitude in customs revenue. Collection rates are an indicator of overall incidence of customs tariffs including countervailing and special additional duties of imports. These are computed as the ratio of revenue collected from these duties to the aggregate value of imports in a year (or period) and thus represent trade-weighted tariffs. The trends in the rates for important commodity groups as well as for all commodities taken together over the years are shown in Table 3.5. A major reason for the fall in rates has been the lower levels of duties on many items including on petroleum, oil, and lubricants (POL), which has significant import value and of course the impact of the various exemptions. At overall level, the effective rate of taxes at around 6 per cent in 2011-12 as against the level of simple average tariff rates of basic customs duties and the CVD indicates the impact of exemptions.

Service Tax

3.21 In 2011-12, growth in service tax revenue was 37.4 per cent amounting to ₹ 97,579 crore, which indicated that service tax has been emerging as an important source of revenue. Budget 2012-13 envisaged a growth of 30.5 per cent in the revenue from service tax vis-à-vis 2011-12 (RE). This was based on the increase in the rate from the existing 10 per cent to 12 per cent and a change in the tax base (Table 3.6). As against the usual practice of expanding the list of services, the Budget for 2012-13 introduced a 'negative list' approach effective 1 July 2012. For operationalizing the negative list approach, a number of changes have been made in Chapter V of the Finance Act 1994 (when service tax was initially introduced). Service of transportation of passengers with or without accompanied belongings by railways in first class or an air conditioned coach and services by way of transportation of goods by railways has been subjected to service tax effective October 1, 2012. Following the revision in the rate of service tax, changes have also been made in specific and compounding rates of tax for services in relation to purchase and sale of foreign currency including money changing; promotion, marketing, organizing, or in any manner assisting in organizing lottery; and reversal of Cenvat credit under rule 6(3)(i).

3.22 A number of amendments in the Finance Act 1994 and changes in the rules governing the levy of

Table 3.5 : Collection Rates for Selected Import Groups*

(in per cent)

Sl. No.	Commodity Groups	2006-7	2007-8	2008-9	2009-10	2010-11	2011-12
I	POL	5	6	3	2	6	3
II	Non-POL	12	13	9	8	9	7
	of which:						
	1. Food products	23	19	4	3	3	3
	2. Chemicals	22	22	16	14	17	14
	3. Man-made fibres	28	30	17	22	30	22
	4. Paper & newsprint	10	10	8	8	8	7
	5. Natural fibres	12	13	6	4	5	3
	6. Metals	24	24	17	17	22	20
	7. Capital goods	14	16	13	11	13	12
	8. Others	6	6	4	4	4	4
III	**Total**	10	10	7	6	8	6

Source **: Department of Revenue, Ministry of Finance**

*** Collection rate is defined as the ratio of revenue collection (basic customs duty + countervailing duty) to value of imports unadjusted for exemptions, expressed in percentage.**

Notes **: S.No. 1 includes cereals, pulses, tea, milk and cream, fruits, vegetables, animal fats, and sugar.**
S.No. 2 includes chemical elements, compounds, pharmaceuticals, dyeing and colouring materials, plastic, and rubber.
S.No. 4 includes pulp and waste paper, newsprint, paperboards and manufactures, and printed books.
S.No. 5 includes raw wool and silk.
S.No. 6 includes iron and steel and non-ferrous metals.
S.No. 7 includes non-electronic machinery and project imports, electrical machinery.

Table 3.6 : Service Tax: A Growing Revenue Source

Year	No. of services	Tax rate in per cent	Revenue (₹ crore)	Growth over previous year in per cent
2004-5	75	10	14200	80.0
2005-6	78	10	23055	62.4
2006-7	92	12	37598	63.1
2007-8	98	12	51301	36.4
2008-9	106	12*	60941	18.8
2009-10	109	10	58422	-4.1
2010-11	117	10	71016	21.6
2011-12(P)	119	10	97579	37.4
2012-13 (April- December)@	Negative list#	12	80927	33.0

Source **: Receipts Budget and Controller General of Accounts.**

*** Reduced to 10% w.e.f. 24 February 2009.**
@ Growth for 2012-13 (April-December) is over corresponding period previous year.
 # Shifted to negative list approach w.e.f 1 July 2012.

service tax have been made. These include: the Place of Provision of Service Rules 2012; new reverse charge mechanism; Cenvat Credit Rules 2004; Service Tax Rules 1994; and Point of Taxation Rules 2011 (Box 3.3).

Tax Expenditure

3.23 There is significant divergence between the statutory rates of taxes as notified in the various schedules and the actual or effective rate of taxation, which is essentially a simple ratio of tax revenue collected to the tax base. This arises on account of the exemptions to the tax rate specified in the schedule. As indicated earlier in the section on collection rates, the magnitude of revenue foregone (tax expenditure) is indeed high. In the Receipts Budget for 2012-13, tax foregone on account of exemptions under corporate income tax for 2010-11 and 2011-12 was estimated at ₹ 57,912 crore and ₹ 51,292 crore respectively net of MAT. In the case of corporate taxpayers, deduction on account of accelerated depreciation, deduction for export profits of export-oriented units located in special economic zones (SEZs) and profits of businesses in the power and telecom sectors were some of the major incentives. The absolute amount of deductions has decreased as a result of phasing out of profit-linked deductions. Further, the levy of MAT has led to a higher effective rate of taxation in the case of corporates from 20.55 per cent for 2006-7 to 24.1 per cent for financial year 2010-11. Tax forgone on account of exemptions under personal income tax for individual taxpayers was estimated at ₹ 30,653 crore and ₹ 35,698 crore respectively in 2010-11 and 2011-12. The bulk of the revenue foregone under personal income tax was on account of the exemptions given for certain investments and payments under section 80 C of the Income Tax Act.

3.24 In so far as indirect taxes are concerned, revenue forgone is defined as the difference between duty that would have been payable but for the issue of exemption notification and actual duty paid in terms of the relevant notification. The revenue forgone for financial year 2011-12 in respect of excise duties is estimated at ₹ 2,12,167 crore including ₹ 12,880 crore on account of area-based exemptions. Duty forgone for the year 2010-11 on account of all the exemption notifications on customs was estimated at ₹ 2,30,131 crore as against the duty forgone of ₹ 2,33,950 crore in 2009-10. This is projected to rise to ₹ 2,76,093 crore in 2011-12. All these estimates are based on certain assumptions and have to be interpreted with caution and the actual outcome in dynamic markets with different elasticities for different products may turn out to be very different.

Box 3.3 : Changes in Service Tax

1. **PLACE OF PROVISION OF SERVICES RULES 2012:** An important component of the changes is the introduction of the Place of Provision of Services Rules 2012. The new rules have replaced the existing Export of Services Rules 2005 and the Taxation of Services (Provided from Outside India and Received in India)Rules 2006. Rule 5 of the export rules has been incorporated in Service Tax Rules.

