M.A 1st Sem Public Administration

Course Code

MPUB104

FINANCIAL ADMINISTRATION

Unit1-20

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Unit-1

FINANCIAL ADMINISTRATION: MEANING, NATURE, SCOPE AND SIGNIFICANCE

Structure

1.0. Introduction

1.1 Learning Objectives

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1.0. INTRODUCTION

The financial administration refers to how the government manages its finances, encompassing activities such as budget preparation, managing various revenue sources, safeguarding public funds, overseeing spending procedures, and maintaining financial records. These functions are essential for the efficient operation of public finance. The relationship between finance and government is fundamental, as the available financial resources determine the limits of the government's overall activities and those of its individual departments. Effective financial management is one of the primary and unavoidable duties of the government. To ensure the smooth functioning of government operations, financial administration is of utmost importance.

1.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand about the meaning and nature of Financial Administration
- To comprehend the scope of Financial Administration
- To discuss about various principles of Financial Administration
- To know about bilateral and multi-lateral agencies.

1.2. NATURE, SCOPE & AGENCIES INVOLVED IN FINANCIAL ADMINISTRATION

A sound financial policy implemented through a sound financial system is sure to produce best results. Even the best financial policies and plans will come in naught, if the financial administration is weak or inefficient. Thus. the financial administration involving the machinery and methods by which funds for the support of public services are raised spent and accounted for, is at the core of modern government. In a democratic form of government, soundness and efficiency of financial administration become all the more important, otherwise, all governmental action and policies remain ineffective, and the government becomes target of severe criticism of the hands of enlightened citizens. This is also necessary because of the vastness of the funds that pass through governmental machinery, for ensuring their lawful and efficient use.

F. A. Nigro says, Financial administration is of great importance today because of the tremendous increase in the amounts of money expended for 'government services. Everything government does requires money and it now does so much that it is utterly essential that sound-principles and techniques of financial administration be employed.

AGENCIES INVOLVED IN FINANCIAL ADMINISTRATION

The financial administration involves the means for determining with maximum accuracy, the revenue and expenditure needs of the government, provision for meeting those needs through the enactment of revenue and appropriation laws and the establishment of an accounting and audit system that will furnish a detailed record of the manner in which these laws are administered.

The following agencies are involved in the Financial Administration:-

i. The executive

ii. The legislature

iii. The Finance Department of Ministry

iv. The Audit Department.

Government budget is an essential element in the sound financial administration of nation; it is on the budget that the whole financial administration rests.

THE EXECUTIVE

The financial operation of this agency comprise of planning, determining, executing and controlling The executive formulates its plans for the financial year and on the basis of that plan determines the financial needs. This is done through the med Annual Financial Statement comm. The Financial initiative. For with the exclusive has can be imposed or asked for by the parliament cannot act in these terms of its own. The government alone has the right to draw up and present a budget. This' major constitutional principle is one of the four fundamental principle of financial procedure provided by Sir Gilbert Cambion.

The pilot incharge of steering a vessel, is the only competent judge of the position and of the speed he needs to give his Sails, because he alone is posted in such a way as to know the force of direction of the winds and currents which may hinder or delay his movements. Similarly, government is the only capable authority with which financial initiative should vest and propose its financial plan in the form of budget.

The Legislature:

Under parliamentary democracy system, the legislature as a representative-body of the people has to safeguard the rights and interests of tax payer in field of financial administration. In order to assure this the constitution provides for:

a) Parliamentary Control Over Taxation :

According to the Article 265 of the Indian Constitution, "No tax shall be levied or collected except by authority of law." The government has to present all tax proposals before parliament in the form of a Bill to by passed into law, and unless that Act is passed, no tax can be levied.

b) Parliamentary Control Over Expenditure :

According to Article 266 of the Indian Constitution. "No expenditure can be incurred except with the sanction of the legislature." This principle lays down that all revenues, all loarts by the Union or State shall be paid into the consolidated fund of the Union or the State and that no money can be withdrawn out of the fund except in accordance with law and for purpose and in the manner provided for in the constitution.

c) Parliamentary Authorization of Public Loans :

In India, according to the Article 292 of the constitution, the government of India has the exclusive power to borrow from the security of the consolidated fund of India, subject only to such limitation as Parliament may be law impose.

a) Parliament' Enforcement of Financial Accountability

The Government is, bound to spend the money granted by Parliament for no purpose other than those for which they were granted. This control is exercised through the Comptroller and Auditor General of India, whose reports are scrutinized by the public accounts committee of Parliament and laid before the House. Thus it safeguards the finance of the nation.

SCOPE OF FINANCIAL ADMINISTRATION

Financial administration is a crucial aspect of public administration, focusing on the management of state finances. It involves the principles and practices that ensure the proper and efficient handling of public funds. On a practical level, financial administration deals with the collection, preservation, and distribution of public funds, the coordination of revenues and expenditures, the management of state credit operations, and the overall control of the public finances. While theoretical aspects of financial administration address its principles, the practical side emphasizes real-world implementation.

Recently, the importance of financial administration has grown due to various factors. One significant factor is the rise of the welfare state, leading to an increase in public expenditure and corresponding revenue needs. This has resulted in a more complex system of managing state finances. As such, the effective administration of finances must be handled by experts who can navigate the complexities involved.

In democratic systems like India, where elected representatives govern, financial administration must align with the needs of democratic institutions. To serve these needs, the procedures for managing finances should be simple, organized, and understandable to the general public, at least in broad terms. The challenge lies in setting up a system that is both efficient and transparent, while ensuring public oversight through democratic institutions. Coordinating these efforts to make the system effective and optimize state revenue is one of the toughest challenges of public administration.

Moreover, advances in management techniques have influenced financial administration, aiming for simplicity and rationality. As PJ.J. Pinto points out, "Science creates order and simplicity, and similarly, in finance, there has been a drive for more streamlined and efficient procedures." While achieving mechanical precision in social science is impossible, the goal is to develop an administration that is simpler, more understandable, and more efficient. The more citizens comprehend how the state machinery functions, the greater their interest in governance will be, fostering stronger democratic institutions.

Self-Check Exercise-1

Q.1 The Government is, bound to spend the money granted by Parliament for no purpose other than those for which they were granted. True/False

Q.2 Which Article of Indian constitution reads that "No tax shall be levied or collected except by authority of law."?

1.3 SIGNIFICANCE OF FINANCIAL ADMINISTRATION, POLITICAL PARTIES &CITIZENS

The significance of financial administration became more apparent only after the Industrial Revolution. Prior to that, the idea of minimal government, influenced by the laissez-faire doctrine, emphasized low taxation. However, as society became more complex due to industrialization, the role of government expanded considerably. Additionally, the rise of the welfare state led to a dramatic increase in state involvement in various sectors previously beyond its scope. In this new context, financial administration became crucial in finding ways to generate resources to address growing public expenditures.

The Great Depression (1929-1933) exposed the limitations of governments adopting a neutral economic stance. This crisis spurred a search for stability in income and employment, as well as for greater social equity. Drawing from Keynesian economics, the state took on a more active role in promoting national income and employment while also ensuring fairness and improving the socio-economic conditions of citizens. Public spending, including defense and administrative costs, shifted from being viewed as nonproductive to a tool for stimulating economic activity and job creation. As a result, financial administration was tasked with devising policies to meet these new state objectives, turning financial resources into public benefits and promoting distributive justice.

With the rise of democracy, the principle of "parliamentary control over public funds" gained global recognition. The idea that there should be "no taxation without representation" and "no public expenditure without parliamentary approval" became fundamental principles of modern political systems. This led to the need for clear, straightforward financial procedures to make the system understandable to the general public. Financial administration thus became essential in ensuring that "popular sovereignty" was a reality in modern governments.

The concept of planned development further empowered public administrators to play an active role in designing and executing development projects. The efficiency, time, and cost of implementing these projects became increasingly important. Consequently, financial administration shifted its focus from merely controlling fund disbursements to managing the execution of development programs. Innovations such as performance budgeting represent significant advancements in financial administration’s ability to address these challenges.

Since the 1980s, modern governments have faced a critical issue with limited resources. Although there is constant pressure to increase government spending to meet the growing demands of the population, taxpayers are often unwilling or unable to bear the additional tax burden. This has led to the need for careful prioritization of public expenditure. As a result, financial administration and management have become essential areas of study, with efforts like zero-based budgeting aimed at eliminating wasteful spending and maximizing efficiency in a resource-constrained environment.

In conclusion, financial administration has become a central and influential part of modern governance.

FISCAL POLICY AND PLANNING

Legislature and its Committees

'The final authority pertaining to financial matters is that of legislature. Legislature controls finances both directly and through its committees. In the representative democracy, elected representatives are the custodians of the interests of the people. The quality of financial legislation and responsiveness of financial administration depends upon the capability, capacity and interest of the elected representatives. Lord Beveridge has said that, "Democracy need not fear bureaucracy if it knows its business." Ministers and civil servants cannot go astray, if the elected representatives are sincere to the people who have elected them.

A personal discussion with some of the elected representatives revealed that they lack interest in analyzing the financial documents presented to the legislature. They do not even find time to go through the reports of their own financial Committees. Under such conditions, ministers and civil servants design the financial system in their own way.

There is a great need to improve upon this system, which is causing great damage to the efficiency and integrity of the financial administration. It is suggested that there is a need to train the elected representatives in the art and science, of parliamentary affairs and the financial implications of modern Government so that they can really watch the interest of the people for whom they have been elected.

POLITICAL PARTIES

Democratic governments function through political parties, the party, which runs the government is called, the ruling party while, the other party/parties are called the opposition parties. Since the decisions of the government are dependent upon the informal decisions already taken by the ruling party, it becomes essential that the political parties work on sound lines to promote national development. This does not mean that the opposition parties view the national problems subjectively and in the political context only. They should examine the financial documents issued by the government from time to time and formulate issues based on facts for drawing the attention of the government. They are there to point out the weaknesses of the financial system in order to put the Government on the right path. A new emerging trend, which is dangerous, is the blind supporting and safeguarding of the members of one's party or its allies, irrespective of its ramifications. This dilutes the representative character of our democracy. Sham Lal in his article, "The National Scene" has said that this is clear from its cynical reaction whenever events conspire to expose a scandal involving one of the leading lights of the party. Instead of purging the leadership of such elements and doing whatever it can in the interest of the integrity in public life, it tries to hush up the scandal and questions the motives of those who make the exposure. Can't it see that what is relevant in an exposure of a case centering on gross abuse of official power of patronage, is the reliability of the evidence which discredits the government, it makes it all the more imperative for the party in power to stay above board.

Besides, political parties interfere in the affairs of Government to get financial favors like loans, subsidies, grants, etc. for their supporters. Those members of the bureaucracy who do not obey them are threatened with consequences like transfers etc. The Tribune editorial said that the interference of political parties in the affairs of administration to get illegal and improper things done has caused a great deal of stress and strain in the administration? In this context, we-would suggest the following:

a) Political parties need to set-up their research ceils to analyze the finances of the country and through this exercise contribute to the development of the financial system of the country.

b) Since financial administration is highly complicated and complex, we should impart training to legislators of all political parties to understand the basics of financial administration, so that they can contribute to the process of improving the financial system and administration.

c) Ways and means may be devised to avoid interference in the functioning of the financial system by political parties.

Citizens

Interest groups and pressure groups: In the sphere of financial administration, government is influenced by vested interests, interest groups and pressure groups. Daily observations and comments in newspapers indicate that the citizens are harassed by the financial system, such as the delay in getting loans, grants and subsidies, on account of rampant corruption. Citizens are penalized financially through fines etc, and are asked to pay penalties, otherwise there is the threat that services will not be provided. It does not apply vice-versa.

Audit reports are also full of instances where personnel in financial system have not cared for the people. Most of the development programs failed as finances were not provided adequately and a major part was spent on wrong priorities. Recently, CAG has made very critical observation on the foreign trip of Gujarat CM, funded by the public exchequer, for his private purpose. When a citizen is proved guilty of an offence, he is punished, as he should be. But when a government department or a public functionary is proved guilty, mere judicial structures cannot be considered adequate. Those managing the administration in our country are thoroughly insensitive to criticism, including judiciary. Therefore, the only way to make the administration realize that it is as much accountable for its actions, or inaction, as any individual, is to put the whole department in the dock when facts establish its guilt. For example, if a power consumer fails to pay his bill, he is prosecuted, but when the electricity department overcharges the consumer, it gets off at best with judicial, strictures. To the popular mind, this situation indicates that government employees enjoy immunity not available to the ordinary citizen. That impression is hardly conducive to the maintenance of the judiciary's image of impartiality. Therefore, it is upto the judiciary, rather than to the executive, to discipline the administration and to bring home to those manning it that they are as liable to be punished for their inefficiency resulting in suffering to the common people as the average citizen is for violation of the laws of tire land. That is the additional role that the judiciary needs to assume today. Let a few government employees at all levels be administered the bitter medicine that they are used to administering to other citizens mostly without justification."

B.B. Tandon in his article, 'Quality in Government', rightly stresses, "It is indeed sad that Indian bureaucracy is considered to be lethargic, rule-bound, un-responsive and corrupt. In an era of liberalization and economic reforms when, on the one hand, we are talking about second generation reforms, the bureaucracy, I am sorry to say, is still in the first gear. It would be well nigh impossible to make any great progress in any direction unless the mindset of the bureaucracy is changed. The bureaucracy has to change its role of being a regulator and the authoritarian governor of archaic rules and regulations to that of a facilitator and a service provider, and that too quality service which should include service provided with a smile and at reasonable user charges".

The critical role of the State in the delivery of public goods and services can be realized only through an efficient, effective and responsive administration, delivering quality public service. Measures for administrative reforms have, therefore, acquired urgency as the framework, for an effective administration capable of quality service needs to be sensitively achieved. High quality and effective public services are a vital part of a modern state as people are entitled to expect that services which are often central to their lives, should be responsive, sensitive to their needs, easy to use, flexible and efficient.

A constitution is not a parchment of paper, it is a way of life and has to be lived upto. Eternal vigilance is the price of liberty and in the final analysis its only keepers are the people. The Imbecility of men, history teaches us, always invites the imprudence to power? Jacques, The Governor of Bank of France, has rightly said that reforms in the financial system can be effective if the people understand them and they must be in a position to grasp what is at stake. For that, Government should strive to communicate and create a political and social climate conducive to a sense of involvement and commitment to the reforms.

BILATERAL AND MULTI-LATERAL AGENCIES

Financial aid 'can be provided either through bilateral or multilateral sources. Multilateral aid has several advantages over bilateral aid. The aid through the former is normally with no strings attached. It is more acceptable politically to the recipients and, to a large extent, it takes national politics out of the sphere of foreign assistance that often complicates bilateral operations. In other words, these channels are governed more by technical than by political considerations.

Today, the World Bank and developed countries put great pressure on the Government to change the financial system before aid may be given. Therefore, the Government must analyze this pressure and take necessary decisions in the interest of the country and not due to the outside pressure. Jacuqes de Larosiere, Governor of the Banque De France, in his lecture on "World-wide Adjustment process in the 1980's" on March 24, 1992 rightly cautioned, "Beyond applying the disciplines of adjustment to the industrialized countries themselves, more needs to be done in respect of development aid. Clearly, external aid can never replace domestic progress. But aid has an important role to play in efforts to redirect savings geographically, in financing certain proj ects and helping to cope with temporary, payment imbalances, in particular, the cost arising as countries are opening up their economies." "This approach to governance has come under critical scrutiny in recent years. The expected economic benefits have not always been realized in practice. Retrenchment in government employment has not necessarily generated efficiency gains or changed the way that public officials interact with the general public.

Financial accountability mechanisms have been difficult to implement and sustain. Despite ostensible commitment to reform, manifest in official policy pronouncements, public disenchantment with government continues to grow. The tangible benefits of reform have not always been evident to ordinary citizens, especially those from the poor and marginalized sections of society. In many countries, government is still perceived as remote and public officials are considered to be self interested and motivated by job security and monetary gain rather than by a public service ethos and high standards of integrity.

CONTROL

Constitutional Law

There are many Articles in the Constitution, which deal with financial system, financial powers, and financial procedures to keep the financial, system under control. Besides, the Constitution prescribes the procedures to regulate financial relations between the Union and States.

Political Head/Minister

Since the minister occupies the top position in the politico administrative hierarchy, it is essential that he should have full legal and constitutional authority to administer the financial affairs of his department. Theoretically it is feasible but in practice, he cannot achieve much whether it is policymaking or implementation or evaluation, unless he gets due co-operation, help, participation and involvement of the personnel of his department.

Ministry-may engage the services of financial experts to control financial operations and devote time to understand the financial management to ensure optimum performance.

Research

Public Administration and Financial Management Institutions can take up research and consultancy to help the government in improving financial system. Many committees and Commissions are appointed to advise the government on financial issues. The financial administration is influenced to a great extent by such advice, but full advantage does not accrue to the system because of general resistance to change and interference by vested interests.

Self-Check Exercise-2

Q.1 Democratic governments function through political parties. True/False

Q.2 Who said that, "Democracy need not fear bureaucracy if it knows its business."

1.4. SUMMARY

According to Newman, "The Political party is the articulate organization of society's active political agents, those who are concerned with the control 'of government power and compete for popular support with another group or groups holding divergent views" financed by transfers from the Center During 1990-2000. This situation is not characteristics of the non-special category states. Besides, despite the all State GFD-DFP ratio being placed at 4.9 percent in 1999-2000, there exist wide variations in State-wise CFD-NSDP ratios, which may be addressed through state specific measures.

The Stability and efficiency of Public financial system in each state would depend largely upon the efforts and understanding of the factors, which affect directly or indirectly the functioning of financial system. The help from outside can act only as a catalyst. Time has come when Politico-Administrative leadership have to plan, implement and monitor development schemes keeping the financial aspect in view.

1.5. GLOSSARY

- **Control :** a way of keeping something within certain limits.
- **Expenditure:** the act of spending money, the amount of money that is spent.
- **Treasury :** the funds or revenue of state, institution or society.

1.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 Article 265

Self-Check Exercise-2

Q.1 True

Q.2 Lord Beveridge

1.7. REFERENCES/SUGGESTED READINGS

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1.8. TERMINAL QUESTIONS

a) What do you mean by pressure group?

b) What are the role of bilateral and multi-lateral agencies in Financial

UNIT-2

PRINCIPLES OF FINANCIAL ADMINISTRATION

Structure

2.0. Introduction

2.1 Learning Objectives

2.2 Principles of Financial Administration

Self-Check Exercise-1

2.3. Summary

2.4. Glossary

2.5. Answers to Self-Check Exercises

2.6. References/Suggested Readings

2.7. Terminal questions

2.0. INTRODUCTION

The financial administration refers to the financial management of the government, including the preparation of the budget, method of administering the various revenue sources, the custody of public funds procedures in expending money, keeping of the financial record and the like. These functions are important to the effective conduct of the operation of public finance. Finance and government are inseparable. Available financial resources set a maximum limit on administrative activity of the government as a whole and each of its separate parts. The management of the finance is one of the first and inescapable responsibilities which the government has to shoulder. For an effective discharge of these responsibilities and proper governmental functions, efficient government, none is of greater importance than that of financial administration.

