

Understanding the Budget process

Indian Budget process

The budget is prepared by the Finance Minister with the assistance of number of advisors and bureaucrats. The Finance Minister seeks the view of the industry captains and economists prior to preparation. Various accounting and finance related organisations send in their opinions and suggestions. The budgeting exercise in India remains mainly the domain of bureaucrats to participate and influence the outcomes.

Normally, the budget-making process starts in the third quarter of the financial year. The budget has four stages viz., (1) estimates of expenditures and revenues, (2) first estimate of deficit, (3) narrowing of deficit and (4) presentation and approval of budget.

Stage 1: Estimates of expenditures and revenues

Part A: Estimates of Expenditure

The process begins with various ministries providing initial estimates of plan and non-plan expenditures. The ministries discuss the plan expenditures with the Planning Commission. The Planning commission allocates resources for continuing plan programmes and decides on the new programmes that can be undertaken on the basis of a tentative estimate of resources available, that is provided to it by the finance ministry. The financial advisors of the ministries prepare the non-plan expenditures. The expenditure secretary consolidates them and after intensive discussion with financial advisors, budget estimates are set for the ensuing fiscal year.

The majority of the non-plan expenditure is accounted for by interest payments, subsidies (mainly on food and fertilisers) and wage payments to employees.

Part B: Estimates of Revenue

Apart from estimating the expenditure, an assessment of expected revenues likely to flow into the government treasury has to be done as a concurrent exercise. Revenue receipts are of two types - capital and current receipts.

Capital receipts include repayment of loans given by the government, receipts from divestment of public-sector equity and borrowings - both domestic and external. Current receipts include mainly, tax revenues, receipts by way of dividends from public-sector units and interest payments on loans given out by the central government.

The amounts to be received by way of tax revenues is estimated on the basis of existing rates of taxation and taking into consideration the likely growth and inflation rate over the ensuing fiscal year.

On the capital receipts side, targeted amounts to be realised through divestment of public sector equity and amounts to be realised by way of repayments of loans is made. All the estimates are provided to the revenue secretary.

STAGE 2: First estimates of deficit

After the estimates of revenue and expenditure are made, they are matched together. This provides the first estimate of expected shortfall in revenue to meet projected expenditure. The government then, in consultation with the chief economic advisor, decides on the optimum level of borrowings to meet this deficit. The figure of external borrowings is known as much of the external borrowing by the government consists of bilateral and multilateral assistance which is known by the time budget exercises are undertaken. The level of domestic borrowing depends partly on the desired level of fiscal deficit that the government targets for itself. A part of the revenue gap is left unfilled to be met through the issue of ad hoc treasury bills.

STAGE 3: Narrowing of the deficit

After the targets for the fiscal deficits and the overall budget deficit is decided, any remaining shortfall is filled through a revision in tax rates if feasible , keeping in mind the fiscal incentive structure the government wishes to put in place to stimulate the growth in different sectors. Following the initial plans, if any changes need to be made adjustments are made to the expenditure; usually the plan expenditure has to be modified. The non plan expenditure comprises of interest payments, subsidies and administrative expenditure. Due to the political sensitivities involved in reducing subsidies, non-plan expenditure of the government is inflexible about changing it and it

is the plan expenditures which get the axe after pre-emption have already been made for non-plan expenditure.

STAGE 4: The Budget

The presentation of the Budget for the ensuing fiscal year (beginning April 1) is usually done on the last working day of February. The Indian constitution has made the Parliament supreme in financial matters. The Union government, under Article 112 of the constitution, is required to lay an annual financial statement of estimated receipts and expenditure before both Houses of Parliament. It can levy taxes or disburse funds only on approval in both houses of Parliament. However, the proposal for taxation or expenditure has to be initiated within the Council of Ministers--specifically by the Minister of Finance. The Finance Minister presents before the Parliament, a financial statement detailing the estimated receipts and expenditures of the central government for the forthcoming fiscal year and a review of the current fiscal year.

Under Article 114 of the Constitution, the government can withdraw money from the Consolidated Fund of India only on approval from Parliament and so it has to get the Appropriation Bills approved by Parliament. This authorises the executive to spend money. Article 265 of the Constitution prohibits the government from collecting any taxes without the authority of law. Therefore, the government comes up with the Finance Bill. The Bill may levy new taxes, modify the existing tax structure or continue the existing tax structure beyond the period approved by Parliament earlier. The bills are forwarded to the Rajya Sabha for comment. The Lok Sabha, however, is not obligated to accept the comments and the Rajya Sabha cannot delay passage of these bills. The bills become law when signed by the President. The Lok Sabha cannot increase the request for funds submitted by the executive, nor can it authorize new expenditures.