2. **AMENDMENTS IN THE FINANCE ACT 1994:** Chapter V of the Finance Act 1994 has been amended to: (i) Prescribe that the value of taxable service (particularly in the case of import and export of taxable services)and the rate of tax shall be determined in terms of Point of Taxation Rules 2011; (ii) Introduce provisions relating to special audit in the service tax law on the lines of the Central Excise Act 1944. Now special audit can be ordered under specified circumstances. Consequently, section 14AA has been omitted from section 83; (iii) Increase the one-year time limit for issuance of notice for specified category of offences prescribed under section 73(1)of the Finance Act 1994 to 18 months. A new sub-section (1A)has been inserted in section 73 of the Finance Act 1994 to prescribe that follow-on notices issued on the same grounds need not repeat the grounds but only state the amount of service tax chargeable for the subsequent period. Statement of tax due for the subsequent period, served on the assessees with reference to the earlier demand notice, will be deemed as a notice under section 73(1)of the Finance Act 1994; (iv) Make Settlement Commission provisions applicable to service tax in line with the similar provisions contained in the Central Excise Act 1944; (v) Make the revision mechanism prescribed in section 35EE of the Central Excise Act 1944 applicable to service tax to the extent possible; (vi) Amend sections 85 and 86 on the lines of sections 35 and 35E of the Central Excise Act so as to harmonize the limitation for filing assessee's appeal before Commissioner (Appeals)and revenue appeal before the Tribunal; (vii) Obtain powers (a) to provide for the manner of compounding and to specify the amount of compounding of offences along the lines of Central Excise (Compounding of Offences)Rules 2005; (b) to provide for rules for settlement of cases along the lines of Central Excise.

3. **NEW REVERSE CHARGE MECHANISM:** (i) Section 68(2) of the Finance Act,1994 has been amended to put the onus of payment of service tax on reverse charge basis partly on service provider and partly on service receiver. The scheme has been made applicable on three specific services, i.e. hiring of means of transport; construction; and manpower supply and security services; (ii) Consequent to the above change, suitable amendment has also been made in the concept of 'person liable to pay' provided in Rule 2(1)(d) of Service Tax Rules 1994.

4. **RENTING OF IMMOVABLE PROPERTY SERVICE:** Constitutional validity of the levy of service tax on renting of immovable property had been the subject matter of litigation leading to pronouncement of court judgments favourable to revenue, including those of Hon'ble Delhi High Court and Hon'ble Supreme Court. Taking an overall view, the government has decided to waive the penalty for those taxpayers who pay the service tax due on the renting of immovable property service (as on 6.3.2012), in full along with interest. For this purpose, a new section 80A has been inserted in the Finance Act 1994. This scheme of penalty waiver was open only for a period of six months from the date of enactment of the Finance Bill 2012.

5. **AMENDMENTS IN RULES:** (i) Cenvat Credit Rules 2004 have been amended as follows: (a) Existing rule 5 replaced with a new rule to simplify the procedure for refund of unutilized credit on account of exports; (b) Credit allowed on motor vehicles (except those under heading nos 8702, 8703, 8704, 8711 and their chassis). The credit of tax paid on the supply of such vehicles on rent, insurance, and repair is also allowed; (c) Credit of insurance and service station service is allowed to insurance companies in respect of motor vehicles insured and re-insured by them; and manufacturers in respect of motor vehicles manufactured by them; (d) Rules 4(1)and 4(2)amended to allow a service provider to take credit of inputs or capital goods whenever the goods are delivered to him, subject to specified conditions. (e) Rule 7 for input service distributors amended to provide that credit of service tax attributable to service used wholly in a unit should be distributed only to that unit and that the credit of service tax attributable to service used in more than one unit should be distributed prorata on the basis of the turnover of the concerned unit to the sum total of the turnover of all the units to which the service relates. (f) Rule 9(1)(e)amended to allow availment of credit on the tax payment challan in case of payment of service tax by the service receiver on reverse charge basis.

   (ii) Service Tax Rules, 1994 has been amended as follows: (a) The time period provided in rule 4A for issuance of invoice increased to 30 days. For banks and financial institutions providing banking and other financial services, the period is 45 days; (b) Rule 6(4A)amended to allow unlimited amount of permissible adjustments. (c) In case of export and individuals and firms rendering eight specified services, the point of taxation shifted from the Point of Taxation Rules to the Service Tax Rules. (d) In case of exporters, the period extended by the Reserve Bank of India (RBI)on specific requests included in the period for which the tax liability is allowed to be deferred. (e) The option of deferred payment allowed for all service providers rather than for specific services. The facility is available only to individuals and partnership firms (including limited liability partnership)up to a turnover of taxable services of ₹ 50 lakh subject to the condition that their turnover of taxable services in previous year was below ₹ 50 lakh. For computing the above limits, the turnover of the whole entity is required to be summed up and not any single registration.

   (iii) Point of Taxation Rules 2011 have been amended to : (a) Change the definition of continuous supply of service to capture the entire dimension of the concept, viz. the recurrent nature of services and the obligation for payment periodically or from time to time; (b) Omit rule 6 in respect of continuous supply of service and merge it with rule 3. Rules 4 and 5, which deal with situations covering change in effective rate of tax and taxation of new services, are now applicable to continuous supply of services also; (c) Define the date of payment; (d) Give an option to determine the point of taxation in respect of advances up to ₹ 1000 received in excess of the amount indicated in the invoice, on the basis of invoice or completion of service rather than payment; and (e) Incorporate a new residual rule to ascertain point of taxation in cases where the same could not be ascertained by the rules prescribed.

Nevertheless, there is merit in limiting the exemptions or their grandfathering on a case-by-case basis so as to realize fuller tax potential through a wider tax base.

Non-tax revenue

3.25 Non-tax revenues grew at a compound annual rate of 7.6 per cent in the 10 years ending 2009-10. The spurt in 2010-11 owed to higher-than-budgeted realization from the proceeds of auction of telecom 3G/broadband wireless access spectrum. As against the estimated revenue of ₹ 1,25,435 crore in 2011-12 (BE), the realization fell marginally short at ₹ 1,24,307 crore notwithstanding the fact that the auctions of telecom spectrum and phase III FM Radio which were to bring in ₹ 14,600 crore could not take place. Budget 2012-13 estimated a growth of 32.0 per cent over 2011-12 (RE) in non-tax revenue mainly on account of estimated receipts of ₹ 40,000 crore from the telecom spectrum auction. As the 2G telecom spectrum auction elicited lukewarm response on account of the high reserve price in the current year, the government has revised the reserve price downwards. As such, the proceeds from this component are as yet an important risk to the actual fiscal outcome for 2012-13. The other main component is dividends and profits, which have also in the past exhibited sluggish growth.