2.1 Learning Objectives: After learning the lesson the students will be able to

- Comprehend the principles of financial administration
- understand their utility and relevence

2.2 Principles of Financial Administration

The significance of financial administration emerged in the early 20th century. Thinkers such as Adams considered financial administration a component of finance. Contemporary authors share a similar perspective, viewing it as a fiscal science. Since "fisc" is related to the state's financial matters, financial administration reflects the nature, character, and scope of the government. Additionally, it deals with real-world challenges, and its methods and objectives depend on the type of economy. Due to this variation, it is difficult to fully categorize financial administration as a pure science. As a result, some economists, such as Hicks, regarded public finance as an art. Consequently, identifying core principles of financial administration becomes challenging. However, by studying the evolution of financial administration across different nations and cultures, it is possible to derive some practical guidelines. The following are some key principles:

The Principle of Primacy of Public Interest, Public Choice, and Public Policy
According to Professor Adams in *The Science of Finance*, fiscal policy should prioritize the state's welfare and avoid harming its resources. While the concept of state patrimony has evolved, today, public interest takes center stage in guiding state activities. Public interest can be understood as the collective well-being, encompassing social values, rights, and privileges. Financial policies should aim to enhance public satisfaction as expressed through public policies, ensuring they contribute to the common good.

The Principle of Political Direction and Control
Every society operates within a politico-legal framework, shaped by laws, traditions, and political ideals. Financial administration must align with these political ideals as expressed through the constitution. In modern times, democratic ideals have replaced older systems, and financial administration must ensure compliance with legislative will, as shown through the Appropriation Act, Finance Act, and other policies. To maintain control, legislatures also monitor financial functions through independent audits.

The Principle of Correspondence
This principle emphasizes the need for a logical relationship between the goals of financial administration and the resources—both human and material—necessary to achieve those goals. The types of functions, the staff required to handle them, and the facilities needed must be well-coordinated. The primary focus should be on ensuring that objectives and functions guide the staffing and equipping of financial organizations.

The Principle of Unity of Organization and Management
Indian financial administration expert P.J.J. Pinto highlighted the importance of this principle, which links centralization to efficiency. However, it doesn't imply centralizing every aspect of decision-making. It suggests that while the work of various financial agencies is coordinated at the top, decision-making should be decentralized. The focus should be on centralized guidance that allows decentralized decision-making, ultimately improving productivity and utility, as seen in national planning efforts.

The Principle of Stability and Balance
Financial administration requires specialized expertise and cannot be effectively managed by unskilled personnel. Therefore, this principle stresses the need for financial organizations to develop systems that maintain efficiency, even when skilled personnel are lost. Effective manpower planning and human resource development programs are essential to ensure continuity and stability.

The Principle of Simplicity and Flexibility

In democratic systems, the electorate holds ultimate authority, and all democratic institutions derive their power from the people. Thus, the financial system and its procedures should be simple enough for the average citizen to understand. If properly implemented, this principle can reduce costs and improve efficiency. The principle of flexibility emphasizes the need for financial organizations to adapt to changes in workload, staff, and available resources.

The Principle of Conduct, Discipline, and Regularity

Public financial organizations should uphold high ethical standards, with officials acting as role models for ethical behavior. Discipline refers to adherence to objectives, rules, and regulations, ensuring the proper functioning of the organization. Regularity highlights the continuous nature of administrative tasks, emphasizing that financial organizations cannot operate intermittently. Firm self-discipline is crucial for achieving effective outcomes.

The Principle of Public Trust and Accountability

Financial administration involves the collection and disbursement of public funds, which are held in trust by the government. This responsibility requires transparency and accountability at various levels, including political, legal, and administrative. Accountability ensures that officials are answerable for how funds are used, maintaining trust with the public.

Self-Check Exercise-1

Q.1 The Principle of Correspondence signifies that there should be a causal relationship between the objectives of financial administration and the functions, the human and material resources necessary to accomplish such objectives.True/False

Q.2 The Science of Finance treats of the wants of the State and the means of their supply and hence the fiscal policy should not impair the patrimony of the State. True/False

2.3 Conclusion: So, to conclude we can say that there is great significance of financial administration in every systems. Without efficient financial administration no country can-achieve developmental goal; In this paper we will concentrate on important issues involved in financial administration in our parliamentary system of Govt. viz. study of certain Institution i.e. Planning Commission. Finance Commission, control of public moneys and very important concept of performance budgeting and its application.

We have divided various aspects into four major areas and each area has been further divided into four important factors. Let us now discuss this complex consisting of 16 variables (Refer Chart 1.1).

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T

A-4: BILATERALAND MULTILATERALAGENCIES

A-3: CITIZENS-INTEREST&PRESSURE GROUPS

A-2: POLITICALPARTIES

A-l: LEGISLATURE AND ITS COMMITTEES

A

FISCAL POLICY

ANDPLANNING

ASPECTS

OF

FINANCIAL

ADMINISTRATION

B

EXECUTION

B-1: MINISTRYOF FINANCE

B-2 : INTEGRATED FINANCIALADVISORS

B-3 : CONTROIIJNGOFFICERS/DD.Os.

B-4: TREASURES

2.4. GLOSSARY

- **Control :** a way of keeping something within certain limits.
- **Expenditure:** the act of spending money, the amount of money that is spent.
- **Treasury :** the funds or revenue of state, institution or society.

2.5. ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

2.6. REFERENCES/SUGGESTED READINGS

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2.7. TERMINAL QUESTIONS

a) What do you mean by The principle' of simplicity and flexibility?

b) Discuss the various principles of financial administration.

CENTRE-STATE FINANCIAL RELATIONS

Structure

3.0 Introduction
3.1. Learning Objectives
3.2. Constitutional Provisions
3.2.1. Taxes and Duties
3.2.2. Grant- in- Aid
3.2.3. Loans to state Government
3.2.4. Power to Borrow
Self-Check Exercise-1
3.3. Finance Commission & Sarkaria Commission on Centre- State Relations
Self-Check Exercise-2
3.6. Summary
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3.8 Answers to Self-Check Exercises
3.8. References/Suggested Readings
3.9. Terminal questions

3.0 INTRODUCTION

The nature of financial relations between the centre and the states depends upon, (1) Financial position of the states, (i) whether states are the creators of the federation or are the creation themselves for the sake of administrative Convenience. Where states are financially strong or the creators of federation, they will have an upper hand in Financial matters, otherwise, the centre will dominate.

The basic point of financial relations is the division of tax sources between the Centre and the States, in India, the constitution-makers have successfully attempted a logical allocation of powers and functions between the union and the States. The Union List contains the powers and functions of the union. The State Lists enumerates the taxes and levies, which can be imposed by the States. List III which is the concurrent list, does not include any source of taxation; thus there is no overlapping of tax- jurisdiction. Inspite of compartmentalization of taxing powers, there exists imbalance between financial resources and functions assigned to different levels of government. In order to remove the imbalance, the Constitutions provides for the distribution of some union taxes between the centre and the States and also for grants in-aid to the states.

3.1 LEARNING OBJECTIVES

After studying the lesson, the learner will be able:

- To understand Centre State Financial Relations.
- To know about Constitutional provisions on Centre- State Financial Relations.
- To discuss important recommendations of Sarkaria Commission on Centre- State Relations.

3.2 CONSTITUTIONAL PROVISIONS

The task of the imposition and collection of taxes to meet the development as well a non-developmental needs has been kept under the jurisdiction of the Union 'as well as the States. Taxes levied by the States are appropriated by them. This has been done in order to avoid any duplication or overlapping of taxes. In the case of taxes imposed by the Union and their distribution, there is a scheme of interdependence between the Union and the State Governments in the Constitution.

The Indian constitution assigns more flexible, elastic and major sources of revenue, like taxes on income, corporation tax, customs duties, to the Union Government in order to perform the innumerable functions, like the defence of the country and the adequate running of the economy. Since all these major taxes are collected from its constituent State, the constitution makes it obligatory for the union to share them with the states. The constitution divides such cases into four categories.

1) Taxes and Duties
2) Grants-in-Aid
3) Loans to State Governments
4) Power to Borrow

3.2.1 Taxes and Duties in India

a) **Duties Levied by the Union but Collected by States**
Under Article 268 of the Indian Constitution, certain duties, such as stamp duties and duties of excise on medical and toilet preparations specified in the Union List, are levied by the Central Government but collected by the States in which these duties are applicable.

b) **Taxes Levied and Collected by the Union but Assigned to the States**
According to Article 269, certain taxes are levied and collected by the Union

Government, but the net proceeds are distributed among the states based on a formula prescribed by Parliament. These include:

1. Succession and estate duties on non-agricultural property
2. Terminal taxes
3. Taxes on railway fares and freights
4. Taxes on the sale or purchase of newspapers and advertisements published within them.

c) **Taxes Levied and Collected by the Union but Shared between the Union and the States**
Article 270 specifies that taxes on income, other than agricultural income, and corporate tax are levied and collected by the Union Government, but the proceeds are shared between the Union and the States.

d) **Union Duties of Excise Shared Between the Union and the States**
Under Article 272, Union duties of excise, excluding those on medicinal and toilet preparations, are levied and collected by the Union Government. However, Parliament may decide by law that all or part of the proceeds from these duties be distributed to the States, based on principles laid out in that law.

e) **Taxes for the Purpose of the Union**
Article 271 provides that if Parliament imposes a surcharge on any of the duties or taxes outlined in Article 270, the entire proceeds from that surcharge will be part of the Consolidated Fund of India.

Grants-in-Aid

In addition to the share of proceeds from certain taxes collected by the Union and assigned to the States, the States are also entitled to grants-in-aid from the Union, as outlined in Article 275(1) of the Constitution. The Constitution provides for three types of grants to the States from Union resources:

1. **Grants-in-Lieu of Export Duty on Jute and Jute Products**
   Article 273 provides grants to jute-growing states like West Bengal, Bihar, Odisha, and Assam, in lieu of the export duty on jute. The extent of these grants is prescribed by the President of India.
2. **Grants from the Union to Certain States**
   Article 275 authorizes Parliament to provide financial assistance to States in need. Special grants are available for states that undertake schemes aimed at promoting the welfare of Scheduled Tribes (STs) and improving the administration of Scheduled Areas.
3. **Expenditure Defrayable by the Union or a State from Its Revenue**
   Article 282 allows the Union or any State to provide grants for any public

purpose, even if the purpose does not fall within their legislative competence, as long as it serves the public interest.

This structure of taxes, duties, and grants ensures a system of fiscal federalism where resources are shared, and states receive the necessary support for their financial needs, especially for socio-economic development and welfare programs.

3.2.3 Loans to State Governments

In addition to all these sources of revenue, the states are given financial assistance in the form of payable loans to meet their needs to develop and implement their continuing plan development programmes.

3.2.4 Power to Borrow

According to Art. 292, the Government of India can borrow money on the security of consolidated Fund of India. The States also deposit with the Union Government certain states and local funds, which are in fact loans to the Centre and used for general purpose. The borrowing power of a state is however subject of a number of constitutional limitations, e.g. (1) it cannot borrow outside India. (2) Limitation may be imposed by the State Legislature (3) If the Union has guaranteed and outstanding loan to the state, no fresh loan can- be raised by the state without the consent of the Union Government etc. (Art. 293).

f) of the Part-1 (Taxes and duties)

g) Taxes for the purpose of States

Article 276 and 277 are saving supervision Article 276 empowers the state to impose taxes on-professions, traders, calling and employment for the benefit of a state of a municipality, distinct, board. Local boards or other local authorities But the provision of Article 277 does not-extend to taxes levied under a law passed after the Constitution come into force.

Self-Check Exercise-1

Q.1 According to Art. 292, the Government of India can borrow money on the security of consolidated Fund of India. True/False

Q.2 According to Art. 282, the Union or State may make any grants for any, public purpose even if it is not within their respective legislative competence. True/False

Q.3

3.3 FINANCE COMMISSION

Broadly speaking the general 'Rule of federal constitution is that the proceeds of a tax is to be appropriated by the authority which imposes it. Thus if the Union authorities imposes a tax in respect of a source assigned to its competency they retain the proceeds accruing from such a tax similarly, the proceeds of a tax imposed by the constituent units would be appropriated by them. Not with standing all this "a chronic gap between the own, resources and expenditure potential of the states seems to" be an inherent feature of all well established federations. Since, in the fast changing circumstances the extent of the gap varies from time to time. He/devices or at any rate, the maj ority of them, have to be necessity flexible. It is worthwhile having definite provisions and providing a mechanism for their periodical review rather than trust to their being changed when they are proved grossly inadequate, and out of date. (T.D-Lakadala). The framers of India Constitution having taken into account the imperative need for flexibility in balancing devices and mindful of the inconvenience to which other federations were put due to the rigidity of the provisions in their respective constitutions, provided for a periodical revision of the arrangements by incorporation in the constitution itself. More over the general weakness of the federal state financial relations, more particularly in the field of devolution is that federal assistance tends to be discretionary in character not necessity on the principles of uniform application. The constitution provides, therefore that the assessment of the needs of the states as well as the measure of assistance to be afforded and the form in which it should be given are determined by the independent commission to be constituted at intervals of not more than five years." (Report of Finance Commission, 1961).

The Finance Commission refers to the body established under Article 280 of the Indian Constitution, which functions as follows:

i. The President is required to constitute a Finance Commission within two years of the commencement of the Constitution, and subsequently, every five years or at an earlier time if the President deems it necessary. The Commission consists of a Chairman and four other members, all appointed by the President.

ii. The Parliament may, through legislation, define the qualifications required for the appointment of members to the Commission and specify the method of their selection.

iii. The Finance Commission is tasked with providing recommendations to the President on the following matters:

a. The distribution of the net proceeds of taxes between the Union and the States, as specified in this Chapter, and the allocation of the respective shares among the States.

b. The principles that should guide the grant-in-aid of State revenues from the Consolidated Fund of India.

c. Any other issues referred to the Commission by the President that concern sound financial management.

iv. The Commission has the authority to determine its own procedure and exercise such powers as may be conferred upon it by Parliament in the course of fulfilling its functions.

SARKARIA COMMISSION ON CENTRE-STATE RELATIONS:

The long awaited report of the Sarkaria Commission on Central State relations, published at the end of January, 1988 made wide ranging recommendation, broadly endorsed the existing set up while indicating the lines on which it could be made more in tune with the provisions of the constitution. The main conclusions of the commission are:

a) No change is needed in the constitution to meet the growing demands of the states;
b) A strong centre is necessary to ensure national unity.
c) Concentration of power is undemocratic and there should be decentralization to enable the states to develop their resources;
d) There would be generous use of Art. 258.
e) There is a strong case for an inter-state commission (under Art. 263);
f) A rapport is necessary between the centre and the states on the question of appointment and transfer of judges, choice of governors, sharing of revenues and role of police and Paramilitary forces.

Self-Check Exercise-2

Q.1 In which Article of the constitution, there is a provision of Inter-State commission?

Q.2 The Sarkaria commission of Centre-State relations gave its report in 1988?

3.4 SUMMARY

Article 268 to 293 in Part XII of the Constitution of India deal with Centre- State Financial Relations. Beside these, there are other provisions dealing with the same subject. Constitutional provides for grant-in-Aid to the States from the Centre resources. There are two types of grant- in- aid i.e. statutory grants and discretionary grants. The statutory grants under Art. 275 (both general and specific) are given to the states on the recommendations of the Financial Commission. Art. 282 empower both the Centre and the State to make any grants for any public purpose, even if it is not within their respective legislative competence under this provision, the Centre makes grants to the state on the recommendations of NITI Ayog - an extra Constitutional body.

3.5 GLOSSARY:

- **Grant-in-aid:** an amount of money given to local government, an institution or a particular scholar.
- **Borrowing power :** the amount of money that a person, company or government can borrow at a particular time.

3.6 Answers to Self-Chech Exercises

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 Article 263

Q.2 True

3.7 REFERENCES/SUGGESTED READINGS:

- Laxmikant, M. 'Public Administration' Fifth Edition, Tata McGraw-Hill Publishing Company Limited, New Delhi, 2016
- Gupta., B.N. Indian Federal Financial and Budgeting Policy, Chaitanya Publishing House, Allahabad, 1970.
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- IGNOU notes, egyankosh

3.8 TERMINAL QUESTIONS

a) What are the role of Finance Commission with regard to Centre- State Financial relations?

b) What do you mean by statutory grants?

Chapter-4

MINISTRY OF FINANCE

Structure

4.0. Learning Objective

4.1. Introduction

4.2. History and Organisation of Finance Ministry & its Departments

Self-Check Exercise-1

4.3. Functions of the attached officer under the Central Board of Direct taxes

Self-Check Exercise-2

4.4. Summary

4.5. Glossary

4.6. Answers to Self- check exercise

4.7. References/Suggested Readings

4.8. Terminal questions

4.0. INTRODUCTION

The Ministry of Finance is responsible for managing the central government's finances and overseeing financial matters that impact the entire country. It is tasked with raising resources for development and other national needs, as well as regulating taxation and borrowing policies. The Ministry also addresses issues related to banking and currency, and in collaboration with relevant ministries, ensures the effective use of foreign resources. Additionally, it oversees the full expenditure of the Government of India in cooperation with administrative ministries.

The Ministry of Finance plays a crucial role in (1) mobilizing resources to fund government spending and (2) controlling government spending during both the budget formulation and execution phases. It also actively participates in creating financial, fiscal, and economic policies. Among its key responsibilities are consolidating the government's annual budget, issuing government loans, managing public debt, overseeing central banking policy, controlling foreign exchange, producing coins and currency, and enhancing administrative efficiency across government operations.

4.1. LEARNING OBJECTIVES

After reading this lesson, the learner will be able:

- To understand about power and functions of Ministry of Finance
- To know about various departments and its role of Ministry of Finance

- To evaluate the power and functions of Finance commission.

4.2. HISTORY OF FINANCE MINISTRY:

The Ministry of Finance traces its origins back to 1810 when a separate Finance Department was established, initially part of the Public Department. For a period, the department was managed by the Secretary of the Public Department. In 1816, the Finance Department was placed under the Territorial Department, which was later abolished in 1830. Following this, the Finance Department came under the control of the Secretary of the General Department.

In 1843, a separate Secretariat for the Government of India was created, organized into four departments, one of which was the Finance Department. In 1879, the department was renamed the Department of Finance and Commerce, but it reverted to the Department of Finance in 1905.

The Government of India Act, 1919, introduced significant changes in the country's political framework. As a result, the Finance Department was reorganized into seven branches: (1) General Finance, (2) Revenue, (3) Currency and Banking, (4) Salary and Allowances, (5) Civil Accounts, (6) Army Finance, and (7) Military Accounts.

The Government of India Act, 1935, did not bring major changes to the Department of Finance, though a Financial Advisor was appointed to assist the Governor-General in his financial responsibilities. After World War II, the department was further reorganized into nine divisions.