The proposals in the budget come into force on April 1. Between the presentation and effective date there is a gap of 1 month during which the Lok Sabha can review and modify the government's budget proposals. This does not happen most of the time and the Parliamentary scrutiny of proposals and the passage of the budget gets completed

in May, well after the commencement of the new fiscal year. Since the proposed budget has to be effective from April 1, the government usually seeks an interim approval to meet emergent expenditures that have to be incurred pending the approval of the budget.

This is called the vote-on-account and the sanctions given by the passage of the vote-on-account get automatically overridden once the Budget is approved by Parliament.

Other budgets

The Indian Railways, the largest public-sector enterprise, and the Department of Posts and Telegraph have their own budgets, funds, and accounts. The appropriations and disbursements under their budgets are subject to the same form of parliamentary and audit control as other government revenues and expenditures. Dividends accrue to the central government, and deficits are subsidized by it like other government enterprises.

State Budget

Each state government has its own budget, prepared by the state's minister of finance in consultation with appropriate officials of the central government. Primary control over state finances rests with the state legislature. However, State finances are which latter reviews the state government accounts annually and reports the findings to the state governor for submission to the state's legislature.

Because of its greater revenue sources, the central government shares its revenue received from personal income taxes and certain excise taxes with the states. It also collects other minor taxes, the total proceeds of which are transferred to the states. The division of the shared taxes is determined by financial commissions established by the president, usually at five-year intervals.

The central government also provides the states with grants to meet their commitments.

Budget documents

The Union Budget comprises various documents. The first one is the speech of the Finance Ministry, which he reads in the Lok Sabha. **The Budget speech** provides the direction in which the government wishes to move in the coming financial year, the

growth targets and the major thrust areas. The Finance Minister spells the broad tax policy measures in his speech. The speech lists the problems being faced by the country on the economic front and indicates the government's response to them. The speech also summaries the various expenditure and tax proposals

The other important documents are:

1. Key to Budget

This document provides an understanding of the budget documents

2. Budget Highlights

This statement gives the key features of the budget

3. Annual Financial Statement

Annual Financial statement is the main document. This statement shows the receipts and payments of the government under the three parts in which government accounts are kept.

- (1) Consolidated Fund- Resources raised by the government through taxes, loans, dividends from PSUs and banks form the Consolidated Fund.
- (2) Contingency Fund- It is imprest at the government's disposal to meet unforeseen expenditure.
- (3) Public Account- The amount collected by the government acting as a banker .e.g. PF, small savings collections.

4. Finance Bill

The Finance Bill includes the tax proposals and the tax rates .It provided the fine print of the budget

5. Memorandum

Explanatory Memorandum provides a quick overview of tax provisions contained in the Finance Bill.

6. Budget at a Glance

Budget at a Glance provides an overview of government finances. It's more like a balance-sheet of the Union. It gives a broad break up of tax revenues, other receipts, expenditure-plan and no-plan allocation of outlays by ministries and resource transfer

to states and Union Territories. Progress towards implementation of Budget proposals announced in previous years are listed in the Implementation Budget

7. Expenditure Budget

Expenditure Budget Volume I and II explains the provisions made. While Volume I explains the provisions ministry-wise, Volume II analyses expenditure trend over the years with regard to Plan and non-Plan expenditure.

8. Receipts Budget

Receipts Budget gives details of revenue receipts and capital receipts and explains the estimates so as to make them intelligible to an ordinary citizen. It also include trend of receipts over the years and details of external assistance

9. Customs & Central Excise

This document gives the customs and excise notifications

10. Implementation of Budget Announcements

This contains status of implementation on initiatives announced by the Finance Minister in the Budget Speech

11. The Macro Economic Framework Statement

The Macro-economic Framework Statement, as enjoined by the Fiscal Responsibility and Budget Management Act, 2003 (FRBM Act), contains an assessment of the growth prospects of the economy with specific underlying assumptions. It contains assessment regarding the GDP growth rate, fiscal balance of the Central Government and the external sector balance of the economy

12. The Medium Term Fiscal Policy Statement

The Medium-term Fiscal Policy Statement, as enjoined by the FRBM Act sets forth a three year rolling target for specific fiscal indicators along with underlying assumptions. The statement includes an assessment of sustainability relating to balance between revenue receipts and revenue expenditure and the use of capital receipts including market borrowings for generation of productive assets.

13. The Fiscal Policy Strategy Statement

The Fiscal Policy Strategy Statement, as enjoined by the FRBM Act, contains the policies of the Central Government for the ensuing financial year relating to taxation, expenditure, lending and investments, administered pricing, borrowings and guarantees. It outlines the strategic priorities of the Government in the fiscal area, how the current policies are in conformity with sound fiscal management principles and rationale for any major deviation in key fiscal measures.