Non-debt capital receipts

3.26 Recoveries of loans and disinvestment are the two key receipts of the non-debt capital variety. As against ₹ 16,897 crore in 2011-12 (provisional actuals), Budget 2012-13 has placed recoveries of loans at ₹ 11,650 crore this year. The 12th Finance Commission's recommendation against loan intermediation from the centre to states coupled with the fact that such recoveries of loan have become a minor source in the receipts side has resulted in disinvestment assuming greater importance in comparison. As against ₹ 40,000 crore budgeted under disinvestment in 2011-12, actual receipts were ₹ 15,622 crore on account of the subdued financial market conditions. The Budget for 2012-13 has estimated that ₹ 30,000 crore would accrue in 2012-13. In April-December 2012, receipts under this head were ₹ 8,178 crore. The government has taken several steps to expedite the process of disinvestment. The Cabinet Committee on Economic Affairs has approved disinvestment in the following:—

(a) Disinvestment of 9.33 per cent paid up equity of Minerals and Metals Trading Corporation (MMTC) Ltd out of the Government of India's holding of 99.33 per cent through an offer for sale of shares through stock exchanges, as per the Securities and Exchange Board of India (SEBI) Rules and Regulations.

(b) Disinvestment of 10 per cent paid up equity of Oil India Ltd. (OIL) out of the Government of India's holding of 78.43 per cent through an offer for sale of shares through stock exchanges as per SEBI Rules and Regulations.

(c) Disinvestment of 12.15 per cent paid up equity in National Aluminium Company Limited.

(d) Disinvestment of 9.59 per cent equity in Hindustan Copper Limited.

(e) Disinvestment of 9.50 per cent paid up equity capital in the National Thermal Power Corporation (NTPC) Ltd out of the Government of India's shareholding of 84.50 per cent. The Cabinet Committee on Economic Affairs has approved disinvestment of 9.50 per cent equity of NTPC Ltd, out of its holding of 84.50 per cent through an offer for sale of shares through stock exchanges as per SEBI Rules and Regulations.

(f) Exchange-traded fund (ETF) for the stocks of the listed central public-sector enterprises (CPSEs) is also being proposed.

Actual revenue outcome in 2012-13 vis-à-vis Budget Estimates

3.27 Against the estimated growth in non-debt receipts discussed in the previous section in terms of various taxes, non-tax revenue, and disinvestment receipts, the actual outcome in the first nine months of the current fiscal indicates the challenge in marksmanship for this year (Table 3.7). Gross tax revenue in April-December 2012 has grown year-on-year by 15 per cent to reach ₹ 6,81,345 crore. While this level of growth is much higher than that of 12.2 per cent in April-December 2011, it falls significantly short of the growth envisaged by BE 2012-13. As a proportion of BE, gross tax revenue

in April-December 2012 was 63.2 per cent, lower than the last five-years' average of 69.0 per cent. This level of growth in April-December 2012 comprises a growth of 17.4 per cent in union excise duties; 6 per cent in customs; 22.5 per cent in personal income tax; 33 per cent in service tax; and 10.6 per cent in corporate income tax. In terms of the implied year-on-year growth envisaged by BE 2012-13 over provisional actuals of 2011-12, there is slippage in the first nine months of the current fiscal in corporate income tax by 4.9 percentage points, customs by 18.9 percentage points, and central excise by 16 percentage points. There is overperformance in service tax collection by 5.9 percentage points and personal income tax by 7.6 percentage points. In terms of overall gross tax revenue the slippage is 6 percentage points in April-December 2012. Based on the observed collection in the last quarter of the previous year, the slippage in tax revenue collection could be lowered with some additional efforts.

3.28 Apart from these, non-tax revenue in April-December 2012 is placed at ₹ 86,380 crore, which is 52.5 per cent of BE, well below the last five years' average. This outcome is because of the lower realization from auction of 2G spectrum thus far. In non-debt capital receipts, there is significant shortfall as of April-December 2012 on account of disinvestment receipts, as only ₹ 8,178 crore of the budgeted amount of ₹ 30,000 crore has been realized. Thus the overall outcome in terms of non-debt receipts was ₹ 5,86,424 crore in April-December 2012, which is 60.0 per cent of the BE, indicating the stiff challenge in the fourth quarter of the current fiscal for better marksmanship.

Table 3.7 : Central Government Finances

	Budget Estimates 2012-13	April-December 2011-12	April-December 2012-13	Col.(4) as % of (2) 2012-13 (BE)	Per cent change over 2011-12 Col.(4) over (3)
(1)	(2)	(3)	(4)	(5)	(6)
		(₹ crore)			
1. Revenue receipts [(ii)+(iii)]	**935685**	**498491**	**570536**	**61.0**	**14.5**
(i) Gross tax revenue	1077612	592348	681345	63.2	15.0
(ii) Tax (net to Centre)	771071	420414	484156	62.8	15.2
(iii) Non-tax revenue	164614	78077	86380	52.5	10.6
2. Capital receipts	**555241**	**397870**	**420587**	**75.7**	**5.7**
(i) Recovery of loans	11650	14115	7710	66.2	-45.4
(ii) Other receipts	30000	2743	8178	27.3	198.1
(iii) Borrowings and other Liabilities	513590	381012	404699	78.8	6.2
3. Total receipts (1+2)	**1490925**	**896361**	**991123**	**66.5**	**10.6**
4. Non-Plan expenditure [(i)+(ii)]	**969900**	**619457**	**695233**	**71.7**	**12.2**
(i) Revenue account	865596	550692	625598	72.3	13.6
of which:					
Interest payments	319759	179429	201959	63.2	12.6
Major subsidies	179554	104181	166824	92.9	60.1
Pensions	63183	40454	44839	71.0	10.8
(ii) Capital account	104304	68765	69635	66.8	1.3
5. Plan expenditure (i)+(ii)	**521025**	**276904**	**295890**	**56.8**	**6.9**
(i) Revenue account	420513	233903	242975	57.8	3.9
(ii) Capital account	100512	43001	52915	52.6	23.1
6. Total expenditure [(4)+(5)=(i)+(ii)]	**1490925**	**896361**	**991123**	**66.5**	**10.6**
(i) Revenue expenditure	1286109	784595	868573	67.5	10.7
of which:					
Grants for creation of capital assets	164672	84149	74283	45.1	-11.7
(ii) Capital expenditure	204816	111766	122550	59.8	9.6
7. Revenue deficit	**350424**	**286104**	**298037**	**85.1**	**4.2**
8. Effective revenue deficit	**185752**	**201955**	**223754**	**120.5**	**10.8**
9. Fiscal deficit	**513590**	**381012**	**404699**	**78.8**	**6.2**
10. Primary deficit	**193831**	**201583**	**202740**	**104.6**	**0.6**

Source **: Controller General of Accounts, Ministry of Finance.**

Expenditure trends

3.29 Given the large unmet minimum needs of development, and factoring in the resource availability, the annual budgets estimate the expenditure to be incurred for the year with due consideration to the level of fiscal deficit that is required under the FRBM mandate. Rapid reduction in expenditure as part of fiscal consolidation is constrained by the level of committed expenditure on interest payments, defence, civil service pay and pensions, etc., which appropriate large part of the revenue receipts on the one hand, and the need to step up development expenditure that is so critical for raising the level of welfare of the masses on the other. Thus the annual budget has to maintain a delicate balance between the need to reduce the expenditure that is perceived as non-developmental, given the structural rigidities in the key expenditure components and the needs for raising the levels of development expenditure for inclusive growth. It is in this context successive budgets have focused on reprioritization of expenditure.