Post-independence, the Finance Department became known as the Ministry of Finance and was divided into three main wings: Expenditure, Economic Affairs, and Revenue. In 1949, the Ministry was further structured into two departments: the Department of Revenue and Expenditure and the Department of Economic Affairs. In the 1950s, two more departments were added to the Ministry: the Department of Expenditure and the Department of Company Law Administration.

Organisation of Finance Ministry

At present the Finance Ministry is organised into the following five departments:

(a) Department of Expenditure

(b) Department of Economic Affairs

(c) Department of Revenue and Banking

(d) Department of Disinvestment

(e) Department of Financial Services

Department of Expenditure:

The Department of Expenditure consists of the following divisions:

1. Establishment division including implementation Cell;
2. Staff Inspection Unit;
3. Defence Division;
4. Cost Accounts Wing;
5. Plan Finance Division;
6. Special cell including organisation of controller General of Accounts;
7. Bureau of Public Enterprises.

1) Establishment Division:

It is mainly responsible for the administration of various financial rules and regulations including those of services of central government Employees.

Implementation Cell:

Set-up-in April, 1973 the main function of this' cell is to advice various ministries regarding the revised pay scales of the employees of autonomous bodies and public sector undertakings following Central Government pattern of pay scales.

2) Staff Inspection Unit:

This unit was established in April 1964. This' unit has three types of functions:

1. To review the staffing of Government establishment with a view to determining, the strength and composition of staff required.
2. To forecast staff requirement by evolving and prescribing standards of performance
3. Job grading in terms of content responsibilities attached to posts.

3) Defence Division

This division is headed by a financial advisor with the rank of Addl. Secretary. The Financial Advisor is assisted by the three Addl. Financial Advisors (Joint Secretaries) and a number of Deputy Financial Advisors, each of them closely associated with an important branch of the Defence Organisation. The Financial Controller Raksha Utpadan Board, located, at Calcutta is also a part of defence division and is responsible for scrutiny, sanction and accounting of the expenditure of Defence Ministry.

1) Cost Accounts Wings:

The Wing is headed by Chief Cost Accounts 'Officer (Joint Secretary). He is further assisted by (1) Deputy Chief Cost Accounts Officer (2) Senior. Cost Accounts Officers (3) Cost Accounts Officers (4) Asstt. Cost Accounts Officers (5) Cost Accountants. The main functions of this Wing are :

1. To undertake cost studies in various units both, in public and private sectors.
2. To advice various Ministries/Departments of Government of India and Public Undertakings on costs and accounting matters referred for such advice.
3. To serve as members in Export Committee appointed by Government, when so required.

2) Plan Finance Division:

This division deals with matter relating to the finances and the plan outlays of the states. It is the focus points in the ministry of Finance for matter, connected with State Finances and State Plans. It analysis the state budgets and the States efforts at fiscal management and keeps close touch with states as regards their resources for including in the plan. This division also handles the work relating to the assessment of resources like the metropolitan authorities, Bombay, Calcutta and Madras, Damodar-Valley Corporation etc. and the determination of outlays for their plans programmes.

3) Special Cell Including Organisation of Controller General of Accounts:

A special cell has been created in the Ministry of Finance to bring about innovation and improvements in the Financial Administration system with special reference to the requirement of the Plan. This cell has been performing useful works by suggesting suitable changes after due deliberations. The controller General of Accounts is now responsible for consolidating. The Controller General of Accounts is now responsible for consolidating. The monthly accounts of the Central Government are to be placed before the Parliament.

4) Bureau of Public Enterprises:

This Bureau was set up in April, 1965 by the Ministry of Finance and the recommendations of the Estimates Committee. It performs the following functions:

1. To assist the concerned ministries and Finances Ministry in making a more expert scrutiny and evaluation of feasibility studies/ DPRs to the extent practicable.
2. To assist the ministries in controlling expenditure on residential and administrative buildings.
3. To compile information in terms and conditions of services of employees and to advice public undertakings, with a view to ensuring desirable uniformities in, these matters.
4. To furnish periodical reports to Parliament and Government on the working of Public undertaking
5. To function as the secretariat of Public Enterprises Selection Board

The Bureau is organised into Six constituent divisions, namely production, construction. Finance, Management, Information and Research and Administration and Coordination.

DEPARTMENT OF ECONOMIC AFFAIRS :

This department prepares and controls government budget, makes periodic assessments of foreign exchange needs and resources and taken steps to mobilize and allocate resources, in keeping with development and other needs. This department comprises of seven main division namely:

1. Budget
2. Internal Finance
3. External Finance
4. Economic
5. Administration
6. Insurance
7. Banking

1. BUDGET DIVISION

This division is responsible for the preparation of the central Budget, it is also responsible for certain other matters like preparation of the Ways and Means Estimates," floating of public loans promotion of small saving movement, administration of public debt, borrowing by the State Government, implementation of the recommendations of Finance Commission etc.

2. INTERNAL FINANCE DIVISION:

The division is responsible for the control of capital issues.. It deals with the matters concerning currency and coinage, including administration of Mints and their Assy. offices, the Security Paper Mills, the Indian Security Press, the Bank Note Press and Silver Refinery. This division is also responsible for administering the Securities contracts Act. 1956 and the regulation of stock exchange in the country.

3. EXTERNAL FINANCE DIVISION :

This division is concerned with the matters relating to exchange budget. Foreign investments and other external Finance including technical assistance received by India or rendered by her to foreign countries.

4. ECONOMIC DIVISION :

The main functions of this division are to study and analyse the trends and development in the economy in India as well as abroad and their implications with a view to keeping the Ministry informed and to render Economic advice to the Ministry. The work of this division is organised under five main units namely: 1. Prices production and wage policy, (2) Public Finance, money banking and credit policy, (3) Fiscal Policy, (4) Balance of Payments and Foreign Trade and (5) Economic information.

5. ADMINISTRATION DIVISION:

This divisions looks after the administrative matters the Department and vigilance and organisation methods of the Department as well as its attached subordinate offices. The internal work study cum D&M unit in this department assists in the identification of Kanor problems and other related studies besides its usual Q & M functions. This division is responsible for watching the progress in implementation of the instructions issued by the Ministry of Home Affair under the Official Languages. Act 1903, in the Secretariat proper and the attached subordinate organisation of the Department.

6. INSURANCE DIVISION :

The Insurance Wing administers the Insurance Act 1938. the LIC. Act, 1956. The Emergency Risks (Goods) Insurance Act, 1962, the Emergency. Risks (Factors) insurance Act, 1962, the General Insurance Emergency Provision Act, 1971 and General Insurance Business (Nationalization Act, 1972). This Wing is also administrative charge of the Insurance Claims Board set up under the Displaced Persons Act 1951.

7. BANKING DIVISION

The Banking Wing is concerned with the formulation and implementation of Government policies having a bearing on the working of Commercial banks and long term financial institutions excluding the LIC and UTI. the Banking wing have Five Functional Units - (1) Banking Operation Division (2) Industrial Finance Division (3)Agricultural Credit and Establishment Division (4) Development and Credit Policy Division, (5) Coordination, Vigilance and Industries Relations Division.

DEPARTMENT OF REVENUE AND BANKING:

The headquarters administration of the Department of Revenues is divided into three Divisions.

1. CENTRAL DIVISION

The division deals with settlement commission Appellate Tribunal for forfeited property. Indirect Taxation Enquiry Committee and also the Directors of Enforcement.

2. DIRECT TAXES DIVISION

The Central Board of Direct Taxes is responsible for the administration of direct taxes levied the Central Government, headed by the Chairman and six other members of the board, control and supervision over the function of subordinate offices.

Self-Check Exercise-1

Q.1 The Central Board of Direct Taxes is responsible for the administration of direct taxes levied the Central Government. True/False

Q.2 Department of Economic Affairs is responsible for Budget Making. True/False

4.3. FUNCTIONS OF THE ATTACHED OFFICER UNDER THE CENTRAL BOARD OF DIRECT TAXES

a) Directorate of Inspection, (income Tax and Audit New Delhi). The main functions of this office are:

3. Prescribing policy and programme of Inspection by I.A.Cs' Officers and supervising the work of Internal Audit parties and dealing with matters pertaining to Revenue Audit Objections
4. Carries out Administrative Inspection of field organisation.
5. Holds Department Examinations for department staff.
6. Dealing with all references received from all Heads of Departments relating to the recruitment examination.

b) Directorate of Inspection (Investigation), New Delhi.

There are three Directors of Inspection in this Directorate:

1. Functions of Investigation Wing:

To help field officers in improving techniques of investigation and also in gathering of income tax intelligence in order to combat tax evasion.

Coordination and keeping watch over investigations conducted in Selected cases in various income tax charges.

2. Functions of Vigilance Wing :

Director of Inspection (Vigilance) functions as Addl. Chief Vigilance Officer and deals with all cases of Gazetted and non-Gazetted staff involving vigilance angle.

3. Function of Special Cell:

This cell deals with cases of tax evasion by the Large Industrial Houses.

Directorate of Inspection (Research Statistics and Publications) New Delhi; This directorate is a combination of two wings:

1. Publication and Public Relations Wing:

a) Compilation and Publication of Various rules. Acts, Bulletins, and other publications pertaining to income-tax department.

b) Translation of material in Hindi and watching progressive use of Hindi.

c) All matters connected with public Relations.

2. Research and Statistics Wing:

a) Compilation and Supply of All India Revenue Statistics relating all direct-taxes.

b) Compilation and statistics on the basis of monthly progress report.

c) Conducting Research on various matters referred to them by the Central Board of Direct Taxes.

3. Directorate of Organisation and Management Services, New Delhi:

The main functions of this Directorate are :

1) Simplification of methods of work aiming at optimum utilization of manpower resources.

2) Solving and receiving the stalling norms and patterns supported by method studies.

3) Review of organisational structures and system of work.

4) Examination staffing proposals from the Heads of Department.

NDIRECT TAXES DIVISION:

This Division deals with the Custom Department; Central Excise Department, Narcotic Department and many other directorates. All these offices are under over all control of Central Board of Excise and Customs.

FUNCTIONS OF THE DEPARTMENT OF REVENUES AND BANKING

1) This Department exercises control vested in it in respect of revenue matters relating to all direct and indirect union taxes, through two statutory Board under it namely, Central Board of Direct Taxes and Central Board of Excises and Customs. The Chairman and six members of each of these two boards functions as ex-officio Addl. Secretaries to the Government of India;

2) Control over production and disposal of opium and its products produced within the country.

3) This department is also responsible for the administration of the Central Sales Tax Act.

4) The Administration of the conservation of foreign exchange and Prevention of Smuggling Activities Act. 1974 is also vested in the department of Revenue.

Self-Check Exercise-2

Q.1 This Division deals with the Custom Department; Central Excise Department, Narcotic Department and many other directorates. True/False

Q.2 CBDT holds Department Examinations for department staff. True/False

4.4 SUMMARY

Article 268 to 293 in Part XII of the Constitution of India deal with Centre- State Financial Relations. Beside these, there are other provisions dealing with the same subject. Constitutional provides for grant-in-Aid to the States from the Centre resources. There are two types of grant- in- aid i.e. statutory grants and discretionary grants. The statutory grants under Art. 275 (both general and specific) are given to the states on the recommendations of the Financial Commission. Art. 282 empower both the Centre and the State to make any grants for any public purpose, even if it is not within their respective legislative competence under this provision, the Centre makes grants to the state on the recommendations of NITI Ayog - an extra Constitutional body.

4.5 GLOSSARY:

- **Grant-in-aid:** an amount of money given to local government, an institution or a particular scholar.
- **Borrowing power :** the amount of money that a person, company or government can borrow at a particular time.

4.6 Answers to Self-Check Exercises

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

4.7 REFERENCES/SUGGESTED READINGS:

- Laxmikant, M. 'Public Administration' Fifth Edition, Tata McGraw-Hill Publishing Company Limited, New Delhi, 2016
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- Mahajan., S.K. & Mahajan., A. P. Financial Administration in India, P.H.I, New Delhi.
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4.8 Terminal Questions

Q.1 Discuss the structure of Department of Expenditure of Ministry of Finance.

Q.2 What are functions of the attached officer under the central board of direct taxes?

CHAPTER-5

FINANCE COMMISSION

Structure

5.0. Introduction

5.1. Learning Objective

5.3. Finance Commission: need & power

Self-Check Exercise-1

5.4. Commission's functioning & 15^{th} Finance Commission

Self-Check Exercise-2

5.5. Summary

5.6. Glossary

5.7. Answers to Self- check exercises

5.8. References/Suggested Readings

5.9. Terminal questions

5.0 Introduction: Federations are formed out of political, economic and social need. In a federation, the nature of financial relations between the centre and' the states depend upon the financial position of the states and the way in which the federation is established, i.e., federation established through independent States coming together, or countries dividing themselves into state for administrative convenience. When states are the creators of federation, they will have an upper hand in financial matters, otherwise the centre will have an upper hand. The basic characteristic of federations is the division of functions and tax-sources between the centre and the, states under the constitution. But there should be no overlapping of tax jurisdiction, otherwise it will cause conflicts and confusion.

5.1. LEARNING OBJECTIVES

After reading this lesson, the learner will be able:

- To understand about Finance Commission, need and power

- To know about functions of finance commission
- To evaluate the 15th Finance commission.

5.2. FINANCE COMMISSION: NEED & POWER

Need

In a federation, economic differences exists between different constituent units, two or more fiscal systems operate upon the financial resources of the citizens, and two or more taxing authorities Operate in the same geographical area. The. peculiarities of federal finance arise due to division of functions and financial resources between the centre and the states resulting in multiplicity of taxing and spending authorities and decentralized fiscal structure. A fixed division of functions and resources cannot work because of changing conditions, needs and aspirations. Hence, there is an inherent need for adjustments or reallocation, flexibility and adaptability without undermining the federal sprit and autonomy. The need for administrative and economic-efficiency, maximum utilization of national resources, 'acceleration of the pace of economic development, reduction in disparities and augmentation in production and productivity require adjustments and flexibility. Indeed, flexibility seems to be a sine-quo-non of a rational system of federal finance. The revenue sources allocated to the central and State Governments do-not yield precisely the sums needed for the discharge of functions by these governments.

The Centres revenue expenditure has/been on rise or more than its revenue receipts yet it has been found by experience that federal revenues are growing more quickly than states revenues and states' expenditure is growing as rapidly as federal expenditure. Therefore, resources have increased in the account of federal government and for spending has increased in the account of states devolvement. This is so because federal government has more elastic resources an states have more expansive functions. Hence, the imbalance in federal financial system. It' becomes inevitable to make adjustments in the financial system of federations because of the growth of activities of the modem state on the one hand, and the lopsided allocation or growth of financial resources on the other hand. Hence, there is need for adjustments or transfer of resources in the light of changing circumstances so, a constant and constructive appraisal of the federal finance system is essential, more so in a developing economy.

Article 280 of the Constitution provides for an independent quasi-judicial expert body known as finance commission for recommending the principles and proportions of financial transfers from the Union to the States through the built in balancing devices Finance Commission is constituted at the expiration of the every fifth year so at such earlier times as the President considers necessary. Finance Commission is governed by the basic principles of federal finance, which seeks to meet the residuary budgetary needs of the states, after taking into account the devolution of the proceeds of the 'Union taxes to the States. The underlying idea is that the constituents units, being at different stages of development need to be brought up to a minimum level, thereby aiming at equal sacrifice and equal opportunity. Finance Commission devise their own schemes and determine the quantum of statutory assistance to the states. By and large emphasis has been on the need to meet the budgetary gaps of the states.

The Finance Commission recommends on the followings:

7. The distribution between the Union and the States of the net proceeds of taxes which are the allocation between the States of respective shares of such proceeds.

8. The principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India.

The recommendations of the FC are laid before each House of Parliament. Eleven such Commissions have been set up so far. "The last" EC is yet to submit its report.

Composition of Finance Commission

The Indian Constitution has provided- for a FC under Article 280; to recommend mainly the financial transfers from the Union Government to the States with a view to reduce fiscal imbalances. This constitutional provision require that the President should appoint the-PC within two years from the commencement of the constitution and thereafter once in every five years or even earlier, if necessary. Article 280 also specifies broadly the terms of references of the FC under clause 3(a) and 3(b) and leaves only the terms of reference under clause 3(c) to be determined by the President depending upon the need for such references. Further, Article 280 has fixed the total strength of the FC by specifying that it could consists of:

Chairman	1
Other members	4

However, the Article 280 has left to the Parliament the power to prescribe the qualifications of a Chairman and other members of the FC as also the procedures for their appointment "and for the work of the FC.. Accordingly, the Parliament has created a legislation viz. the Finance Commission (Miscellaneous Provisions) Act of 1951.

The Finance Commission Act of 1951 specifies the qualification for the chairman and the members under section (3) in the following way:

"The Chairman of the Commission shall be selected from among the persons who have had experience in public affairs, and the four other members shall be selected among persons who:

1. are, or have been, or are qualified to be appointed as Judge of a high court: or
2. have special knowledge of finance and accounts of the government, or
3. have had wide experience in financial matters and in administration;

4. have special knowledge of economics;

The qualifications outlined for the members appear well-suited for the responsibilities of the EC. However, the same cannot be said for the Chairman, who should ideally have extensive experience in multiple fields listed for the members. Relying on experience in public affairs alone could lead to political appointments by the Union Government, neglecting the specialized knowledge and experience necessary for the role. Additionally, the use of the word "or" between the four qualifications for the members suggests that all four members could be chosen from the same area of expertise or experience, which was not the original intention of the framers of the Constitution. Although this extreme approach has not yet been implemented, it could be used by a defiant government at the center. Therefore, it would be better to replace "or" with "and" to clarify the intent and prevent misuse of legal provisions by the Union Government. Generally, the practice has been to appoint well-known public figures as Chairman, with members including at least one person representing the state's perspective, a distinguished economist, and a senior official from the Union Finance Ministry as the Secretary Member of the Commission.

Power of the Finance Commission:

According to clause (4) of Article 280 of the Constitution, the Commission possesses the powers that Parliament may grant to it through law. However, the background of this clause reveals that the Expert Committee on the Financial Provisions of the Union Constitution initially proposed that the Commission should have powers as determined by the President through an order. This proposal was accepted by the Drafting Committee on January 30, 1948. On February 3, 1948, the Drafting Committee revised this provision, replacing "President" with "Parliament" and "order" with "law." This revision was likely a result of changes made to clause (2), which granted Parliament the authority to specify the qualifications for the Chairman and members of the Commission. Consequently, Parliament was given the power to assign the Commission its authority through law, instead of the President doing so via an order.

As per the Constitution, Parliament passed the Finance Commission (Miscellaneous Provisions) Act, 1951, which was later amended by Act 13 of 1955 to confer powers on the Commission. Section 8 of the Act grants the Commission civil court powers under the Code of Civil Procedure, 1908, in the following matters: a) Summoning and compelling the attendance of witnesses; b) Requiring the production of documents; c) Requesting public records from any court or office.