3.30 In the post-FRBM period prior to the global crisis, total expenditure as a proportion of GDP was brought down from 15.4 per cent in 2004-5 to 13.6 per cent in 2006-7. Following the global crisis and the fiscal stimulus that followed, this proportion rose in excess of 15.7 per cent in 2008-9 and 15.8 per cent in 2009-10. Notwithstanding the significant fiscal consolidation achieved in 2010-11 when the stimulus measures were partially rolled back, total expenditure as a proportion of GDP was placed at 15.4 per cent, which was possible due to the one-off nature of surge in non-tax revenues from 3G/BWA telecom spectrum auction/proceeds as well as high levels of nominal GDP. Going forward, fiscal marksmanship in expenditure will depend on the emerging trends in key components that are discussed in the following paragraphs.

Subsidies

3.31 As indicated earlier, while the Budget for 2011-12 had estimated total expenditure to be contained at 14.0 per cent of GDP, there was an overshooting on account of the high global oil prices and the insufficient pass through to domestic oil and fertilizer prices. The overshooting of expenditure on subsidies was also because of the accounting changes which placed all subsidies 'above the line'. The Budget for 2012-13 estimated growth in total expenditure at 13.1 per cent over 2011-12 (RE) and sought to restrict expenditure on subsidies to 2 per cent of GDP. As against a provision of ₹ 23,640 crore in 2011-12 for oil subsidies, the Budget for 2012-13 provisioned an amount of ₹ 43,580 crore assuming a certain level of global crude oil price. It must be noted that oil subsidies are paid to the oil marketing companies (OMC) on a calendar-year basis because only after quarterly results are declared is the subsidy released.

3.32 In the event, the Indian basket crude oil was $107.52 per bbl (April-December) in 2012 and even with the pass through effected in the course of the year, under-recoveries of OMCs surged and were estimated at ₹ 1,24,854 crore during April-December 2012-13. As the bulk of the under-recoveries is accounted for by two subsidized products, viz. diesel and LPG, the government raised diesel prices by ₹ 5 per litre and capped the subsidized cylinders at six per connection per year in September 2012. With continued rise in prices, on January 17, 2013 the government further permitted OMCs to raise diesel prices in small measures periodically. However, in order to protect household budgets, it simultaneously raised the annual LPG cap from six to nine cylinders per connection.

3.33 The high level of global crude oil prices also has a significant bearing on the level of fertilizer subsidies because it is not only a key input as feedstock, but also because there is inadequate pass through in urea (the major domestic fertilizer) prices. Subsidy on fertilizers had increased substantially from ₹ 32,490 crore in 2007-8 to reach ₹ 67,199 crore in 2011-12 (RE). It is budgeted at ₹ 60,974 crore in 2012-13. The government has been calibrating pricing policies to address the issue of burgeoning fertilizer subsidies. One of the important decisions taken was to fix per tonne subsidy on key non-nitrogenous fertilizers, thereby limiting the increase in subsidy outgo to the extent of increase in consumption.

3.34 Another major subsidy outgo in recent years, growing at an annual average rate of 25.4 per cent in the last five years ending 2011-12, is on account of food. While the targeted public distribution system (TPDS) accounts for the bulk of the food subsidy outgo, there are other welfare schemes under which food subsidy is provided. A part of the subsidy outgo

also owes to the carrying cost of the buffer stock, which has mounted in recent years. In terms of the merits of subsidization, priority needs to be accorded to food subsidy in view of the under-consumption of basic food by the poor and the extent of malnutrition in the country. The government has sought to correct this through the National Food Security Act (see Chapter 8), though concerns have been expressed that this will lead to a higher subsidy outgo. However, as indicated earlier, it is a part of the challenge of prioritization to provide for this basic minimum need even as other items of expenditure are minimized. Further, there is need for better targeting of subsidies and for reducing leakages involved in their delivery. Direct benefit transfer (DBT) (Box 3.4) is one such initiative.

Interest payments

3.35 The cumulative impact of the level of deficit and debt is reflected in the interest payments outgo. As a proportion of GDP, interest payments fell in the post FRBM period and have continued to be low at around 3.1 per cent in recent years notwithstanding the rise in fiscal deficit. A part of this owed to lower growth in interest payments vis-à-vis nominal GDP. As against an average annual growth of 12.7 per cent in interest payments in the last five years ending 2011-12, annual average nominal GDP growth was 15.9 per cent. It would be instructive to note that the base for interest payments is the cumulative debt in the previous year plus the incremental assumption of debt in the current year. The average cost of borrowing thus measured is placed at 7.9 per cent in 2011-12 (RE) and was budgeted to remain at the same level in 2012-13 (Table 3.8)

Table 3.8 : Interest on Outstanding Internal Liabilities of Central Government

	Outstanding Internal Liabilities (end-March)	Interest on Internal Liabilities	Average Cost of Borrowings (per cent per annum)
	(₹ crore)		
2004-5	1603785	105176	7.2
2005-6	1752403	111476	7.0
2006-7	1967870	128299	7.3
2007-8	2247104	149801	7.6
2008-9*	2565991	170388	7.6
2009-10	2874683	192567	7.5
2010-11	3212521	212707	7.4
2011-12(RE)	3738151	253995	7.9
2012-13(BE)	4284660	296940	7.9

Source: Union Budget documents.

Notes:* Excludes ₹ 563 crore towards premium on account of domestic debt-buyback scheme and prepayment of external debt.

1. Average cost of borrowing is the percentage of interest payment in year 't' to outstanding liabilities in year 't-1'.
2. Outstanding internal liabilities exclude National Small Savings Funds (NSSF) loans to states,with no interest liability on the part of the centre.
3. The figures for interest payments reported in the earlier issues may differ as these figures are net of interest payments on NSSF paid by the government since 1999-2000, i.e. the constitution of the NSSF.

Pay allowances and pension

3.36 Pay and allowances constituted 0.9 per cent of GDP in 2007-8, rising to 1.4 per cent of GDP in 2009-10 on account of the implementation of the

Box 3.4 : Direct Benefit Transfer (DBT)

The DBT plan was introduced on 1 January 2013 with seven schemes in 20 districts. India has embarked on a DBT scheme in selected districts wherein it has been envisaged that benefits such as scholarships, pensions, and MGNREGA (Mahatma Gandhi National Rural Employment Guarantee Act) wages will be directly credited to the bank or post office accounts of identified beneficiaries. The DBT scheme will not substitute entirely for delivery of public services for now. It will replace neither food and kerosene subsidies under the TPDS nor fertilizer subsidies. The DBT is designed to improve targeting, reduce corruption, eliminate waste, control expenditure, and facilitate reforms. Electronic transfer of benefits is a simple design change and transfers that are already taking place through paper and cash mode will now be done through electronic transfers. This has been enabled by rapid roll out of Aadhar (Unique Identity) now covering 200 million people and rapidly growing to cover 600 million (nearly half of our population), with the National Population Register covering the other half of the populace. The DBT in tandem with such unique identification will ensure that the benefits reach the target groups faster and minimize inclusion and exclusion errors as well as corruption that are associated with manual processes.

award of the Sixth Central Pay Commission. At 1.1 per cent of GDP in 2011-12 (BE), there has been some moderation. Similarly, pension constituted 0.5 per cent of GDP in 2007-8 and rose to 0.9 per cent in 2009-10; it is placed at 0.6 per cent in 2011-12. A longer time trend analysis reveals that growth in pensions was very modest prior to 2004-5 and subsequently picked up due to the impact of the contributory scheme introduced for fresh entrants to government service in addition to the outgo under the earlier pension scheme with undefined contribution. In tandem with pay and allowances, pensions also grew sharply in 2008-9 and 2009-10, reflecting the impact of the Sixth Pay Commission.

Central Plan Outlay

3.37 Plan outlay comprises gross budget support (GBS) for Plan (central Plan plus central assistance to states/ union territories [UTs]) and internal and extra budgetary resources of the central public-sector enterprises (CPSEs). The Twelfth FiveYear Plan envisages GBS of 5.25 per cent of GDP. The Budget for 2012-13 placed Central Plan outlay at ₹ 6,51,509 crore as against ₹ 5,58,172 crore in 2011-12 (RE). GBS for Plan is placed at ₹ 3,91,027 crore in BE 2012-13.

3.38 Broad sector-wise, the following are the allocations as a proportion of the total outlay: energy (23.8 per cent); social services (27.5 per cent); transport (19.2 per cent); communication (2.4 per cent); rural development (7.8 per cent); agriculture and allied activities (2.7 per cent); and irrigation and flood control (0.2 per cent). Central assistance to state and UT plans is placed at ₹ 1,29,998 crore in BE 2012-13. Reprioritization of expenditure from non-Plan to Plan would be critical in meeting the proposed Twelfth Plan outlay.

Supplementary Demands for Grants

3.39 Given the constitutional provision that no expenditure can be incurred without Parliamentary sanction, additionalities of expenditure over BE have to be made through supplementary demands for grants. Supplementary demands for grants arise on account of two factors, viz. fresh proposals that were not envisaged at the time of the BE and the additional expenditure arising out of underprovisioning in the BE under various heads. A part of the additionalities are met through re-appropriations from one budget head to another, which implies no net cash outgo, and through additional demands entailing cash outgo. The extent of the latter has implications for overall fiscal marksmanship.

3.40 In recent years, underprovisioning of petroleum and fertilizer subsidies has been an important reason for supplementary demands for grants with a cash outgo. In 2011-12, out of the three supplementary demands for grants with cash outgo that were presented, about 60.7 per cent was on account of petroleum and fertilizer subsidies. In 2012-13, only one supplementary demand for grants has been presented. Of the demands involving net cash outgo of ₹ 30,804.13 crore, ₹ 28,500 crore was the outgo on account of compensation for the under-recoveries of the OMCs and ₹ 2,000 crore on account of equity infusion for the Turn Around Plan and Financial Restructuring Plan of Air India.

Economic and Functional Classification

3.41 While the conventional analysis of the trends in expenditure, revenue, and deficits is useful for understanding the trends in public finances, the macroeconomic impact of fiscal policies is best understood in terms of a national accounting framework. But the latter comes out with some time lag. It is here that the economic and functional classification of the central government Budget is useful. Such an analysis of the central government Budget indicates that out of the total expenditure of ₹ 12,88,763 crore in 2011-12 (RE), consumption expenditure was ₹ 2,56,898 crore and expenditure on gross capital formation ₹ 70,050 crore (Appendix Table 2.21). Financial investments and loans to the rest of the economy were ₹ 46,149 crore. With the rest of the expenditure being transfer payments, such financial transfers were 71.0 per cent of total expenditure. In 2012-13 (BE), out of total estimated expenditure of ₹ 14,97,636 crore, consumption expenditure is placed at ₹ 2,90,124 crore and gross capital formation ₹ 94,906 crore. Transfer payments to the rest of the economy at ₹ 10,10,950 crore constituted 67.5 per cent of the total expenditure.

3.42 In terms of classification by functional heads, social and economic services (broadly covering the total development outlays) at ₹ 6,41,944 crore constituted 42.9 per cent of the total expenditure of ₹ 14,97,636 crore in 2012-13 (BE). Expenditure on

general services is estimated at ₹ 3,49,199 crore, constituting 23.3 per cent of the total. Such items as statutory grants-in-aid to states, non-Plan grants to UTs, food and other consumer subsidies, interest on public debt, pension, and aid to other nations constitute the unallocable category accounting for 33.8 per cent of the total expenditure. The salient feature of the economic and functional classification of the Central Budget 2012-13 is the estimated growth in capital formation (including financial assistance for capital formation) which is placed at 22.9 per cent and growth of 16.2 per cent in social services in 2012-13 (BE) over 2011-12 (RE), indicating the thrust of the Budget on higher investment and an inclusive development agenda.

Expenditure outcome in 2012-13

3.43 As against implied year-on-year growth of 14.8 per cent envisaged by BE 2012-13 (over provisional actuals of 2011-12), growth in total expenditure in April-December 2012 has been 10.6 per cent only (see Table 3.7). Non-Plan revenue expenditure in April-December 2012 is placed at 72.3 per cent of BE, which is well below the five-year average of 77.7 per cent. Similarly expenditure on both Plan revenue as well as Plan capital expenditure in April-December 2012 is well below the five-year average as proportions of BE. However, major subsidies have burgeoned in April-December 2012 to reach a figure of ₹ 1,66,824 crore (92.2 per cent of BE). The expenditure restraint has helped keep deficits lower in April-December 2012.

Deficit outcome in 2012-13

3.44 The Budget for 2012-13 estimated a deficit level of ₹ 5,13,590 crore. The net outcome of slippage in non-debt receipts and expenditure restraint fed into the outcome in terms of the desired indicators of revenue deficit as well as fiscal deficit in April-December 2012. As a proportion of BE, fiscal deficit is placed at 78.8 per cent, significantly below the five-year average of 85.9 per cent and last year's level of 92.3 per cent. Similarly, revenue deficit is placed at 85.1 per cent, well below the level achieved in the recent past. However, the indicator effective revenue deficit is placed at 120.5 per cent in April-December 2012. Though it is below last year's level in the same period, it is a slippage and owes to lower outgo of grants for creation of capital assets.