Additionally, clause (2) of Section 8 empowers the Commission to require individuals to provide information on matters deemed relevant to its work. Such individuals are legally obligated to supply the requested information, as outlined in Section 176 of the Indian Penal Code. Furthermore, the Commission is recognized as a civil court under sections 480 and 482 of the Code of Criminal Procedure, 1898. As such, it has the authority to summon individuals, papers, and records, and compel the provision of information.

Self-Check Exercise-1

Q.1 As per Article 280 of the constitution, the commission enjoys such powers as Parliament by law confers on it. True/False

Q.2 Finance Commission recommends mainly the financial transfers from the Union Government to the States with a view to reduce fiscal imbalances. True/False

5.3. Functioning of the Finance Commission:

Once the Union Government announces the constitution of the Commission, the Chairman and designated members take charge. They then determine the sequence of the Commission's tasks and establish the rules of business. The rules of procedure are based on those outlined in the Constitution. Since the Third Finance Commission, each subsequent Commission has typically adopted the rules set by the Second Commission, with minor adjustments. They also generally follow the procedures established by their predecessors for engaging with State Governments and other stakeholders. The Commission issues a press note inviting input from all interested parties on the tasks assigned to it.

After the first meeting, the Commission's member-secretary sends a letter to the State Governments requesting them to provide forecasts of receipts and expenditures for both revenue and capital accounts for the period covered by the Commission's report. Additionally, the States are asked to supply information on certain related matters.

Similarly, the member-secretary writes to the Union Ministry of Finance requesting forecasts of the Union's revenue and expenditure for the period covered by the report, specifying the divisible pool of income tax and other central taxes likely to be allocated to the states. The Comptroller and Auditor General directs the states' Accountants General to assist the Commission with any required information. Since the establishment of the Sixth Commission, the range of information sought from the Accountants General has expanded significantly compared to previous Commissions, largely due to the inclusion of state governments' non-paid capital accounts in their scope.

The Commission receives memoranda from the States in response to its press note and follow-up letters on the issues at hand. These memoranda are reviewed, and key points for discussion with the States are noted. Similarly, the Commission receives estimates of receipts and expenditures for the relevant period from the State Governments. The Commission verifies the reliability of these estimates and invites relevant state officials to Delhi for clarification. The Sixth Commission introduced preliminary discussions between Commission officers and State Governments before formal meetings, a process that helped clarify numerous details and significantly streamlined subsequent discussions with State Chief Ministers, their colleagues, and senior officials. As stated by the Sixth Commission, "this preliminary exercise considerably facilitated the subsequent discussions." Following this, the Commission sets its schedule for state visits.

Once this initial phase is completed, the Commission embarks on a tour of the states, typically visiting the capitals. After completing these discussions and analyzing the materials presented, the Commission holds consultations with officials from the Union Ministry of Finance regarding the Union Government's forecasts and its views on the Commission's terms of reference.

Once the second stage concludes, the Commission reconvenes in Delhi to prepare and finalize its report. At this point, the role of the staff becomes crucial. The Commission is supported by skilled officers, research staff, advisors, and consultants, who contribute significantly to the Commission's successful operation and high-quality output.

Fifteenth Finance Commission (Chairman: N.K. Singh)

The terms of reference and key considerations for the Fifteenth Finance Commission, under the leadership of N.K. Singh, for the period 2020-25, in formulating its recommendations, are as follows:

- The distribution of net tax proceeds between the Union and the States, as outlined in Chapter 1, Part XII of the Constitution, and the allocation of the respective shares of these proceeds among the States.
- The principles that should guide the allocation of grants-in-aid from the Consolidated Fund of India to the States, as specified under Article 275 of the Constitution, for purposes beyond those mentioned in the relevant clauses of that article.
- The measures required to enhance the resources of the states' Consolidated Funds to support Panchayats and Municipalities, based on the recommendations made by the respective State Finance Commissions.

The Commission will also assess the financial health of the Union and State Governments, focusing on deficits, debt levels, cash balances, and fiscal discipline. It will recommend a roadmap for fiscal consolidation aimed at sound fiscal management, considering the responsibilities of both the Central and State Governments to maintain appropriate levels of debt and deficit, while promoting inclusive growth. The Commission will also evaluate whether to provide revenue deficit grants.

In formulating its recommendations, the Commission will consider, among other factors, the financial resources available to both the Central and State Governments for the five-year period beginning April 1, 2020. This will be based on expected tax and non-tax revenue levels for 2024-25, taking into account both the potential and fiscal capacity of these revenues.

Self-Check Exercise-2

Q.1 Finance Commission suggests the measures needed to augment the consolidated fund of a state to supplement the resources of the Panchayats and Municipalities in the states on the basis of the recommendations made by Finance Commission of the State. True/False

Q.2 Finance Commission recommends the distributions between the union and the states of the net proceeds of taxes which are to be or may be, divided between them under chapter 1, Part XII of the Constitution and the allocation between the states of the respective shares of such proceeds. True/False

5.4. SUMMARY

The Ministry of Finance is responsible for mobilizing resources to Finance Government spending and controlling Government spending at both the stages i.e. budget making and budget execution stage. It is also a major participant in the making of fiscal and Economic policies. It is organised into five department i.e. Department of Expenditure, Department of Economic Affairs, Department of Revenue, Department of Disinvestment and Department of Financial Services. Article 280 of the Constitution of Indi a provides for a Finance Commission as a quasi-judicial body. It is constituted by the President of India every fifth year or at such earlier time as he considers necessary. Finance Commission consists of a Chairman and four other members to be appointed by the President. The Constitution of India envisages the Finance Commission as the balancing wheel of the Fiscal federalism in India.

5.5. GLOSSARY

- **Establishment Division :** it is a division of Deptt. of expenditure headed by Joint Secretary.
- **Fiscal decentralization :** it is essentially the transfer of expenditure responsibilities and revenue assignment to lower level of government.
- **Composition :** the parts that form something the way in which the parts of something are arranged.

5.6 Answers to Self-Check Exercises

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

5.7. REFERENCES/SUGGESTED READINGS

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5.8. TERMINAL QUESTIONS

a) Discuss the main functions of Finance Commission.

b) Finance Commission is a balancing wheel of Fiscal Federation in India. Discuss.

BLOCK-II

Unit-6

BUDGET: MEANING AND PRINCIPLES

Structure

6.0. Introduction
6.1. Learning objectives
6.2. Balanced budget & Problems of deficit financing
Self-Check Exercise-1
6.3. Principles
Self-Check Exercise-2
6.4. Summary
6.5. Glossary
6.6. Answers to self-check exercises
6.7. References/Suggested Readings
6.8. Terminal questions

6.0. INTRODUCTION

Since the inception of the planning era in India, the budgetary transactions of the governments, both at the Union and State levels, have assumed a great significance on account of their magnitude and diversification in the direction of socio-economic development. Before we discuss the principles of budgeting, let us understand the meaning of the term Budget.

The Budget is a statement of Income and Expenditure for a particular period of a Government. Aaron Wild Avoky defines budgets as, attempts to allocate financial resources through political process in the context of USA. The Public Accounts Committee states the object of budgeting in the following words: "The budget is designed to provide for Parliamentary control, for administrative accountability, for the auditing of transactions, for ensuring that the expenditure incurred by the Government is in the specific manner and by the specified authority."

The Oxford Dictionary defines a budget as a "Statement of probable revenue and expenditure for the ensuring year with financial proposals, founded thereon, annually submitted by the exchequer for the approval of the House of commons. Hence, any analogous statement, estimate or proposal." According to W.F. Willoughby, "The Budget, thus, is something much more than a mere estimate of revenues and expenditure. It is, or should be at once a report, an estimate, and a proposal. It is, or should be, the document through which the Chief Executive... comes before the fund raising and fund granting authority and makes a full report regarding the manner in which he and his subordinates have administered affairs during the last completed year; in which he exhibits the present condition of the public treasury: and on the basis of such information, sets forth his program of work for the year to come and the manner in which he proposes that such work should be financed."

A budget is "a comprehensive and coordinated plan, expressed in financial terms, for the operations and resources of the government for some specific period in the future". It is a predetermined plan expressed in financial terms which generate all the income and expenditure estimates required by a government for a definite' future period.

Budget preparation is a highly intellectual exercise and needs expertise in the areas of finance, development administration, statistics, computer programming, international economics and trade. It is very difficult to discuss all the principles, which need to be followed in the preparation of the budget. Accordingly, we discuss here only a few important principles.

6.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand the meaning and principles of budget.
- To know about preparation of budget as per Economic and functional classification
- To discuss the different types of budget.

6.2. BALANCED BUDGET AND CHALLENGES OF DEFICIT FINANCING

A balanced budget means that the government's revenue matches its expenditure. When the government’s income exceeds its expenditure, the budget is considered a surplus, which can lead to deflationary conditions, resulting in unemployment and falling prices. On the other hand, if income is less than expenditure, the budget is termed a deficit, which can cause inflation and rising prices.

However, many governments, particularly in developing countries, use deficit budgeting as a tool for development. Graham Hockley has advocated for using deficits to stimulate development. He states, "The concept of the balanced budget is appealing on an individual level, due to the analogy with household economies, but it holds no validity at the national level. It is dangerous as it obscures the real issues, which concern the optimal use of the nation’s resources."

In a broader sense, the gap between investment and domestic savings (resources) is an indicator of the deficit in the economy. The First Five-Year Plan defines deficit financing as, "The term deficit financing refers to the direct increase in gross national expenditure through budget deficits, whether on the revenue or capital account. This policy involves government spending exceeding its revenue from taxes, state enterprise earnings, public loans, deposits, and other sources. The government may cover the deficit by drawing from accumulated reserves or borrowing from the banking system," which leads to an increase in the money supply. The rationale behind deficit financing is the need for resources to promote development. Since taxation and borrowing alone are insufficient, the government resorts to deficit financing to expedite the development process. Deficit financing becomes necessary due to the depletion of resources and the rise in expenditures.

The term "deficit financing" used by the Government of India has typically referred to "overall budget deficit," which excludes government borrowing from markets or raising funds from public savings schemes like national small savings, post office savings, and provident fund collections. These receipts are classified as capital receipts and are excluded from the budgetary deficit calculation. This traditional view of deficit financing was limited and only indicated the extent of the monetary deficit.

A revenue deficit occurs when current revenue expenditure exceeds current revenue receipts, reflecting the government’s inability to cover its current expenses with its current revenues. A budgetary deficit is the excess of total expenditure over total receipts, which includes both revenue and capital receipts. After years of debate over the "budget deficit" or "overall budget deficit" concept, the Finance Ministry moved away from this conventional definition in the 1997-98 budget.

Fiscal deficit is the difference between total expenditure and total revenue receipts, including capital receipts but excluding borrowings and liabilities. In recent years, the Finance Ministry introduced the concept of "primary deficit," which is calculated as: **Primary Deficit = Fiscal Deficit - Interest Payments.**

To illustrate, revenue deficit increased significantly from Rs. 18,650 crore in 1991 to Rs. 77,430 crore in 2001. As a percentage of GDP, the revenue deficit averaged around 3.6%. Meanwhile, fiscal deficit grew rapidly from Rs. 44,630 crore in 1990-91 to Rs. 1,11,280 crore in 2000-2001. The government had set a policy to reduce the fiscal deficit to a permissible 4% of GDP, but it has yet to meet this target.

It is crucial to understand that deficit financing cannot create real resources that are lacking in the economy. It is merely a mechanism to transfer resources to the government. The actual resources needed for economic development—such as materials, equipment, skills, and labor—must already exist within the economy. These cannot be generated by printing money or issuing bank credit.

PROBLEMS OF DEFICIT FINANCING

a) Inflationary Rise in Prices

Prices tend to increase with the increase in money supply. Jacques de Larosiere, Governor of central Bank France, opines that, "inflation is socially unjust as it always hits the worst off hardest-but also it is regressive in terms of economic development.. inflation destabilizes expectations, affecting investment and consumption decisions."

b) Change in the Pattern of Investment

People start investing in unproductive investments like real Estate to beat the inflationary trends.

c) Forced savings resulting in less conssimption by the fixed income groups.

d) Credit Creation by Bonds.

e) Self-defeating in the Long-Run

The Economic Survey also expressed that persistent and large deficits have serious implications not only for the finances of the Government but also for price stability and economic growth... The immediate task is to check the fiscal imbalances before the situation assumes alarming proportions.

We have resorted to deficit financing beyond reasonable limits. The purpose of deficit financing could not be attained, as the resources raised through deficit financing have not been profitably used. The country is passing through a very critical period. It is high time that we should be cautious in the use of more and more deficit financing. The government may also try to increase its own resources through the checking of tax evasion and by reducing its expenditure through administrative reforms. Structural Reforms should be implemented quickly otherwise, the resources will be eaten away as before.

Deficit financing could be a helpful device and a valuable tool in promoting economic development in an under-developed country like India. The increase in the volume of money (because of deficit financing) results in higher demand for labor and other resources: As such, deficit financing is regarded as a good tool to activate a backward and developing economy. But, extreme caution is necessary in using deficit financing for economic development. For, it is basically, inflationary in character, and hence, proper controls are required. Besides, experience of other countries clearly shows that deficit financing may lead to excessive paper currency notes which will greatly reduce the value of money. Deficit financing, like fire, is a good servant but a bad master. This is exactly what has happened in our country. It needs radical steps to control deficit financing. Now that inflation has been officially declared as our number one problem, everyone has started cursing deficit financing.

It is important to emphasize the fact that deficit financing cannot create real resources, which do not exist in the economy. It is otily a device, which helps in the transfer of resources to the Government. The real resources required for economic development must exist in the form of materials, equipment, skill and labor. These things cannot be created by printing money or issuing bank credit.

However, we must use the deficit budget with caution, otherwise, a country can be trapped into debts and the purpose of development can be defeated. The extent of the deficit budget needs to be kept under control and within reasonable limits, otherwise, the whole economic and financial system may collapse.

PREPARATION OF BUDGET AS PER ECONOMIC AND FUNCTIONAL CLASSIFICATION

The budget presented on the basis of revenue and capital accounts does not clearly reveal the true nature of economy. It is not possible, for example, to get a clear idea of capital formation out of budgetary resource's. There is a need to prepare economic and functional classifications of Government budgetary, transactions to understand the true nature of fiscal and economic policies. The ultimate aim of these classifications is to correlate the information generated from the Government Sector to other major sectors of the economy required for an effective economic policy. The Economic and Statistical Organization of the Planning Department of Haryana in Publication No. 493 has delineated the budgetary transactions of the Government of Haryana into six accounts (Based on United Nations Documents) as given below:

Account I : Transactions in Goods and Services and Transfers. Current Account of Government Administration.

Account II : Transaction in Goods and Services and Transfers Current Account of Departmental Commercial Undertakings.

Account III : Transactions in Goods and Services and Transfers Capital Account of Government Administration and Departmental Commercial Undertakings.

Account IV : Changes in Financial Assets Capital Account of Government Administration and Departmental, Commercial Undertakings.

Account V : Changes in Financial Liabilities Capital Accounts of Government Administration and Departmental Commercial Undertakings.

Account VI : Cash and Capital Reconciliation Account of Government Administration and Departments Commercial Undertakings.

The economic classification groups expenditure by their economic character. B.N. Gupta, mentions the following limitations of economic classification?

f) Economic classification does not purport to measure the whole of government's impact on levels of economic activity. It measures a part of the impact and this too, only in approximate terms. It can furnish information about the contribution of the government to the national income and whether that contribution is increasing or decreasing.

g) Such a classification can record only those changes which are due to governmental revenue and expenditure and not otherwise.

h) An economic classification does not, in itself, provide an estimate of the effects of governmental activities on the distribution of income, and not the effects on its division among sectors of the economy (Agriculture, Industry, etc.) This kind of information is of great importance in the formulation of fiscal policy, for both expenditure and taxation.

Functional classification groups the heads of expenditure according to the particular purpose they serve. The functional classification enables one to distinguish between development and non-development expenditure. The UN report on Economic and functional classification of Government transactions has suggested the following functional classifications under eleven 'major categories; (1) General, Government Services, (2) Civil Defence (Police), (3) Education, (4) Medical,. Public Health and Family Welfare, (5) Social Security and Welfare Services, (6) Housing and Community Services, (7) Cultural, Recreational and Religious Services, (8) Economic Services, (9) Other Purposes, (10) Interest, and (11) Public Debt.

These can be further split into development and non-development activities:

a) Development activities- Education, health, social security and welfare, housing and other community services, cultural, recreational and religious services, economic services.

b) Non-Development activities- General Government services, civil defence, other services, interest, public debt.

Such a classification can help in the development of performance budgeting, which is ideal for the developing countries. C.O. Omeh has rightly said &at, "the modem budgetary theory presupposes that budgetary policy is a powerful instrument of economic regulation. It can, therefore, be employed to attain the planned economic objectives."

Such economic goals include high rates of economic growth; reduction in unemployment or attainment of full employment; stability of the price level and equitable distribution of income or reduction in inequality. The budgetary policy could, therefore, be used to keep the economy on an even keel.

Self-Check Exercise-1

Q.1 Deficit financing could be a helpful device and a valuable tool in promoting economic development in an under-developed country like India. True/False

Q.2 Who said that, "the modem budgetary theory presupposes that budgetary policy is a powerful instrument of economic regulation. It can, therefore, be employed to attain the planned economic objectives."

COMPREHENSIVENESS

The budget needs to be an integral part of the fiscal policy of the Government and should project a clear picture of revenue and expenditure of the Government. The comprehensive budget will help us to understand the financial health of the Government- a sine-quo-non for development and nation building.

The elements of comprehensiveness and coordination are indispensable in budgeting. Various ministries are required to prepare their individual budget estimates, which need coordination, as they are mere components of the toaster or comprehensive budget. A master budget is, therefore, a conglomeration of budget estimates of individual ministries, which have been coordinated and collated into a single comprehensive budget.

INTELLIGIBLE

The Budget may be couched in such language and style, which can be intelligible to different sections of the people. In practice, budget is drafted in such difficult language that it is beyond the comprehension of the ordinary citizen, resulting in his disassociation with budget and loss of interest. Keeping in view the level of literacy in the country, we need to find ways and means to enlist the support of the common people and create interest in them so that they can give their viewpoint and assert in claiming the benefit out of the budget.

ACCURACY AND EXACTNESS

All the officers engaged in the preparation of the budget need to devote time and energy to collect facts required for the preparation of the exact budget, otherwise it leads to faulty distribution of resources among, different activities and organizations. This is one of the signs of bad administration, as it results in some organizations having more money than required while others having less money than requited. P.K. Wattal has rightly said that, "the task of preparing budget estimates is of one requiring sound judgement and experience. It is not a simple arithmetical exercise in striking out average of previous year's actuals.... Behind figures lie the insistent realities of administration.

The Eighth Report of Public Accounts Committee 2000-2001, Lok Sabha, based on thorough scrutiny of many departments, rightly mentions that, "The responsibility- of framing Budget Estimates on realistic basis and also to ensure that there is neither considerable short-fall nor unforeseen excess expenditure rests on Ministries/Departments. To achieve this, the Financial Advisers are required to ensure that prescribed Financial Rules and procedures are followed scrupulously. The Heads of the Departments have been advised accordingly The Ministries'/Departments have also been advised to devise suitable mechanism for tightening the exchequer control so that it does not lead to excess expenditure and deal sternly with cases where any slackness in following the prescribed financial rules is noticed". It is, thus, necessary to exercise utmost care and foresight in framing the forecast of receipts and estimates of annual expenditure. There should be a close approximation between the income forecast and actual receipts and also between the budget grants and the actual expenditure.