Government debt

3.45 The high levels of fiscal deficit in the post-crisis period added to the overall debt burden of the central government. Prolonged fiscal deficits lead to accumulation of debt beyond levels sustainable for an economy and can result in higher real and nominal interest rates, slower growth in capital formation, and potentially lower the rate of output growth. The outstanding liabilities of the central government were placed at ₹ 44,68,714 crore, equivalent of 49.8 per cent of GDP at end-March 2012 (Table 3.9). As a proportion of GDP, outstanding liabilities (adjusted) of the centre peaked at 67.0 per cent in 2002-3 and have fallen subsequently notwithstanding the rise in fiscal deficit in the post-crisis years. This is on account of the fact that growth in incremental assumption of liabilities has been lower than that of nominal GDP and the debt to GDP ratio dynamics is aided by the differential between nominal GDP growth and nominal interest rates, which makes it possible to achieve a greater reduction through a given primary balance.

3.46 The total liabilities for the Government of India include debt and liabilities accounted for in the Consolidated Fund of India (technically defined as public debt) as well as liabilities accounted for in the public account. Public debt constitutes 76.3 per cent of total liabilities at end March 2012. It is further classified into internal and external debt. Internal debt, constituting 90.9 per cent of public debt, largely consists of fixed tenor, fixed coupon dated securities (72.1 per cent) and treasury bills (10.2 per cent). State governments are not allowed to directly borrow externally hence their entire debt is domestic. Over time, there is a compositional shift toward marketable debt, while the public account liabilities have seen a commensurate decline. The share of marketable debt to total internal liabilities, which was about 30 per cent in the beginning of the 1990s, increased to 40 per cent in the beginning of the 2000s and is budgeted to increase to 67.5 per cent by end-March 2013. The share of public account liabilities on the other hand is estimated to decline to 22.8 per cent in 2012-13 (BE) from about 30 per cent in 2001-2 and about 46 per cent in the beginning of the 1990s.

3.47 A greater dependence on domestic debt insulates the debt portfolio from volatility in international capital markets. It also minimizes currency risk. Apart from this, internal debt of the

Table 3.9 : Outstanding Liabilities of the Central Government

	End-March					
	2007-8	2008-9	2009-10	2010-11	2011-12 (RE)	2012-13 (BE)
	(As per cent of GDP)					
1. Internal liabilities	**54.6**	**53.9**	**52.4**	**48.5**	**47.9**	**48.3**
a) Internal debt#	36.1	35.9	35.9	34.2	35.7	37.3
i) Market borrowings	22.1	23.8	27.0	26.6	27.9	29.8
ii) Others	13.9	12.1	9.0	7.6	7.7	7.5
b) Other internal liabilities	18.6	18.1	16.5	14.3	12.2	11.0
2 External debt(outstanding)*	**2.2**	**2.2**	**2.1**	**2.0**	**1.9**	**1.8**
3 Total outstanding liabilities	**56.9**	**56.1**	**54.5**	**50.5**	**49.8**	**50.1**
Memorandum items						
a) External debt @	4.2	4.7	3.8	3.6	3.6	3.3
b) Total outstanding liabilities(adjusted)**	58.9	58.6	56.3	52.1	51.5	51.7

Sources : Union Budget documents, Controller of Aid Accounts and Audit and Reserve Bank of India.

\# Internal debt includes net borrowing of ₹ 29,062 crore for 2005-6, ₹ 62,974 crore for 2006-7, ₹ 1,70,554 crore for 2007-8, ₹ 88,773 crore for 2008-9, ₹ 2,737 crore for 2009-10, and ₹ 20,000 crore for 2011-12(BE) under the Market Stabilisation Scheme.

* External debt figures represent borrowings by central government from external sources and are based upon historical rates of exchange.

@ Converted at year end exchange rates. For 2006-7, the rates prevailing at the end of March 2007, for 2007-8, the rates prevailing at the end of March 2008, and so on.

** Internal liabilities and external debt (converted at year end exchange rates).

Note : The ratios to GDP at current market prices are based on the CSO's National Accounts 2004-5 series.

Government of India has the following favourable features which provide some comfort.

(a) Weighted average maturity of outstanding government securities at 9.8 years is high compared to international standards. At end-March 2012, the proportion of debt maturing in less than one year was only 3.5 per cent and 30.2 per cent of outstanding stock had a residual maturity of up to five years. This implies that over the next five years, on an average, about 6.0 per cent of outstanding stock needs to be rolled over every year. Thus the rollover risk in the debt portfolio remained low.

(b) Most of the public debt in India is at fixed interest rates. Of the total outstanding dated securities, only 1.8 per cent was on floating rate. Thus interest payments are largely insulated from interest rate volatility, imparting stability to the Budget.

(c) The average cost of the debt (interest payments/ debt ratio) and interest payments as a percentage of revenue receipts are on a secular decline, though some rise was seen in the past two years. Ratio of interest payments to revenue receipts has declined to around 36 per cent in 2011-12 from about 50 per cent in the beginning of the 2000s.

(d) A relatively stable weighted average yield of primary issuance indicates stability in interest payments/revenue receipts and interest payments/debt ratios, pointing towards the sustainability of the debt in the country.

3.48 Government debt could also arise from the assumption of liabilities associated with recapitalizing public-sector enterprises including the banking sector. It is, therefore, customary to look at their finances.

Performance of Departmental Enterprises of the Central Government

Railways

3.49 The Twelfth Five Year Plan (2012-17) envisions an integrated approach for the transport sector as a whole. It states that the vision for the transport sector should be guided by a modal mix that will lead to an efficient, sustainable, economical, safe, reliable, environmentally friendly, and regionally balanced transport system. The rail network would also have to develop a strategy to be part of an effective multi-

modal transport system. The Twelfth Plan identifies safety, modernization, and capacity augmentation as the focus areas, for which initiatives are underway in Indian Railways to supplement its internal resources judiciously through public-private partnerships (PPP), cost sharing with state governments and other stakeholders, and market borrowings.

3.50 Freight loading by Indian Railways during fiscal 2011-12 was placed at 969.8 million tonnes against 921.7 million tonnes in 2010-11, registering an increase of 5.2 per cent with an incremental loading of 48.1 million tonnes over 2010-11 levels. The freight traffic target for 2012-13 (BE) has been fixed at 1,025 million tonnes, an increase of 5.7 per cent over the previous year. During April-November 2012, Indian Railways has carried 647.11 million tonnes of revenue-earning freight traffic. The freight carried shows an increase of 29.06 million tonnes over the freight traffic of 618.05 million tonnes actually carried during the corresponding period of the previous year, translating into an increase of 4.7 per cent.

3.51 Freight earnings at ₹ 69,547.59 crore during 2011-12 exceeded the revised target by ₹ 927 crore, registering a growth of 10.7 per cent over 2010-11. Passenger earnings (including other coaching earnings) during 2011-12 stood at ₹ 30,962.96 crore as against ₹ 28,263 crore in 2010-11, an increase of 9.6 per cent. The overall traffic revenue for 2011-12 at ₹ 1,04,153 crore registered a growth of 10.2 per cent over 2010-11. Taking into account further accumulation of ₹ 43 crore to the traffic outstanding, the gross traffic receipts of the Railways for 2011-12 stood at ₹ 1,04,110 crore. Gross traffic receipts for 2012-13 have been budgeted at ₹ 1,32,552 crore.

3.52 Ordinary working expenses at ₹ 74,537.4 crore during 2011-12 show an increase of 9.4 per cent over 2010-11. The total working expenses including appropriations to the Depreciation Reserve Fund and Pension Fund at ₹ 98,667.41 crore recorded an increase of 10.3 per cent over 2010-11. Ordinary working expenses are budgeted at ₹ 84,400 crore for 2012-13 while the total working expenses are ₹ 1,12,400 crore.

3.53 Taking into account the net variation of the miscellaneous receipts and miscellaneous expenditure, Railways' net revenue in 2011-12 was ₹ 6,781.60 crore. After fully discharging the dividend liability of ₹ 5,656.03 crore for the fiscal, Railways during 2011-12 generated an excess of around ₹1,125.57 crore. Dividend liability during 2012-13 has been budgeted at ₹ 6,676 crore. There was a marginal deterioration of the operating ratio (percentage of total working expenses to gross traffic earnings) of the Railways, which stood at 94.9 per cent in 2011-12 as against 94.6 per cent in 2010-11. The operating ratio for 2012-13 has been targeted at 84.9 per cent in the Rail Budget. The net revenue as a proportion of capital-at-charge and investment from Capital Fund for the fiscal stood at 4.2 per cent in 2011-12. The target for 2012-13 (BE) is 12.1 per cent.

3.54 The Plan Outlay for 2011-12 (provisional) stood at ₹ 45,499 crore including internally generated resources of ₹ 8,934 crore (i.e. 19.6 per cent of the Plan outlay) and market borrowings of ₹ 15,228 crore (i.e. 33.5 per cent of the Plan outlay) by the Indian Railway Finance Corporation (IRFC), which also includes borrowings of ₹ 108 crore for Rail Vikas Nigam Limited. The Annual Plan outlay for 2012-13 has been budgeted at ₹ 60,100 crore, which is the highest ever Plan investment. The Plan has been budgeted to be financed through GBS of ₹ 24,000 crore (40.0 per cent), internal resources of ₹ 18,050 crore (30.0 per cent), ₹ 2,000 crore from the Railway Safety Fund (3.3 per cent) and extra-budgetary resources of ₹ 16,050 crore (26.7 per cent) including market borrowings of ₹ 15,000 crore through IRFC.

Department of Posts

3.55 The gross receipts in 2011-12 of the Department of Posts were placed at ₹ 7,899.35 crore. The gross and net working expenses during the year were ₹ 14,163.91 crore and ₹ 13,705.27 crore respectively, yielding a deficit of ₹ 5,805.92 crore. In the current fiscal as per BE 2012-13, gross receipts are budgeted to go up to ₹ 7,793.31 crore with gross and net working expenses estimated at ₹ 14,379.71 crore and ₹ 13,714.66 crore respectively. The deficit is projected to be ₹ 5,921.35 crore.

3.56 The government has approved the IT Modernization Project of the Department of Posts for computerization of all the non-computerized post offices, mail offices, administrative and other offices, establishment of required IT infrastructure, and development of required software applications. The continuation of the IT modernization project involving operating and maintenance (O&M) costs of ₹ 4,909.00 crore has been approved on 22 November 2012.

Broadcasting

3.57 The expenditure of Prasar Bharati in 2011-12 was ₹ 3,340.57 crore (provisional) excluding charges on account of space segment and spectrum charges and interest and depreciation costs. The total revenue earned in 2011-12 was ₹ 1,409.54 crore (subject to reconciliation).

3.58 The government has proposed several schemes for the Twelfth Five Year Plan to be implemented through All India Radio (AIR) and Doordarshan which include the scheme for Digitalization of Transmitters, Studios, and Connectivity. The scheme inter alia envisages digitalization of 98 studios and connectivity and installation of 100-watt FM Digital Compatible Transmitters at 100 locations. As such, the scheme for Digitalization of the AIR/Doordarshan Network continues to be one of the Major Thrust Areas of the Twelfth Plan. Auction of 839 additional private FM channels in 294 cities is also likely to be completed in 2013-14. An allocation of ₹ 2,047.35 crore has been made in 2012-13 (BE) to cover the resource gap in the operating cost of Prasar Bharati.In addition, as part of the financial restructuring package for Prasar Bharati, the government has recently approved various measures which include meeting 100 per cent expenses towards salary and salary-related establishment expenses during the next five years from 2012-13 to 2016-17 while all other items of operating expenses are to be borne by Prasar Bharati from its internal resources.

State-level Finances

3.59 While there has been some stress in central government finances in recent years, the finances of states are in fine fettle. The combined gross fiscal deficit of states did not exceed 3.0 per cent of GDP even in the years of global crisis. After reaching a level of 1.5 per cent of GDP in 2007-8, the fiscal deficit of states rose to 2.9 per cent in 2009-10 but has moderated to 2.1–2.3 per cent subsequently (Table 3.10). As a proportion of GDP, tax receipts moderated in 2008-9 and 2009-10 and together with stable non-tax receipts helped in fiscal consolidation

Table 3.10 : Receipts and Disbursements of State and Consolidated General Government

Item	2007-8	2008-9	2009-10	2010-11	2011-12 (RE)	2012-13 (BE)
	(As per cent of GDP)					
State governments						
I. Total receipts (a+b)	15.4	15.8	15.6	15.1	15.9	16.3
a) Revenue receipts (1+2)	12.5	12.3	11.9	12.0	12.7	13.3
1. Tax receipts	8.8	8.6	8.2	8.7	9.0	9.4
2. Non-tax receipts	3.7	3.8	3.7	3.3	3.7	3.8
b) Capital receipts	2.8	3.5	3.7	3.1	3.2	3.0
II. Total disbursements	15.1	15.7	15.7	14.9	16.0	16.3
a) Revenue	11.6	12.1	12.3	12.0	12.7	12.8
b) Capital	3.2	3.3	3.1	2.7	2.9	3.2
c) Loans and advances	0.3	0.3	0.3	0.2	0.4	0.3
III. Revenue deficit	-0.9	-0.2	0.5	0.0	-0.1	-0.4
IV. Gross fiscal deficit	1.5	2.4	2.9	2.1	2.3	2.1
General government						
I. Total receipts (a+b)	27.2	27.8	28.5	27.6	28.3	28.3
a) Revenue receipts (1+2)	21.3	19.8	18.7	20.3	19.5	20.7
1. Tax receipts	17.6	16.5	15.2	16.0	16.2	17.1
2. Non-tax receipts	3.7	3.4	3.5	4.2	3.3	3.5
b) Capital receipts	5.9	8.0	9.8	7.4	8.8	7.6
II. Total disbursements	26.4	28.4	28.6	27.5	28.1	28.3
a) Revenue	21.5	24.1	24.4	23.5	23.8	23.7
b) Capital	4.5	3.9	3.8	3.4	3.6	4.1
c) Loans and advances	0.4	0.4	0.4	0.6	0.6	0.5
III. Revenue deficit	0.2	4.3	5.7	3.2	4.3	3.1
IV. Gross fiscal deficit	4.0	8.3	9.3	6.9	8.1	7.2

Source: Reserve Bank of India.