The Sixth Report of Public Accounts Committee 1999-2000, 13th Lok Sabha rightly comments that, "Although the Constitution as well as the General Financial

Rules and the provisions in various department codes clearly stipulate that no money shall be drawn from the Consolidated Fund of India except under appropriation made by law and that no expenditure shall be incurred over and above the total grants or appropriations authorized by Parliament by law for a financial year except after obtaining supplementary funds or an advance from the Contingency Fund, the Committee are constrained to observe that some Ministries/Departments of Union Government continue to display callous attitude towards rules laid down for containing the expenditure within the authorized limits. While viewing this state of affairs with grave concern, the Committee would like to emphasize that the Secretary, Department of Expenditure in the Ministry of Finance should strongly and effectively draw the personal attention of the Secretaries in all the Ministries/ Departments of the Union Government to bear in mind that excess expenditure is unauthorized" expenditure and that the authority administering a grant/appropriation would be held personally responsible for the control of expenditure against the sanctioned provisions in terms of the instructions issued by Department of Expenditure on 17.10.94 in pursuance of the recommendation made by the Committee in paragraph 1.20 of their 60th Report (10th Lok Sabha). The Committee also desire the Department of Expenditure to impress upon all the Ministries to ensure rigid enforcement of prescribed financial rules and procedures so as to contain the instances of excess expenditure only to genuine and inevitable payments. Steps should also be taken to deal sternly with cases where any slackness is noticed in observance of prescribed financial rules."

All the officers need to make earnest and sincere efforts to ensure that money in the budget is allocated to the areas where maximization of output is possible, and in the priority areas. It has been observed that most of the officers are in a hurry and prepare the budget on intuition, rather than facts. Such officers ought to be given training in the art and science of budgeting.

PUBLICITY

Since the resources are to be raised from the public, they need to be involved at different stages of the budget preparation. It is seen that only a negligible proportion of the people react to budget proposals, which is not a sound tendency. We should educate people in the rural areas to understand the implications of the budget so that they can contribute to this exercise and watch their own interests.

RULE OF LAPSE

Budget may be for a definite period and whatever is not used during that period may be transferred back to the state exchequer. This would keep the drawing and disbursing officers alert and active as they have to use these resources for the welfare of the people in given period of time. The period may be a year as is generally the case in modem Government, including India. However in United Nations, the budget is prepared Biennially.

SEPARATION OF REVENUE AND CAPITAL ACCOUNTS

The revenue and capital portions of the budget should be kept separate. The revenue and capital portion of the budget should be indicated separately so that a correct understanding of the budget is possible.

GROSS AND NOT NET INCOME

The budget should be based on gross income and not net as it gives a total and realistic picture of working of a department by examining separately income and expenditure therein.

FEED BACK

The officers dealing with budget should get a proper feedback, which can help in reviewing and further action during supplementary budget or in the-next year. Feedback should be an integral activity of the budget and in fact should be inbuilt in the system.

RESEARCH

The Government of India and State Government may seek help, guidance and advice from financial research institutions, Departments of Economics. Public Administration, Commerce and Business Management etc., in framing the budgets, based on the research conducted by them. This would bring "Think Tank" of the Government" and the universities nearer, to ensure welfare of the people. The universities would also become active with this role and serve as a bridge between the community and the Government.

UNITY OF THE BUDGET

The budget of the Government should be based on the concept of unity. In India, the Railway budget was made separately to take special care of its business nature. But now there is only one Annual Budget in India.

CASH BASIS

Estimates should be on a cash basis and not the accrual basis i.e. that money should be included in the budget, which is realized in that period. This will make the budget realistic.

Self-Check Exercise-2

Q.1 Estimates should be on a cash basis and not the accrual basis. True/False

Q.2 The budget should be based on gross income and not net as it gives a total and realistic picture of working of a department by examining separately income and expenditure therein. True/False

6.4. SUMMARY

The term "Budget" refers to the statement of Income and Expenditure for a period of a government. The Oxford dictionary defines a budget as a "Statement of probable revenue and expenditure for the ensuring year with financial proposals funded thereon, annually submitted by the exchequer for the approval of the House of Commons. A budget is a "Comprehensive and Coordinated plan, expressed in financial terms, for the operations and resources of the government for some specific period in the future. It is a predetermined plan expressed in financial terms which generate all the income and expenditure estimates required by a government for a definite future period.

6.5. GLOSSARY

- **Estimate :** a gross or judgement about the size, cost etc. of something.
- **Accountability :** admitting responsibility.
- **Incremental :** gradational, gradual step by step.

6.6. ANSWERS TO SELF CHECK EXERCISES:

Self-Check Exercise-1

Q.1 True

Q.2 C.O. Omeh

Self-Check Exercise-1

Q.1 True

Q.2 True

6.7. REFERENCES/SUGGESTED READINGS

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6.8. TERMINAL QUESTIONS

o) "Budget should be on Annual Basis", Discuss.

p) Discuss about the elements of comprehensiveness & Coordination of Budget.

Unit-7

PREPARATION AND PASSAGE OF BUDGET

Structure

7.0. Introduction

7.1. Learning objectives

7.2. Features & Preparation of budget

7.4. Preparation of defence & railway budget

7.5. Summary

7.6. Glossary

7.7. Self check exercises

7.8. References/Suggested Readings

7.9. Terminal questions

7.0. INTRODUCTION

Normally, there are five stages in the budgetary procedure : (1) preparation of the budget; (2) budget in the legislature-presentation, discussion and sanction; (3) execution of the budget; (4) national accounting : and (5) audit. In India, functions (1), (3) and (4) are the responsibilities of the executive government; function (5) is performed by the Comptroller and Auditor General .of India In this chapter, a discussion on the procedure, of the preparation of the budget in this country would be attempted; but before that let us take up the normal features of budget.

7.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand the features of budget.
- To comprehend about method of budget preparation.
- To know about estimates of reverse.

7.2. FEATURES & PREPARATION OF BUDGET :

Features

The budget system, it will be observed, is the means by which financial administration is expressed broadly, and, therefore, what has been laid about the general characteristics of a good system of financial administration applies equally to the budget system. The budget system consequently, provide for unity and centralisation; for control at all stages of budget procedure; for simplicity, promptness regularity: and for efficiency of functioning. Obviously, the budget should be characterized by the following :

1) The estimates should be on cash basis

The budget should be prepared on the basis of what is expected to be actually received for paid, under sanction of the legislature during the current financial year and the arrears of past years, and not for demands or liabilities falling due within the years. Consequently, the budget is an estimate of falling due within the years. Consequently, the budget is an estimate of cash receipts and cash payments during the financial year to which it relates, notwithstanding the fact that such receipts . and payments relate to the year or previous year(s).

2) One budget for all functional transactions:

Separate - budgets for administrative departments or preparation and presentation of extraordinary budgets for special purposes observe the true financial position of the state and make. It difficult to coordinate the financial activities of the various departments so as to assess the real surplus or deficit on the whole. Accordingly, these should be principle of financial transactions of the government for the year. The aforesaid criterion, however, applies to administrative departments, and not to be departmental commercial sand: industrial undertakings, like Railways in India, for which separate budget is considered necessary.

3) Budgeting should be gross and not net :

The gross transactions in the case of both receipts, and charges in each departments should be entered separately estimating, the receipts on the receipt side of the budget and the expenditure on the expenditure side, i.e. to deduct receipts from charges or vice versa and frame the budget for net receipts or expenditure is not allowed. The provision is necessitated because in the absence of such, procedure, the legislature would lose its control over the expenditure of the government which has considerable receipts for meeting expenditure and approaches the former for grants only for the amount of the expenditure which the latter cannot meet from such receipts.

4) Estimating should be close :

The general tendency among the persons responsible for estimation of the budget proposals is to underestimate the revenue, and over-estimate the expenditure. To a certain extent this tendency may be natural and prudent, but the budgeting should be as close as possible so as to assure the legislature that more should be as close as possible so as to assure the legislature that more money is not taken away from the tax payer than is absolutely necessary for the requirements. Obviously, this would be the case if the underestimation of revenue and the over-estimation of expenditure is out of proportion. Moreover, the Ministry of Finance should also be interested to ensure that the administrative departments do not get more funds than what they really need, if a department is allotted funds which are an over-estimate and accordingly they would not be spent, the other useful schemes with other departments may be unnecessarily starved of financial allocation. 'Close budgeting means also that the services for which provision has been made out, the particular items included in any vote should be specified and there should be no demands for lump-sums under any head which the executive may be at liberty to allot after the budget has been voted, for any purpose it pleases.

5) The budget should be on actual basis :

Barring for exceptions almost in all modern economics, the budgets are voted for one year. Firstly, a year corresponds with the customary measure of human estimation, and secondly, a year appears to be the maximum period for which legislatures can afford to give financial sanctions to the executives and the minimum time which the executive needs to. Execute the budget effectively.

6) The rule of lapse:

All appropriations voted by legislature expire at the close of the financial year as "no portion unexpended during the year may be reserved or appropriated by transfer to deposits or any other head, or drawn and kept in the cash chest to obviate the lapsing of the grant was made. This is known, as the 'rule of the lapse'. Although the rule prevents economical planning of expenditure over a long periods and also leads to what is known as rush of expenditure at the end of the financial year, the financial control would become impossible if the administrative departments were permitted to spend, in any year, unutilized savings of previous years in addition to the grants voted for that particular year. Moreover, any advice for rendering grants non-lapsing by withdrawing amounts to a fund outside the Consolidated Fund is contrary to the very fundamentals of parliamentary control and proper financial discipline.

In India, in order to avoid the abnormal rush of payments towards the close of the financial year, the administrative ministries had been advised by the Union Ministry of Finance that, whenever grants have not been used to the full extent for valid reasons, the Finance Ministry would be prepared to consider; proposals to allot provision for the unexpended amounts either in the original budget of the coming year or by means of supplementary grants in that year provided the purposes for which these amounts were originally included in the sanctioned grants continue to be operative. It is hoped that, with this assurance, the ministries concerned would take positive steps to prevent the rash of expenditure in the closing months of the year, and also to refrain from making purchases in a hurry merely to avoid lapse of grants.

7) Form of estimates to correspond to the accounts :

It is essential that, for an easy understanding and proper financial control, the form of estimates should conform to that of national accounts. In India, the rules for the conduct of business in parliament provide that the budget shall be presented to parliament in such term as the Finance Ministry may, after considering the suggestions (if any) of the Estimate Committee settle.

8) Estimates to be prepared on departmental basis :

Each ministry/Department should estimate for the whole receipts and payments with which it deals finally, irrespective of the fact that such receipts or charge is on account of another ministry /department.

PREPARATION OF BUDGET

The preparation of the budget estimates in the first step towards the financial administration of any country. Viewed from the authority responsible for preparing the budget, the budget can be classified into three categories: (a) Legislative type, (b) executive type, and (c) board or commission type. Legislative type or budget is prepared ordinarily by a committee of legislature on the request of the executive. Ordinarily by a committee of legislature on the request of the executive. Since it is the legislature which prepares the budget as well as approves it, this type of budget, gives more importance to the legislature than the executive. It is doubtful, however, if the legislature would command the necessary competence in order to prepare a budget as the requirements of various ministries/departments could best be known only to the executive. As regards the executive type of budget, in almost all the countries who have adopted a system of parliamentary democracy, this type of budget is in vogue. After the budget is approved by the legislature, the executive becomes responsible for its execution. The board or commission type of budget is one which is prepared by or bound or commission consisting' wholly of administrative officers or of administrative and legislative representatives, jointly. The system is prevalent in some of the states in the Unites States of America and in some municipal governments.

Of all the agencies which can possibly be charged with the responsibility of the preparation of the budget, the executive should be the fittest body. "The Executive alone can and should do this work, situated at the centre of government, reaching through its hierarchical organisation to the smallest unit, the executive more than anybody else is in a position to feel public needs and wishes, to appreciate their comparative merits and accordingly to calculate, in the budget, a just appropriation which each of these needs and wishes deserves. Others may know certain ' details as well possibly better than the executive, but no body can have so extensive and impartial a view of the mass of these details, and no one can comprise the conflicting interests with so much competence and precision. Moreover the execution of the budget, is compelled' thorough concern as to its future responsibility, to prepare as well execute the plan." According to another authority, the responsibility for preparing the budget falls upon the executive a procedure which is quite universally approved among the critics. Public opinion ordinarily holds the chief executive responsible for the financial success over either the receipts or the expenditures. The executive is in the best position to view the financial problem as a whole and to assume the responsibilities for the success and failure of a financial programmes.

There is a general agreement, therefore, that the preparation of the budget should be the responsibility of the executive government. In India, as in any other democratic country where the budgetary system has been adopted the same, principle is followed and there is a clear provision in the financial codes that the responsibility for the preparation of the budget estimates lies on the executive government. The task relating to the preparation of the budget is carried on by three agencies: (1) the Ministry of Finance; (2) the administrative ministries/departments; and (3) the Planning Commission, India adopted a system of planning for economic development since 1951- 52, and since a major portion of investment activity is undertaken in the public sector, while regarding the budget, particularly the capital budget, the Ministry of Finance has to be in close touch with the Planning Commission in order to incorporate in the budget the plan priorities.

In India, the 'Annual Financial Statement' laid before both the Houses of Parliament in accordance with the provisions of the constitution, constitutes the budget of the Indian Union. This statement covered all the transactions of the union government during the current and the budget years. The budget of the Indian Railways is separately presented to the parliament and dealt by it. But as the receipt and expenditure of the railways are, nevertheless, the receipts and expenditure of the union government, the figures relating to those are also included in lump sum in the above statement.

The Annual Financial Statement is prepared by Major Heads of Accounts, such heads of accounts falling either under Consolidated Fund or in the Public Account of the government. The receipts and expenditure of government fall under one are other major heads either in the consolidated fund or the Public Account in accordance with the prescribed rules of classification.

The estimate of expenditure, must be shown separately:

1. The sums required to meet expenditure which the constitution has 'charged' upon the Consolidated Fund of India (a) this expenditure is obligatory and therefore, no subject to the "site of the legislature, although there is nothing in the constitution to prevent a discussion on it; and (b) the sums required to meet other expenditure to be voted by the legislature. The estimates are also split-up from those on Capital Account. The letter voters disbursements on capital outlay, advances granted by the government, discharge of permanent debt and other items of similar nature. The estimates of expenditure are also split-up into demands for grants. These demands of expenditure are also split-up 'into demands for grants. These demands are arranged Ministry-wise generally cover the requirements of each administrative service.

The revenue estimates are prepared in the Ministry of Finance on the basis of existing levels of taxation at that Mme and the trends of collections. The effects of taxation proposals, if any, are indicated separately in the budget.

The Indian budget year commences on 1st April and consequently the budget grants for the budget year are available for expenditure from 1st April to 1st March next year. The various stages leading upto the preparation and compilation of the budget are:

1) preparation and consolidation of the estimates . by the needs of ministries/departments;

2) scrutiny of the estimates by tile department controlling, officers;

3) scrutiny by the Ministry of Finance;

4) consolidation of the estimates by the, Ministry of Finance; and

5) consideration of the consolidated estimates by the executive government and a further review in the light of any comments.

In about September or October every year, i.e. 5-6 months before commencement of the fiscal year. The administrative units or the operating agencies are required to make estimates of the expenditure required during the next fiscal year. The general rule is that he who spends the money must also prepare estimate in advance. The items of income and expenditure contained in these statements show: (a) actual figures or the previous three years; (b) the sanctioned budge; estimates of the current year; (c) revised estimates for the current year; (d) proposed estimates for the next financial year, with reason for any increase or decrease in estimate; and (e) accruals of the current year available at the time of preparation of the estimates and accruals for the corresponding period of the previous year. "The tasks of framing the budget estimates is one requiring sound judgement' and experience, it is not a simple arithmetical exercise in striking out averages of previous years accruals and putting in a safe figure which would not look exactly like a repetition of tire last year's performance. No circumstances of one year are exactly similar to those of the previous year and yet they are not quite dissimilar. One has therefore, to use his judgement, estimating the similarities and dissimilarities and making due allowances for each."

The estimates proposed by the ministries/departments then go to the respective department controlling officers who: (a) scrutinize them fully: (b) revise the estimates where necessary giving reasons therefore: and (c) give the approval. The consolidated estimates are then transmitted is to Ministry of Finance.

Self-Check Exercise-1

Q.1 In budget, estimates to be prepared on departmental basis. True/False

Q.2 In Constitution, Annual Financial Statement is mentioned instead of budget. True/False

7.3 PREPARATION OF THE DEFENCE & RAILWAY BUDGET:

DEFENCE

While preparing the estimates for defence, such estimates are split up into primary units of appropriation. The overall control of the defence vests in the Finance Wing of the Ministry of Defence, which is divided into several branches each under a principal staff officer. These branches prepare the estimates which are submitted to the Ministry of Defence where they are scrutinized in a meeting where three services are invited and at which the representatives of the Finance Division of the Ministry of Defence are also present. Then the estimates are submitted and finally reach the Financial Adviser and the Secretary and if any further policy decisions are to be taken, it is done at this level. The budget then goes to the Defence Committee of the Cabinet for approval. After such approval the estimates are sent to the Ministry of Finance for incorporation in their estimates.

PREPARATION OF THE RAILWAY BUDGET:

Indian Railways are a Departmental Commercial Undertaking of the Government of India and as such a different method is followed in preparation of the Railway Budget. The framing of the budget has to be proceeded by a careful forecast of the expected traffic, both passenger and goods, to be handled by the railways during the budget year. Such a forecast must be based upon a clear view of the functioning of the economy in the budget year.

On the expenditure side, there are five broad divisions. Firstly, it is administration, which includes the cost, mainly for the staff of administrative officers and of general departments like accounts, stores, etc. Secondly, comes the repairs and maintenance, perhaps the largest. Thirdly, it is the operating expenses which include the cost of the operating fuel consumable stores, etc. The fourth division consists of items such as retirement benefits, medical aid health services, cost of certain minor works charged to revenue. The budget of each department and subjected to close the expert scrutiny by the built-in financial organisation in each railway administration. Such estimates are then submitted to the Railway Board Administration. Such estimates are then submitted to the Railway Board for final consolidation into the railway budget.

CONSOLIDATION BY THE MINISTRY OF FINANCE

Budget estimates prepared by the administrative ministries/ departments are scrutinized by the ministry of finance. The scrutiny exercised by the Ministry of Finance is different in character from the one applied by the Controlling Officers. The policy behind the prepared expenditure, its necessity or general propriety, etc., are the concern mainly of the administrative unit. The Ministry of Finance is concerned, primarily with the economy and is to keep the demands within the revenues availably for a particular period. Such scrutiny therefore, is:

1) The least in respect of items of expenditure that are charged upon the Consolidated Fund of India.

2) Is nominal and purely administrative in the case of standing charges which relate merely to permanent charges like salaries and allowances of permanent establishments and fixed contingent charges.

3) Is more exacting according to the importance, need and the urgency of the expenditures in respect of new items of expenditure which are either proposed for the first time or are being continued from year to year, but nevertheless are not standing charges. Besides, new items cannot be included in the estimates forwarded by the administrative ministries/departments without the prior sanction of the Ministry of Finance. Such items are separately and distinctly shown in the estimates.

Budgeting for the new schemes poses a different proposition. The new scheme has to be formulated in the administrative units or opera-agency in all its details. The same has to be approved by the ministry-in-charge. The items of expenditure are then examined by the Financial Adviser accredited to various demonstrative ministries/ departments. Estimates of capital expenditure are examined by the financial Adviser of the Ministry and further considered and screened by the Ministry of Finance in consultation with the Planning Commission. Finance examines it to find out whether details have been worked out or something is still left undone, and whether, the rules of common prudence have been observed. If these points are found to be in order, the scheme is declared acceptable. It has them to compete for the available funds along with other new schemes of all the other ministries/departments. If the scheme succeeds in this completion so, budget provision is made, that is to say, the necessary expenditure is included in the budget to be presented before the legislature.

Quite frequently it happens that at the time the budget estimates me prepared, the ministries/department may not be ready with details of the scheme, especially the schemes broadly included in the successive Five year Plans, but think that the scheme is essential to the ensuring year's budget Under such circumstances the ministry department concerned can ask for a lump provision in the budget, subject to details being worked out before execution.

The decision of the Ministry of Finance is final in the matter of determining the provision. Differences over the quantum of provision or the need for including an item of expenditure are resolved by discussion at Ministerial level. If they still persist, the matter is taken to the Cabinet. In case a settlement cannot be reached, then the arbitration is had either from the Prime Minister or the Cabinet.

The budget estimates of the parliament are submitted to the Ministry of Finance. The estimates are not criticized not rare comments made there on by the later.

After all these preliminaries are over the budget Division of the Ministry of Finance Consolidates the estimates received from various ministry/department of the estimated disbursements necessary during the next year on the existing basis that is to say without any new scheme being included.

ESTIMATES OF REVENUE

Estimates of revenue is also an important aspect of the procedure of budgeting. This is arrived at by the Ministry of Finance is consultation with the Central Board of Direct Taxes and the Central Board of Indirect Taxes and with the assistance of the Income Tax, and Central Excise and Customs Departments the most important revenue collecting agencies, A forecast is made of the expected revenue for the coming financial year at the existing rates of taxation. In order to match the revenues with the magnitude of the expenditure the Finance Ministry proposes alterations in the rates of existing taxation. The rates of taxes may be increased or decreased or new taxes may be levied, or old ones may be published.

Next, all the new schemes that have been approved in consultation with the finance in course of the year and which are now forwarded to the finance with a request for provision of funds, are also compiled by the later at this stage and the total expenditure involved, if all the new schemes were to be accepted for execution during the next financial year, is arrived at The ministries/ departments are requested to indicate the polarities of their different schemes of that if anyone has got to be excluded, it can be done on the basis of the said order or priority. Side by side with this are shown actual figures of the previous five years, the budget estimates approved at the commencement of me current year, and the revised estimates for the current year (i.e. the budget figures revised on the basis of actual of the past nine months and estimates for the seasoning three months) In addition to this the finance prepares an estimate of receipts from possible new sources of taxation and form possible increases in the existing rates. Possible proceeds of the borrowings during the ensuring financial year are also estimated.

The considered figures are now considered by the Cabinet who issue order there on.

Self-Check Exercise-2

Q.1 Budget estimates prepared by the administrative ministries/ departments are scrutinized by the ministry of finance. True/False

Q.2 The new scheme has to be formulated in the administrative units or opera-agency in all its details. True/False

7.4. SUMMARY

The Budget Division of the Ministry of Finance then makes the necessary charges in the estimates in accordance with the orders of the Cabinet, brings the revised estimates for the current year up-to-date and prepares two important documents: (a) Annual Financial Statement, (b) Demands for grants. These documents are then submitted to the legislature for consideration and approval.

7.5. GLOSSARY

- **Preparation :** The action or process of preparing or being prepared for we or consideration.
- **Estimate :** Roughly calculate or judge the value.
- **Rule of Lapse :** Lapsing of grant made earlier.

7.6. ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

7.7. REFERENCES/SUGGESTED READINGS

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7.8. TERMINAL QUESTIONS

(a) Write a note on the estimate of expenditure.

(b) Critically analyse about the need of consolidation by Ministry of Finance is budget making process.

ENACTMENT OF THE BUDGET

Structure

8.0. Introduction

8.1. Learning Objectives

8.2. General Discussion, Voting on Demands of the Budget

Self-Check Exercise-1

8.3. Cut Motions & Conditions of Admissibility of Cut Motions

Self-Check Exercise-2

8.4. Summary

8.5. Glossary

8.6 Answers to self-check exercises

8.7 References/Suggested Readings

8.8 Terminal Question

8.0 INTRODUCTION

In all parliamentary democracies, after the executive government prepares and approves the budget, it is presented to the legislature for discussion and approval. The responsibility of presenting the budget to the legislature lies with the executive government. Typically, a representative of the executive, often the Finance Minister, delivers the budget to the legislature. "Centralized executive responsibility for budget preparation and submission helps streamline the budget authorization process in the legislature and allows it to focus on reviewing programs and policies. The exclusive right to present the budget enables the executive to shape the effective implementation of policies. The legislature's review of the budget, as prepared and presented by the executive, provides a critical opportunity—arguably the most significant—for assessing the quality and nature of administrative actions. This scrutiny is a fundamental aspect of a parliamentary democracy, and every legislature has a responsibility to act as a watch-dog."

The budget then goes through the following stages before it is passed finally by the parliament:

1) presentation to the legislature;
2) general discussion :
3) discussion and voting of Demand for Grants.

4) consideration and passing of Appropriation Bill, and

5) consideration and passing of the Finance Bill.

8.1 LEARNING OBJECTIVES

After studying the lesson the learner will be able:

- To understand the enactment and execution process.
- To comprehend some aspect of Delegation of Financial powers.
- To know about the role of Financial Adviser.
- To discuss recommendations of Administrative Reforms Commission with regards to financial power.

8.2 GENERAL DISCUSSION AND VOTING ON BUDGET DEMANDS:

In India, the budget must receive the President's recommendation before being presented to the legislature, as required by the Indian Constitution. The President's approval is necessary for matters such as imposing, abolishing, altering, or regulating taxes, borrowing money, and withdrawing funds from the Consolidated Fund of India. Article 112 of the Constitution specifies the following:

1. The President must present the estimated receipts and expenditure for the Government of India for each financial year before both Houses of Parliament, known as the annual financial statement.
2. The expenditure estimates in the financial statement must clearly distinguish between: a) Expenditure charged upon the Consolidated Fund of India. b) Expenditure required for other purposes from the same fund.
3. The statement also distinguishes between revenue and other types of expenditure.

According to Rule 213 of the Rules of Procedure and Conduct of Business in Lok Sabha, the budget may be presented in multiple parts, and each part is handled as though it were the entire budget. This rule governs the presentation of the railway budget, which, although not specifically outlined in the Constitution, is presented separately from the general budget.

In India, the gap between the presentation of the budget and the start of the financial year is generally about five weeks, with the budget traditionally being presented on the last working day of February. If Parliament is not scheduled to meet on that day, a special session is convened at 5:00 PM for the budget presentation. After the President’s recommendation, the budget is first presented in the Lok Sabha by the Finance Minister, who delivers a speech introducing the budget. This speech includes:

a) A review of the country’s general economic conditions for the current year, covering the foreign exchange situation and related developments in monetary policy. The budget also serves as an instrument for shaping economic, political, and social policies, reflecting the government's progress toward these goals.

b) An explanation of discrepancies between the budget estimates at the start of the year and the revised estimates based on actual figures for the first ten months, along with projections for the remaining months.

c) Clarification on the budget estimates for the coming year and proposals for addressing any deficit, such as through new or increased taxes or other methods, or for handling any surplus.

The presentation of the budget is a significant event, often used to announce policies that affect the country’s economic and financial landscape. While the budget speech and accompanying statements provide substantial information, they may not offer enough detail for thorough examination or criticism by lawmakers. To address this, detailed books containing specific figures are also provided. After the Finance Minister's speech, a junior minister typically presents the budget documents and a copy of the Finance Minister's speech to the Rajya Sabha, completing the budget presentation in both Houses of Parliament.

The following documents are presented alongside the annual financial statement:

1. An explanatory memorandum detailing the nature of receipts and expenditures for the current and next year, and the reasons for any variations in the estimates.
2. A summary of demands for grants.
3. A book of demands showing provisions for each ministry and department under separate headings, detailing the estimates for each item. The Finance Ministry may consolidate grants for multiple ministries or create demands for expenditures that are not easily classified under specific ministries.
4. Demands for Grants related to the Post and Telegraphs Department.
5. Defence Services Estimates.
6. An Appropriation Bill.
7. A Finance Bill outlining the taxation measures proposed by the government.
8. A memorandum explaining the provisions of the Finance Bill and their impact on the country's finances. Government taxation proposals and changes in tariffs are generally announced with the budget or during its discussion. Changes in direct taxes can also be announced at other times during the year as necessary.
9. The Economic Survey.
10. The economic classification of the budget.
11. Annual reports of various ministries, presented alongside the demands for grants for each ministry.

Additionally, the Ministry of Railways presents a separate Railway Budget, typically in the first or second week of February. The Railway Minister introduces the budget, accompanied by an explanatory memorandum.

GENERAL DISCUSSION OF THE BUDGET

There is no discussion on the budget on the date it is presented to the parliament. On a day appointed by the Speaker, a general discussion on the budget as a whole takes place. "According to the practice in the Lok Sabha, the General Budget is ordinarily discussed after about a week or ten days of its presentation to House, while the Railway Budget is taken up for discussion alter about a week of its presentation." The budget is a whole or questions of fiscal policy relating are covered in this discussion and it helps the government to find out the general attitude of members to tin? Budget proposals. The Speaker's direction regarding budget discussion is, "that during (the general discussion on the budget, the House will be at liberty to discuss the budget as a whole or any question or principle involved therein. The scope of discussion at this stage is thus confined to the general examination of the budget i.e. the proper distribution of the items of expenditure according to the importance of a particular subject or service, the policy of taxation as it is expressed in the budget and in the speech of the Honourable Finance Minister.

"Members may, therefore, make observations in regard to the general scheme and the scientific of the budget. The general schemes of the budget. The general scheme of the budget will include consideration of revenue, surplus or deficit, revenue and expenditure account and the overall surplus or deficits. So for as the revenue account is concerned, members may take into account the method of estimation, whether revenue is over estimated or under-estimated whether the expenditure is pitched too high etc."

"As regards general grievances, they may be referred for ventilation at the time of considering the Finance Bill. That will also be; the proper occasion for going into details of taxation and matters related thereto. Similarly details of expenditure may be discussed when demands for grants come up before the House."

Article 113(1) of the Constitution allows discussion of expenditure, charged upon the Consolidated Fund of India. The Article provides. "So much of the estimates as relate to expenditure charged upon the Consolidated Fund of India shall not be submitted to the vote of Parliament, but nothing in this clause shall be construed as preventing the discussion in either House of Parliament on any of those estimates." The provision assures that no item is exempted from discussion in the legislature. Hence, though the article 'prohibits submission of such expenditure to the vote of the House and consequently the House cannot refuse or reduce the items of such expenditures either house gets an opportunity, each year to criticize the conduct or administration of the services which are so charged. Members are also free to ask for any information relating to these items. No motion however, can be moved at this stage and the budget too is not submitted to the vote of the House."

VOTING ON DEMANDS FOR GRANTS:

After the general discussion of the budget is completed, individual demands, or demands for grants, are presented for approval one at a time. Typically, a separate demand is made for each ministry or department. However, the Finance Ministry may combine grants for multiple ministries or create a single demand for expenditures that do not fit neatly into specific departments. The total demand consists of a statement detailing the total grant requested, followed by a breakdown of the detailed estimates for each grant, divided into various categories.

Each ministry is assigned a specific date for the discussion of its respective demands. These discussions and the subsequent voting usually take up about three weeks. According to the established rules, the debate on any particular demand is limited to two days. On the final day of the scheduled discussion, any demands that have not been discussed or approved are put to a vote without further debate, a process known as "guillotining." The motion typically reads: "That a sum not exceeding Rs. ____ is granted to the President to cover the charges for the financial year ending 31st March, 20__ with regard to [the subject of the demand]." If a demand is not fully debated on the day it is introduced, it will be guillotined on the second day.

Along with the presentation of the demands, an annual report from the relevant ministry is submitted to the House. These reports outline the ministry's performance for the past year, its major achievements, and its plans and proposals for the upcoming year, justifying any additional funds requested in the demand for grants. These reports, which started being submitted in 1951, serve as a substitute for the minister's speech when moving a demand and are part of the discussion when the demand for grants is being considered. A similar process applies to the Railway Budget, which is presented separately in Parliament.

In the Upper House, there is only a general discussion on the budget, and it does not vote on individual demands. Instead, the discussion is held collectively. During the budget discussion, members are allowed to propose adjustments to duties or the introduction of new taxes. The government's proposed tax measures are implemented through the introduction of the Finance Bill. During the consideration of this Bill, members can discuss the government's monetary and financial policies. Amendments to the Bill, including changes to tax rates, can be proposed. However, amendments that seek to raise tax limits require the President's recommendation before they can be introduced.

It is important to note that no demand for grants can be made without the President's recommendation. This ensures that all demands for grants originate from the executive government, not from individual members of the legislature. While the legislature can reduce or deny a requested grant, it cannot increase the amount. If the legislature believes that the expenditure on a particular item should be higher, it can only recommend such an increase, which the executive government may or may not accept. This practice aligns with the constitutional norms observed in the British House of Commons. In this system, expenditures from the Consolidated Fund of India can only be incurred if both the legislature (specifically the Lower House) and the executive government agree.

Self-Check Exercise-1

Q.1 No demand for a grant can be made except on the recommendation of the President. True/False

Q.2 Any member may make suggestions during the discussion of the budget for enhancement of duties and the imposition of new taxes. True/False

8.3 Cut Motions and Conditions for Admissibility

The legislature has the authority to propose reductions in grants. Members may introduce a motion to reduce the expenditure on any specific demand for grants presented for approval. This type of motion is known as a "cut motion." There are three primary types of cut motions: (a) reduction of expenditure, typically when the mover believes the proposed expenditure is excessive, (b) cuts aimed at promoting economy, and (c) motions to highlight a specific grievance related to a demand for grant.

The rules of procedure in Indian legislatures define specific categories of cut motions. These include Policy Cuts (or Policy Cut Motions), Economy Cuts (or Economy Cut Motions), and Token Cuts (or Token Cut Motions). Any cut motion introduced by a member must fit one of these categories.

Disapproval of Policy Cut:

A cut motion aiming to disapprove the policy behind a demand reduces the demand to a nominal amount. This is referred to as a "disapproval of policy cut." A typical motion might state: "That the amount of the demand be reduced to Rs. 1." If this motion is approved by a majority, it acts as a vote of censure against the government. Members proposing such a motion are usually required to clearly specify the policy aspects they wish to challenge. The discussion is then focused on the specified policy, and members are allowed to propose alternative policy measures.

Economy Cut:

An economy cut is proposed when members believe that savings can be made from the expenditure being requested. This motion seeks to reduce the demand by a specific amount to reflect these savings. The motion typically reads: "That the amount of the demand be reduced by Rs. [specific amount]." The reduction may be either a lump sum or a specific reduction, and the discussion is centered on how the economy can be achieved.

Token Cut:

A token cut is used to highlight a specific grievance within the scope of the government's responsibility. In this case, the demand is reduced by a nominal amount, usually Rs. 100, to draw attention to the issue. The motion typically states: "That the demand under [the relevant head] be reduced by Rs. 100." The objective is to bring focused attention to a particular grievance, which must be clearly stated so the government can respond. Discussions on token cuts are limited to the grievance mentioned in the motion.

Although cut motions are typically introduced by members of the opposition, there is no formal rule or parliamentary practice (apart from party whips) preventing government supporters from proposing them.

Each cut motion specifies the precise points for discussion. For instance, a policy cut motion allows members to propose an alternative policy, an economy cut focuses on how savings can be made, and a token cut is confined to discussing the grievance raised. Generally, token cuts are the most common, with numerous motions proposed to address specific grievances. Each amendment or cut motion is subjected to a vote.

CONDITIONS FOR ADMISSIBILITY OF CUT MOTIONS

For a motion proposing a reduction in the demand amount to be accepted, it must meet the following conditions:

1. The motion must relate to a single demand.
2. It must be clearly worded, avoiding arguments, inferences, sarcasm, accusations, insults, or defamatory language.
3. It should focus on one specific issue and be stated clearly and precisely.
4. It must not address the character or conduct of any individual, as these can only be challenged through a substantive motion.
5. It should not propose changes to existing laws.
6. It must not involve matters that are outside the scope of the Government of India’s responsibilities.
7. It should not relate to expenditures charged to the Consolidated Fund of India.
8. It must not address a matter that is being adjudicated by a court with jurisdiction in any part of India.
9. It cannot raise a question of privilege.

10. It should not revisit a topic that has already been discussed and decided upon in the same session.
11. It must not anticipate a matter that has already been scheduled for consideration during the session.
12. It should not raise issues currently under review by any statutory tribunal, authority, commission, or court of inquiry.
13. It should not concern trivial matters.

Consideration and Passage of the Appropriation Bill

No funds can be withdrawn from the Consolidated Fund of India without a law that authorizes the appropriation. Voting on the expenditure estimates and the demands for grants alone does not give the government the authority to incur expenditure. To regularize this process, an Appropriation Bill must be introduced, debated, and passed by the legislature. The Appropriation Bill acts as formal legislation that authorizes the grants already approved by the legislature and covers expenditures charged on the Consolidated Fund of India by the Constitution.

The scope of the debate on the Appropriation Bill is limited to matters of public significance or administrative policy reflected in the grants covered by the Bill, which have not already been discussed during the initial debate on the demands for grants. Repetition of debates on points already discussed in the demands for grants is not allowed. Only relevant matters can be addressed in the discussion, and the Speaker may require members to notify the specific points they wish to raise beforehand. The Speaker can withhold permission for points deemed irrelevant or repetitive.

When a member raises an issue with the Speaker's approval, the relevant Minister must be present to address those points.

Article 114(2) of the Constitution prohibits amendments to the Appropriation Bill that would alter the amount or destination of any grant or modify any expenditure charged on the Consolidated Fund of India. The presiding officer's decision on whether an amendment is permissible is final. This ensures that the grants already approved by the House are not changed at this stage, although the debate provides an opportunity for members to offer suggestions and comments on the government's activities concerning the authorized expenditures.