Notes : (1) The ratios to GDP at current market prices are based on the CSO's National Accounts 2004-5 series.
(2) Disinvestment proceeds are inclusive of miscellaneous capital receipts of the states.
(3) Negative (-) sign indicates surplus in deficit indicators.
(4) Capital receipts include public accounts on a net basis.
(5) Capital disbursements are exclusive of public accounts.

notwithstanding a small rise in 2011-12 (RE). With the exception of 2009-10, the combined position of states in terms of revenue deficit has been one of surplus. Besides, what is noteworthy is that there has been an improvement in the quality of expenditure with a rise in capital expenditure to GDP ratio and development expenditure. However, as with many other economic indicators, there are large inter-state variations in the attainments in terms of fiscal outcome. Another concern arising from state finances is that there is incomplete information on extra-budget activities and quasi-fiscal activities. The RBI's study of state budgets 2012-13 has indicated that notwithstanding the information gap, fiscal transparency at state government levels has increased. One of the main problems with states' finances is in the financial health of the power distribution companies, which continue to accumulate losses estimated at ₹ 1,90,000 crore at end-March 2011. This is mainly on account of non-revision of tariffs, subsidy arrears, high aggregate and technical losses and the high cost of buying short-term power. Thus, continued reform initiatives are critical for maintaining sound finances of the states.

Consolidated General Government

3.60 As indicated earlier, fiscal deficit of the centre widened from 4.8 per cent of GDP in 2010-11 to 5.9 per cent in 2011-12 (RE). With the fiscal deficit of states exhibiting a modest deterioration to 2.3 per cent of GDP, the fiscal outcome in terms of centre and states combined was placed at 8.1 per cent in

Box 3.5 : Terms of Reference of 14th Finance Commission

The following are the broad Terms of Reference and the matters to be taken into consideration by the 14th Finance Commission in making the recommendations:

1. (i) the distribution between the union and states of the net proceeds of taxes which are to be, or may be, divided between them under Chapter I, Part XII of the Constitution and the allocation between the states of the respective shares of such proceeds;

   (ii) the principles which should govern the grants-in-aid of the revenues of the states out of the Consolidated Fund of India and the sums to be paid to the states which are in need of assistance by way of grants-in-aid of their revenues under article 275 of the Constitution for purposes other than those specified in the provisos to clause (1) of that article; and

   (iii) measures needed to augment the Consolidated Fund of a state to supplement the resources of the panchayats and municipalities in the state on the basis of the recommendations made by the Finance Commission of the state.

2. The Commission has been mandated to review the state of finances, deficit, and debt levels of the union and states and suggest measures for maintaining a stable and sustainable fiscal environment consistent with equitable growth including suggestions to amend the FRBMAs currently in force. The Commission has been asked to consider and recommend incentives and disincentives for states for observing the obligations laid down in the FRBMAs.

3. In making its recommendations, the Commission inter alia is required to consider: the resources of the central government and the demands on the resources of the central government; the resources of the state governments and demands on such resources under different heads, including the impact of debt levels on resource availability in debt-stressed states; the objective of not only balancing the receipts and expenditure on revenue account of all the states and the union but also generating surpluses for capital investment; the taxation efforts of the central government and each state government and the potential for additional resource mobilization; the level of subsidies required for sustainable and inclusive growth and equitable sharing of subsidies between the central and state governments; the expenditure on the non-salary component of maintenance and upkeep of capital assets and the non-wage-related maintenance expenditure on Plan schemes to be completed by 31 March 2015 and the norms on the basis of which specific amounts are recommended for the maintenance of capital assets and the manner of monitoring such expenditure; the need for insulating the pricing of public utility services like drinking water, irrigation, power ,and public transport from policy fluctuations through statutory provisions; the need for making public-sector enterprises competitive and market oriented; listing and disinvestment; relinquishing of non-priority enterprises; the need to balance management of ecology, environment, and climate change consistent with sustainable economic development; and the impact of the proposed goods and services tax on the finances of the centre and states and the mechanism for compensation in case of any revenue loss.

4. The Commission is required to generally take the base of population figures as of 1971 in all cases where population is a factor for determination of devolution of taxes and duties and grants-in-aid; however, the Commission may also take into account the demographic changes that have taken place subsequent to 1971.

5. The Commission is to review the present public expenditure management systems in place including budgeting and accounting standards and practices; the existing system of classification of receipts and expenditure; linking outlays to outputs and outcomes; best practices within the country and internationally and to make appropriate recommendations thereon.

6. The Commission is to review the present arrangements as regards financing of Disaster Management with reference to the funds constituted under the Disaster Management Act 2005(53 of 2005) and make appropriate recommendations thereon.

7. The Commission is to indicate the basis on which it has arrived at its findings and make available the state-wise estimates of receipts and expenditure.

2011-12 (RE) as against 6.9 per cent in 2010-11 (Table 3.10). In 2012-13 (BE), fiscal deficit is budgeted to come down to 7.2 per cent of GDP. While there is a likely slippage of 0.2 percentage point in terms of the centre's target, the over-performance in states might help in achieving the budgeted levels in the overall fiscal outcome in 2012-13.

3.61 The 14th Finance Commission was constituted on 2 January 2013 under the Chairmanship of Dr Y.V.Reddy, former RBI Governor. Other members of the commission are (i) Professor Abhijit Sen (ii) Ms Sushma Nath (iii) Dr M.Govinda Rao (iv) Dr Sudipto Mundle. The Commission's mandate is detailed in Box 3.5.

Outlook

3.62 It might be recalled that the Mid-Year Economic Analysis 2012-13 sought to allay concerns about the fiscal outcome for 2012-13 through allusion to the measures taken and indicated that the fiscal deficit for the year would be contained at 5.3 per cent of GDP. The outcome in April-December 2012 in terms of fiscal deficit broadly indicates that this is likely to happen notwithstanding the significant shortfall in revenue. The overall shortfall in non-debt receipts could be contained with ongoing greater efforts at mobilization and reforms already in place. The longer-term outlook has already been outlined in terms of the fiscal consolidation roadmap leading to a fiscal deficit of 3.0 per cent of GDP in 2016-17. As indicated earlier in the chapter, addressing the key fiscal risk of petroleum subsidies is critical in better fiscal marksmanship. With the recent reforms in diesel prices and efforts at expenditure reprioritization, the medium-term fiscal consolidation plan is credible and could yet again yield macroeconomic dividends in terms of higher growth and price stability.