According to the Constitution, an Appropriation Bill is also required for the Vote on Account, which must be considered and passed by Parliament before the start of the financial year. The Appropriation Bill introduced after the voting on the grants applies only to the remaining sums.

Once the Appropriation Bill is passed by the Lower House, it is reviewed and passed by the Upper House without any modifications. Only after receiving approval from both

Houses and the President's assent does the Appropriation Bill become law, allowing money to be withdrawn from the Consolidated Fund of India.

Consideration and Passage of the Finance Bill

The Finance Bill is a legislative proposal typically introduced annually to implement the Government of India’s financial plans for the upcoming fiscal year. It may also be used to address supplementary financial measures for any given period. However, the Finance Bill does not include provisions aimed at making permanent changes to existing laws unless they are directly related to or a result of the taxation proposals. Once the expenditures are voted on by the House, the next step is to consider how to generate the necessary revenue to meet those expenses. This involves reviewing the income side of the budget, which is addressed through the passage of the Finance Bill.

The Finance Bill includes provisions related to the imposition, modification, or regulation of taxes and must be passed by Parliament before any of the proposals can be enforced. In India, these proposals are typically presented alongside the budget. The Bill may cover: (a) new taxes to be introduced, (b) increases in existing taxes, and (c) taxes that require annual renewal or revision. After being discussed and reviewed, the necessary laws are enacted to enable the government to implement these proposals.

Considerable latitude is allowed during the debate on the Finance Bill, allowing for a broader discussion on the government's financial policy and general administration. This is different from the Appropriation Bill, which typically involves two stages of debate—general discussion and the debate on the demands—before the bill is passed with little further discussion. In contrast, the Finance Bill is debated for the first time, giving members an opportunity to thoroughly examine the taxation proposals. The debate on the Finance Bill covers several key points:

1. Members are allowed to discuss actions of the Government of India.
2. Criticism of state government actions is not within the scope of this debate.
3. General critiques of government policy are permitted.
4. Detailed discussions of specific estimates are not allowed, but members can address public policy issues that may contribute to a deficit.
5. While the general principles behind the budget can be debated, specific details of these principles are not open for discussion.
6. The entire administration may be reviewed, but topics already discussed in prior debates cannot be revisited.
7. Discussions on individual clauses and amendments to the Finance Bill are restricted to the proposed taxation measures and potential alternatives.

Under the Provisional Collection of Taxes Act of 1931, the Finance Bill must be passed by Parliament and receive presidential assent no later than 75 days after its introduction.

Self-Check Exercise-2

Q.1 A Finance Bill deals with imposition, remission or regulation of taxes. True/False

Q.2 Cut motions should not be confined to only one specific matter which shall be stated in precise terms. True/False

8.4. SUMMARY

Principally the accounting responsibilities should be decentralized and should come to/be vested with the executive government instead of the Comptroller and Auditor General of India. This involves, however, intricate and complicated problems to be sorted out at various levels before some final decision is taken. Until such time, the system of 'internal finance' would positively help devising techniques as are best suited to keep a watch over the progress of expenditure. Such techniques should aim at the formulation of realistic and valid budget estimates; realistic projections of forward expenditure; keeping expenditure within the limits of appropriation, and keeping expenditure up to the level to reach Plan objectives.

The scheme has, without doubt, gone a long way towards efficient execution of the budget. This is what was required in the context of increasing development activity undertaken in the public sector involving investments of hundreds of crores of rupees years by year. The system of internal finance still, however, leaves a considerable scope for further improvements. The Public Accounts Committee, in its Report on the Finance Accounts of the Central Government (1961-62), remarked that large savings continued to occur despite the delegation some years ago of financial powers to administrative ministries.' The committee recommended that the Ministry of Finance should examine the feasibility of making more effective the financial control exercised through the financial advisers attached to the various Ministries. The Committee also stressed the need for curbing the tendency of administrative Ministries to overlook avoidable expenditure in the delegated set-up.

8.5. GLOSSARY

- **Delegation :** A body of delegates or representatives, a deputation.
- **Execution :** The carrying out of a plan, order or course of action.
- **Cut Motion :** It is a power given to the members of the Lok Sabha to oppose a demand in the financial bill discussed by the government.

8.6. Answers to self-check exercises

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 False

8.7. REFERENCES/SUGGESTED READINGS

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8.8. TERMINAL QUESTIONS

(a) Write a note on consideration and Passing of The Finance Bill.

(b) Describe the execution process of budget on the revenue side.

CHAPTER-9

Structure

9.0 Introduction

9.1 Learning Objectives

9.2 The execution of the Budget

Self-Check Exercise-1

9.3 Financial Adviser & Recommendations of the Administrative Reforms Commission

Self-Check Exercise-2

9.4 Summary

9.5 Glossary

9.6 Answers to Self-Check Exercises

9.7 References/Suggested Readings

9.8 Terminal Question

9.0. INTRODUCTION

The execution of the budget is the responsibility of the executive government, and therefore, the distribution of power within, the executive government determines the procedure for the execution of the budget; it is an axiom of financial control that for every grant there must be an authority responsible for its administration and particularly to see that the amounts are spent on the subjects as sanctioned, moneys are utilized in the most economical manner and the expenditure is kept within the funds allotted for the purpose. An efficient execution of the budget presupposes, therefore, strong control direction and control. If this is not done the budget will fall in a, large measure to accomplish its purpose, which is to produce stability in government's finance by making both ends meet. In order to make the execution of the budget an ideal one, the system must aim, at the following objectives: (a) preservation of the intent of the legislature; (b) observance of financial limitations and (c) the maintenance of flexibility.

9.1. LEARNING OBJECTIVES

After studying the lesson the learner will be able:

- To understand the execution of budget process.
- To know about the role of Financial Adviser & his role.

- To discuss recommendations of Administrative Reforms Commission with regards to financial power.

9.2. EXECUTION OF THE BUDGET

As regards the preservation of the intent of the legislature, it must be kept in mind that the budget to be executed is the budget sanctioned by the legislature. The expenditure to be incurred and the revenues to be raised must be put into practice in the spirit and intent the legislature had while sanctioning such authorizations. It is only in this way that the sovereignty of the electorate and authority of the legislature can duly be safeguarded.

So far as the observance of financial limitations is concerned, the use of the resources must be with utmost economy and efficiency, and the financial sanctions expressed by the legislature must be adhered to. A proper execution of the budget, as a matter of fact means execution of financial control in the sense that not only the expenditures are available for such disbursement in time. There must therefore, be in efficient planning of the ways and means position on the part or the executive government.

Coming to the maintenance of flexibility, it must be borne in mind that during the course of the financial year, changes in economic conditions from those assumed at the time of preparation of budget may come about leading to cost fluctuations in the programmes. The execution of the budget must, therefore, be able to cope with such unexpected eventualities.

EXECUTION OF THE BUDGET ON THE EXPENDITURE SIDE

In India, the Ministry of Finance oversees the overall execution of the government's budget. This Ministry plays a vital role in implementing financial policies and supervising the finances of administrative authorities. The Ministry monitors public spending through three primary stages: (a) approval of policy frameworks, (b) acceptance of budget estimates, and (c) granting prior approval for incurring expenditures, while also managing any delegated powers to administrative Ministries or Departments. The Ministry's control is especially focused on the first and third stages, which significantly impact the daily functioning of administrative Ministries. However, excessive rigidity or detailed scrutiny at these stages may slow progress and delay the execution of projects, particularly in areas like development, commerce, or industry. This can result in a loss of national productivity or income. While control and oversight are essential, they should be constructive, efficient, and forward-thinking, avoiding unnecessary restrictions.

Once the budget receives legislative approval and the Appropriation Act and Finance Act are passed, the budget becomes operational. The funds authorized by the legislature for the financial year are allocated to the executive government for specific purposes. At this point, the primary task is to ensure compliance with the approved budget. The government's framework for fulfilling this responsibility involves several key components: (1) a system of controlling officers, (2) authorities who approve financial sanctions, (3) drawing and disbursing officers, and (4) a payment and accounting system.

Typically, each Minister or Department acts as the controlling officer for the portion of the budget within their jurisdiction. Following the passage of the budget and the enactment of the Appropriation Act, the Ministry of Finance notifies each administrative Ministry/Department about the specific section of the budget relevant to them. The allocated funds are then placed at the disposal of the designated controlling officers, who are responsible for monitoring and ensuring that the funds are spent according to the approved purposes, without exceeding the allocated amount unless additional funding is legally sanctioned. The controlling officers further guide the disbursing officers by providing them with budgetary limits, ensuring that spending stays within the specified boundaries. It is the duty of the controlling officers to ensure that the execution of the budget follows the plan as approved by the legislature.

EXECUTION OF THE BUDGET ON THE REVENUE SIDE

The execution of the revenue side of the budget involves three key aspects: (1) efficient collection of revenue, (2) secure management of collected funds, and (3) appropriate allocation of those funds.

The executive government is responsible for proposing taxes, which are then authorized by the legislature. Once this approval is in place, it falls on the government to establish an effective system for administering the taxes, including rules and procedures to ensure smooth and cost-effective operation. In India, the Ministry of Finance's Department of Revenue oversees the overall management and supervision of tax collection, which includes both direct and indirect taxes. This supervision is carried out through two main bodies: the Central Board of Direct Taxes and the Central Board of Excises and Customs. These boards oversee various administrative authorities, ensuring that they properly enforce tax laws and regulations. The funds collected are then handled and distributed by the Treasuries and Sub-Treasuries.

SOME ASPECTS OF DELEGATION OF FINANCIAL POWERS

Till recently, opinion was held that there was an excessive concentration of financial authority in the Ministry of Finance and there was no delegation of this authority even to the high-ranking and-responsible officers in the other administrative Ministries/Departments type of right financial control obviously resulting dilatory and inefficient execution of the budget, especially so when under the impact of planned charged with the execution of large scale investment programmes in the public sector "Sir Richard Tottenham in his report to the Government in 1945-46 emphasized that the need of the time was to develop a sense of financial responsibility in the spending departments and, for this purpose, to provide them with the assistance of their own financial adviser at distinct from the Finance Ministry's officials. He attached special importance to the strengthening of the financial set up within the spending departments. Shri Gopalaswamy Ayyangar, in his report on the Reorganisation of the Machinery of Government (1949) referred to the delays and deficiencies of the existing system of financial advice and observed: that the system requires to be improved so as to increase the responsibilities of the individual ministries and remove the sense of frustration among them:

Sh. Ashok Chanda a former Comptroller and Auditor General of India observed. "The present conception of control extends also to the examination of technical details, through the Finance Department is not properly equipped for the purpose. As a result, the objections raised are often elementary and uniformed in charterer. This not only acts as an irritant, but it is also time-consuming. Ultimately these objections' mostly come to be waived, but often only after interminable discussions, and control becomes affective only over establishment proposals, the expenditure on which forms but an insignificant fraction of the total cost. The Financial Ministry therefore, whilst straining at the grant has often to swallow the camel." Shri A.D. Gorwala suggested, "What is really needed in financial matters is control and not interference in small matters leading to a great deal of waste of time and energy and frustration on the part of, the administrative departments that is the greater part of the Government. This must be avoided."

In this connection, the Estimates committee, in its 9th Report on 'Financial Administrative, and Other Reforms' emphasized the need for coordination between the Ministry of Finance and the administrative Ministries/Departments and recommended delegation of more financial powers to the later. The Committee observed that "concentrated steps should be taken to achieve the end in view and to establish perfect cordiality between the administrative Ministries and the Ministry of Finance and to see that one is complementary to the other and helps in the ultimate objective. Following recommendations were made by the committee."

> Before a scheme is embarked upon, it should be properly planned and it, should also be ascertained whether the money required for it is available or can be made at the proper time.
>
> Detailed plans and estimates should be worked out fully so as to enable the Ministry of Finance to approve the scheme and accord financial concurrence.

After the scheme is concurred from the financial point of view of the Ministry of Finance, the detailed execution of the Scheme and spending the money there on should be the responsibility of administrative Ministry, which should also be given power to vary or to alter the amounts under the sub-heads of the scheme so long as the total outlay is not affected.

The general opinion developed, therefore, that the administrative efficiency and efficient execution 'of the budget demand that the administrative Ministries/Departments should possesses sufficient financial powers once their demands for grants are sanctioned by the legislature. The Ministry of Finance could exercise, however, overall control only.

As regards the delegation of powers, the order of the executive government of August 1958, were followed up by the promulgation, in December 1958, of the Delegation of powers Rules, 1958. These rules were subject to some general limitations, conferred wide powers upon the administrative Ministries, Administrators and Head of Departments. The salient features of the conferment of such powers are as follows;

(1) Full posers had been granted to the administrative Ministries/ Departments for appropriations and re-appropriations subject to expenditure being within the scope of the grant with certain provisions for prior consultation with the Ministry of Finance.

(2) After the scheme is concurred in form the financial point of view by the Ministry of Finance, the detailed execution of the scheme and spending the money there on should be the responsibility of administrative Ministry, which should also be given power to vary or to alter the amounts under the sub heads of the scheme so long as the total outlay is not affected.

The general opinion developed, therefore, that the administrative efficiency and efficient execution of the budget demand that the administrative Ministries/ Departments should posses sufficient financial powers once their demands for grants are sanctioned by the legislature The Ministry of Finance could exercise, however, overall control only.

In view of the pressing need for better financial coordination between the Ministry of Finance and the Administrative Ministries, the Government of India examined the details of the delegation of more financial powers to the administrative Ministries/Departments early in 1955. The Organisation and Methods Division of the Cabinet Secretariat issued a brochure in 1957 entitled "Financial and Cognate Powers delegated to Ministries and Heads of Departments," in which the financial powers delegated as such were embodied. Proceeding further, the President made a reference in this regard in his address to the Parliament on February 9, 1959 in the following words : "My Government have recently made some important changes in regard to arrangement for budgeting and financial control over expenditure from the Civil estimates in order to secure a speedier implementation of our development plans, the Administrative ministries have been given wider financial powers to issue expenditure sanctions to schemes which have been included in the budget estimates after scrutiny by the Finance Ministry.

Self-Check Exercise-1

Q.1 Execution of the budget on the revenue side involves three considerations; (1) proper collection of revenues; (2) proper custody of the collected funds; and (3) proper distribution of funds. True/False

Q.2 In India, the Ministry of Finance of the Government of India exercises an overall control over the execution 'of the budget. True/False

9.3. THE ROLE OF THE FINANCIAL ADVISER

Before explaining the role of the Financial Adviser, a distinction may be drawn between; (1) the External Financial Adviser, whose main function is to exercise some of the powers of the Finance Ministry and advise on its behalf; and (2) the Internal Financial Adviser, whose main function is to assist in the exercise of powers delegated to the administrative Ministry.

The aforesaid distinction may further be amplified as follows:

The External Financial Adviser is responsible to the Ministry of Finance. While discharging various functions on behalf of the Ministry of Finance, however, there is nothing to prevent him being asked to advise-6n the delegated financial roles of External and Internal Financial Adviser'.

1. An Internal Financial Adviser strictly so called (i.e., one who does not exercise any powers whatever on behalf of the Ministry of Finance) confines himself to not only the financial matters finally disposed of by the' administrative Ministry but also with those which being outside the delegated powers necessitate a reference to the Ministry of Finance. This, however, is not a combination of roles as in (1) above.
2. Another distinguishing feature of the Internal Financial Adviser's advice is that it is susceptible to being overruled within the Ministry itself. The level at which it may be overruled and the condition,, if any, on which it is overruled are points of relative details, through important in, themselves.

Summarizing the latest position, certain financial powers are delegated to the administrative Ministries. In the exercise of such powers it is open to the Administrative Ministry : (1) whether or not to make purely internals arrangements for financial advice; (b) in the event of making such arrangements, whether or not they should conform of appointing an Internal Financial Adviser, strictly so called; and (c) in the event of not appointing an internal Financial Adviser, whether or not to refer one or more categories or cases, within the delegated sphere, for advice, to Finance Minister, it being understood that such advice is not binding on the administrative Ministry.

The role and functions of the Financial Adviser, who under the-new scheme, is to be internal and not 'external to the administrative Ministry as before assume great importance. "It should be obligatory in our view, for each Department or Ministry to have a whole-time' Internal Financial Adviser of adequate seniority and rank it should not be left to the discretion of the Individual Department or Ministry to decide whether it should have an Internal Financial Adviser. The internal Financial Adviser should be placed in charge of Financial management and controlling all matter within the Ministry's field of responsibility and for maintaining requisite liaison with the Finance Ministry."

The Administrative Reforms Commission states further that "the Internal Financial Adviser should be responsible to and under the administrative control of the Secretary of the Ministry. The Finance ministry should, however, be required to concur in the appointment of this officer and should have overall and coordinating interest in the development careers of Financial Advisers. The annual assessment of his work should be made by the Secretary of the Expenditure Department, who should obtain the views and comments of the administrative Ministry under whom the 'Financial adviser may, for the time-being, be working. While it will be open to the secretary of the administrative ministry to overrule him without being required to report the fact to any other authority, the relationship between him and the administrative Secretary should, as envisaged by the study team in Financial Administration, be that of senior partners in a common enterprise.

In terms, of the existing rules, the administrative Ministry, in respect of the delegated financial powers, can lay down, in its discretion, the procedure for consultation with the Financial Adviser, "In view of the increased delegation to the administrative ministries and of the dimensions of expenditure controlled by one ministries, it is necessary that a set of model rules should be framed for the guidance of administrative ministries in these matters."

RECOMMENDATIONS OF THE ADMINISTRATIVE REFORMS COMMISSION

The Chief recommendations of the Administrative Reform Commission are reproduced below:

1. It should be obligatory for each Ministry to have a whole-time Internal Financial-Adviser of adequate seniority and rank. This officer should be placed in charge of the Finance and Budget Cell of the Ministry and should be responsible for the financial management and control within the Ministry's field of responsibility. He should not be entrusted with any other work of the administrative Ministry like personal work or office management, etc. It should be open to the entrusted the officer with the work relation to more than one Ministry Department.
2. The procedure for constitution with the Financial Advisor and the type of cases in which he would be consulted should not be left to the discretion of individual Ministry. A set of model rules should be framed for the guidance of administrative Ministries in this matter.
3. The Finance and Accounts Branches of the Administrative Ministries should be suitably strengthened where necessary staffed with qualified and well trained personal.

4. The Finance Ministry should help the administrative Ministries to organise well-equipped internal Finance Branches. For this purpose, it will be necessary to (i) ensure proper-training of the junior officers, and (ii) provide for officers in the middle levels suitable' opportunities to acquire varied experience and knowledge of public administrations.

5. The Financial Adviser should bring to his assignment of background of field experience-and at an appropriate state he should be given such orientation as to equip him for this role and functions of Financial Adviser. The officers without a similar background should be provided this experience as 'early as possible in their careers as Financial Adviser.

6. There should be a provision for periodical interchange between the officers of the Finance Branches and other branches of Administration.

7. If a feasibility report has been accepted by Govt. and the detailed scrutiny thereof is likely to take considerable time the administrative Ministry should be allowed to incur expenditure on preliminary work subject to specified financial limit.

8. A definite time limit, say three months should be prescribed for the consideration of schemes by the Finance Ministry. If the decision of that Ministry is not reached within the prescribed period the case should automatically be put up to the Finance Minister who will decide upon the action to be taken and will communicate the decision to the administrative Minister concerned.

9. Proposals of the administrative Ministries for additional staff or creation of new posts should be considered by an independent agency namely, well- equipped and well-trained Staff inspection Unit.

10. In cases of sudden unforeseen increase in work due to. extraordinary circumstance, the Miniseries and Departments should have power to create", only for very short periods not exceeding three months temporary posts if funds can be found by re-appropriation within the existing budget provision Such powers may be made available to Heads of Departments also.

The system of Internal finance under the control of the Secretary of the administrative Ministry/Department is a recent development, and has been introduced on a model as in the United Kingdom. It has to be recognised that the Secretary of the administrative Ministry/Department is primarily responsible for the efficient and economic functioning of the Ministry/Department under his charge and, therefore he should have sufficient financial authority for the due discharge of that responsibility. The system now assures that there should- not be any difficulty on the administrative side of the Ministry/ Department which may arise in the formulation, and proper execution of the schemes and projects.

Self-Check Exercise-2

Q.1 The Finance bill is passed before Appropriation bill. True/Fasle

Q.2 The External Financial Adviser is responsible to the Ministry of Finance. True/False

9.4. SUMMARY

Principally the accounting responsibilities should be decentralized and should come to/be vested with the executive government instead of the Comptroller and Auditor General of India. This involves, however, intricate and complicated problems to be sorted out at various levels before some final decision is taken. Until such time, the system of 'internal finance' would positively help devising techniques as are best suited to keep a watch over the progress of expenditure. Such techniques should aim at the formulation of realistic and valid budget estimates; realistic projections of forward expenditure; keeping expenditure within the limits of appropriation, and keeping expenditure up to the level to reach Plan objectives.

The scheme has, without doubt, gone a long way towards efficient execution of the budget. This is what was required in the context of increasing development activity undertaken in the public sector involving investments of hundreds of crores of rupees years by year. The system of internal finance still, however, leaves a considerable scope for further improvements. The Public Accounts Committee, in its Report on the Finance Accounts of the Central Government (1961-62), remarked that large savings continued to occur despite the delegation some years ago of financial powers to administrative ministries.' The committee recommended that the Ministry of Finance should examine the feasibility of making more effective the financial control exercised through the financial advisers attached to the various Ministries. The Committee also stressed the need for curbing the tendency of administrative Ministries to overlook avoidable expenditure in the delegated set-up.

9.5. GLOSSARY

- **Delegation :** A body of delegates or representatives, a deputation.
- **Execution :** The carrying out of a plan, order or course of action.
- **Cut Motion :** It is a power given to the members of the Lok Sabha to oppose a demand in the financial bill discussed by the government.

9.6 Answers to Self-Check Exercises

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 False

Q.2 True

9.7. REFERENCES/SUGGESTED READINGS

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- IGNOU New Delhi, egyankosh

9.8. TERMINAL QUESTIONS

(a) Write a note on consideration and Passing of The Finance Bill.

(b) Describe the execution process of budget on the revenue side.

Chapter-10

BUDGET AS AN INSTRUMENT FOR ECONOMIC DEVELOPMENT AND MANAGEMENT

Structure

10.0. Introduction Learning Objectives

10.1. Learning Objectives

10.2. Budget-As an instrument of Management and Economic Development

Self-Check Exercise-1

10.3. Summary

10.4. Glossary

10.5 Answers to Self-Check Exercises

10.6. References/Suggested Readings

10.7. Terminal Questions

10.0. INTRODUCTION

The word budget is derived from the French word "Baguette" which means a small leather bag. It was first used in England to describe the white leather bag that holds the seal of the medieval court of the exchequer. Later on chancellor of the Exchequer's bag containing his proposals for Financing Government expenditure became known his budget.. This term was used in 1773. Gradually the word Budget' came to be used for the proposals themselves carried to parliament for approval This word has now become current in all countries and has been incorporated in many languages. Thus the word Budget' is commonly understood as a document presented by a Government, containing an estimate of proposed expenditure of a given period and proposed means of financing them, for the approval of the legislature. The budget is future oriented in that it, expresses anticipated action as distinguished from an accounting balance sheet that indicates actual revenues and expenditure.

10.1. LEARNING OBJECTIVES

After studying the lesson, the learner will be able:

- To understand about the budget as on instruments of Management and Economic Development.

10.2. Budget-As an instrument of Management and Economic Development

Public budgeting provides an effective 'means of organising management information to make correct decisions concerning, the allocation of limited fiscal resources. A budget may be defined as,' "A comprehensive plan, expressed in financial terms, by which ah operating programme is effective for. a given period of time. It includes estimates of, the services, activities and projects comprising the programmes, the resultant expenditure requirements and the resources enable for their support."

The budget is much more than a financial document, it represents a process by which (i) public policy is made, (ii) public programmes are put into effect, (iii) both the legislative and the administrative controls are established.

The budget has primarily three functions to perform: control, management and planning. Control in budgeting is the process of enforcing the limitations and conditions set in the budget in appropriations, securing compliance with the spending restrictions ensure the efficient use of staff and other resources in the conduct of authorised activities. Planning refers to the process of determining public objectives and the evaluation of alternative programmes.

Historically, the fiscal objects of budgeting have received the greatest emphasis. The rapid growth of government activities and expenditures, made it exceedingly difficult to cope with the governmental task with the traditional type of budgeting. In 1949, the Hoover Commission, called for modification in budget classification, so as to be in accordance with management orientation. The term performance budgeting was first used by the commission. A performance budget is a budget based on functions, activities and projects.

Performance budgeting has strong management orientation. Its principle objective is to assist administrators in their assessment of the work efficiency of operation units. It seeks this objective by (1) casting budget categories in functional terms, and (ii) providing work cost-measurement to facilitate the most effcierst performance of prescribed activities.

The common components of performance budgeting system are: (1) activity classification, (ii) performance measurements, (iii) performance reports. Performance budgeting places considerable emphasis on redesigning expenditure, accounts and grouping expenses into functional and activities categories.

The budget innovations in the budget process that has received the greatest attention in the recent years is the Planning Programming and Budgeting System.

Planning:

Planning is the determination and the review of objectives the development of alternative and subsequent analysis.

Programming :

Programming is the organisation of related activities by main obj ectives and their representation in the form of programme and financial plan, and looking ahead for a number of years into the future. It also included further detailed analysis of alternatives within the contest of major policy decisions and regular' review of programmes as a whole.

Budgeting :

Budgeting is the translation of the first year a programme and financial plan, to a more detailed and precise annual budget, which sets targets for performance, fixes limits for spending and forecast income.

System:

System is the emphasis upon coordinating planning, programming and budgeting with one all embracing, approach or system. The production of information, whether for analysis or for progress reporting should be viewed in terms of the system as a whole. This is a very important component in PPBS.

Under PPBS, a conscious effort is made, (1) to state the objectives, (ii) to seek a weak range of alternatives, and (iii) to link programmes and financial plans.

There are Five Major Components of PPBS :

1. The first involve an identification of major public goals and objectives, in programme terms.
2. The second involves the structuring and analysis of public programmes' across the board, i.e. without concern initially for the variety of agencies that might be involved in the process of implementation.
3. The third involves an extended time horizon and multi-year-programme and financial plans.
4. The Fourth Component, programme analysis is the comer stone of PPBS.

The final component involves programme updating procedure.

BUDGET

The volume of government activity and consequently the magnitude, of government budget all-over the world have grown considerably since the beginning of the century. The expansions of budget is partly due to the financial consequences of two world-wars; but its principle cause lies in the radical changes of ideas regarding the role of State and its responsibility for the creation of sound economic social and technical development society. This has resulted in government budgeting undergoing a complete change. It has now acquired some economic significance. Budget has become instruments for searching new grounds and evolving a new economic thinking. New economic theories have come 'on the scene and they say that budgets can be very well utilized for planning long range economic development. It also points out to modem budgets of a country, which is under developed and trying to march on the rough and torturous road of economic development, have become, real means of guiding the country.

In almost all the countries, the government has come to assume increasingly important role in determining the level of economic activity in the modem times, it is enlisted with the responsibilities of conducting development programmes and maintaining full employment of the available men and material resources in order to contribute to current and future levels of the country's productive capacity. It is also expected to enhance pace of capital formation in the country through special attention to long term Investment projects which do not attract private capital. The presentation of its programme and more specifically its budgets, therefore, assume special importance, because comprehensive economic policy is impossible without a proper system of financial planning' and reporting at all levels of government.

Hence a budget is not merely a financial estimate of revenue and expenditures of the government, it is something more. The whole policy of the government is reflected in the budget. Through government budgets, great improvements can be in the economic conditions of the people. The great power of today achieve higher economic status only with the help of budgets through which their policies were implemented and the process of economic development was initiated, and it is due to their economic power that they have great political power. Great programmes of economic development have been undertaken in the European countries and the United States with the help of budgetary techniques A.E. Buck has cited the case of Japan, rapidly developed country, which (introduced as early as in 1889 a budget system as a mean of rationaling and controlling government activities. In that country, government budgeting appears to have led and not aged in the process of economic development.

Self-Check Exercise-1

Q.1 In PPBS, the structuring and analysis of public programmes'across the board, i.e. without concern initially for the variety of agencies that might be involved in the process of implementation. True/False

Q.2 The budget is much more than a financial document, it represents a process by which (i) public policy is made, (ii) public programmes are put into effect, (iii) both the legislative and the administrative controls are established. True/False

10.3. SUMMARY

Government budgeting is an important tool initiated for making economic development in a country. The modem government which is regarded a welfare state, especially in the under-developed countries, has to shoulder greater responsibilities for providing a better living standard to the people. In order better the standard of living implementing programmes for development. In this task, budgeting arid budget process are major instruments. In the countries, when a system of mixed economy has been followed, a major part of government budget is devoted to the activities of the public sector; while the private sector is also helped by making provisions. In the budget for loans, grants and subsidies to be given to the units of the private sector.

Thus in the conclusion we can say that the budget is an important instrument for the economic development of a country.

10.4. GLOSSARY

Management: the process of dealing with or controlling things or people.

Economic Development : is a process by which the economic well being and quality of life of a nation region or local community are improved.

10.5. ANSWERS TO SELF-CHECK EXERCISES

SELF-CHECK EXERCISE-1

Q.1 True

Q.2 True

10.6. REFERENCES/SUGGESTED READINGS

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10.7. TERMINAL QUESTIONS

(a) Do you think budget is the instruments of Management and Economic Development? If yes then how?

BLOCK-III

Chapter-11

PERFORMANCE BUDGET

Structure

11.0. Introduction

11.1. Learning Objectives

11.2. The Concept & Prerequisites of Performance Budget

Self-Check Exercise-1

11.3. Desirability and Scope of Performance Budgeting in India

Self-Check Exercise-2

11.4. Summary

11.5. Glossary

11.6. Answers to self-check exercises

11.7. References/Suggested Readings

11.8. Terminal Questions

11.0. INTRODUCTION

An important characteristics of planning for economic development, as adopted by most of the under developed economics, has been the dominating role assigned to the public investments and the consequent importance accorded to the public sector. The governments of these countries have assumed not only a centralized direction of resource mobilization and their use, but also have undertaking a significant amount of entrepreneurial allocations, which have led to a logical developmental of public sector becoming a dominant factor in the process of economic development. This development has brought in its wake many important structural changes in the economic and financial administration in these countries.

These, structural changes have brought along with institutional adjustments in the organization and conduct of public sector programmes and activities. The entrepreneurial functions and activities in the public sector are mostly excluded from the conventional budgetary framework and are 'entrusted to autonomous corporation joint stock companies. In a number of instances, however, the government budget includes in addition to normal administrative programmes and activities, certain entrepreneurial activities commonly known as departmental undertakings. "The institutional separation of enterprise activities rests partly on blueprint for action while budgetary provision is mainly operational in nature. It would be, therefore, only logical to expect that management considerations should be of eminent importance in budgeting/and that the budget' should be so devised as to high light the truly operational character, both physical and financial, of any given programme, such is however, not the experience in many developing countries. As a result the operational character of government budget and its links with planning are largely obscured.

The system of conventional budgeting, which is in vogue in the majority of the countries, conceives an emphasis on financial aspects of governmental operation. The financial accountability to the legislature is usually the overriding consideration and this permeates the entire budgetary process. Emphasis is placed mainly on the observance of appropriation limits. Moreover, the object-cum-organizational classification of expenditures in the budget does not enable identification of programmes or projects, and, furthermore, is not related to the cost of major inputs or the work performed. In other words, the system of budgeting does not provide information from departmental reports or other supplementary documents, but in many cases this information cannot be linked directly with financial, data as they appear in a budget or in the accounts because it does not constitute a basis for budget management. The absence of pertinent information of this type reduces the usefulness of this budgetary approach even for purposes of legislative review and appropriation. The sanctions resulting from this process then tend to be accorded to policy objectives that are not explicit in the budget."

The need, development, adoption and use of performance budgeting have developed, therefore essentially in the context of effective connections in this situation. The primary consideration was to highlight management aspects in the budgetary framework and in so doing to bring out the most significant economic, financial and physical aspects of 'the budgetary activity.

The concept of performance budgeting was developed in the U.S.A. and has been given its most rigorous application in that country. Although a programme based budget was in vogue, in different forms and details in metropolitan centres and a few states in the U. S.A. the concept as it is understood now got a major recognition after the first Hoover Commissions Report in 1949. The commission recognizing that the most important aspect in budgeting is the performance in respect of the work to be done or the services to be rendered and the cost involvement of such work/service, recommended that "the whole budgetary concept of the Federal Government should be refashioned by the adoption of a budget based upon functions, activities and project" and this was designated by the Commission as a "Performance Budget."

This recommendation was supplemented by the proposals put forward by A.E. Buck in the Commissioner's Task Force Report. It was stated: "A programme or performance budget should be substituted for pre-present budget, thus presenting in a document: of much briefer compass the government's expenditure requirements of the things brought. Such a budget would not detract from congressional responsibility and should be greatly improved and expedite committee consideration."

Following the Commission a recommendations, the Federal Government of the U.S.A. decided to formulate its budget on a performance basis since 1951. The importance of the concept was further stressed in the second Hoover Commission's Report in 1955. Substantial progress has been made in the U. S.A, since then and quite recently, a few other developing countries have - either adopted this technique or are in the process of considering its introduction.

It may be added here that some distinction has been made in the past between a programme budget and a performance budget, though the Hoover Commission did not seem to view them as different concepts. "There is no practice definition for performance budgeting. It has come to mean something different in every jurisdiction which puts it into operation. In particular, there has been a tendency to make programme budget and performance budget synonymous forms, and this has contributed a good deal to the terminologi cal confusion. In an attempt to clarify what is meant here by programme and performance, definitions will precede organisational and hierarchical lines. For present purposes, programme will be defined in relation to a higher level of organization than performance. A programme embraces a number of performance units. Programme and performance may also be distinguished according to their time dimension. Budgeting programmes are inherently forward-looking a projection of the economic and social policies of a government. Performance must be based on the past on the recorded of prior accomplishment in the preparation of budget estimates, programme determination should precede and set the framework in which the measurement of performance can be undertaken."

Quite recently, a United National Manual on programme, and performance Budgeting has a useful distinction between programme budgeting and performance budgeting. "In programme budgeting the principal emphasis is on a budget classification in which functions, programmes and their sub-divisions are established for each agency, and these are related to accurate and meaningful financial data. Performance budgeting involves the development of more refined management tools, such as unit costs work measurement and performance standards. Of course, the measurement of work, both in a physical and financial sense, presumes an already formulated set of work units which can be derived only when programme and their sub-division is an all-inclusive concept embodying programme formulation as well as measurement of the performance of work in the accomplishment of programme objectives."

It may be mentioned that quite recently, a new programme budget (Planning-Programming-Budgeting ' System) has been developed in the U. SA the purpose of which is to provide for more and better information for decision-makers at all levels of government. It seeks to focus attention on alternative means to achieve carefully defined goals, specifying the full costs and benefits of each alternative etc. Its special feature is the concept of long range planning and programming which brought into the whole process of budget making for the first time.

11.1. LEANING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand about meaning and concept of Performance Budget.

- To know about the prerequisites of Performance Budget in India.
- To discuss about desirability and scope of Performance Budgeting in India.

11.2. THE CONCEPT & PREREQUISITES OF PERFORMANCE BUDGETING

Performance budgeting, as is generally understood, is essentially a technique of presenting government operations in terms of functions, programmes, activities and projects. Through such a meaningful classification of sensations, government activities are sought to be identified in the budget in financial and physical terms so that a proper relationship between inputs and outputs could be established and performance assessed in relation to costs.

The focus in a performance budget is basically different from that in the conventional budgets. The two approaches differ in their scope and content. Firstly, under the performance budgeting emphasis is shifted from the budget as a means of accomplishment to the accomplishments themselves. It concerns itself-primarily with the objectives aimed at by the government rather than on the outlays incurred on several projects. An important aspect of the techniques of the performance budgeting is the precise detaliment of the job to be performed or services to be rendered and a realistic estimate of what that job or service will cost. Secondly, a performance budget is prepared in terms of functional categories and their sub-division into programmes, activities and projects rather than 'being prepared in terms of organisational units and the objects of expenditure. The object classification show's what the nature of governmental programmes, or accomplishments under these programmes" Thirdly, a performance budget prepared in terms of costs and results facilities management control by bringing out the programmes and accomplishments in financial and physical terms close interwoven into the comprehensive document.

The technique of performance budgeting, it may be emphasised, divides the whole gamut of governmental operation into functions, programmes, and activities/projects. A function represents a major division of the total efforts of the government such as Education, Health, Agriculture, Industry, etc. programmes are broad categories within a functions that identify the end products or accomplishments towards the fulfillment of the objectives of a function. The term project is generally used to distinguished such activities as are of a capital nature. For example, education is a function, university education a programme, training of university teacher an activity and the construction of buildings equipping the laboratories a project.

The introduction of a system of performance budgeting involves three basic steps : (a) establishment of meaningful programmes and activities for each function entrusted to an organization or an agency in order to show' precisely the work objectives of various agencies; (b) adoption of a system of accounting and financial management in accordance with the aforesaid classification, and (c) determination of suitable norms 'yardsticks, work-units of performance and unit costs, wherever possible, under each programme and activity for reporting and evaluation. Thus, a performance budget is one which present the purposes and objectives for which funds are required, the costs of programmes proposed for achieving those obj ectives, and quantitative data,' measuring the accomplishments and work performed under each programme."

The main objects sought to be achieved by the performance budgeting are :

- to coordinate the physical and financial aspects of every programme or activity;
- to improve budget formulation, review decision-making at all levels of management in the government machinery;
- to facilitate better appreciation and review by the legislature;
- to make possible, more effective performance audit;
- to measure progress towards long-term objectives as envisaged in a development plan; and
- to integrate the annual budget and developments plans.

In a planned economy, where the public sector outlays constitute a major step towards accelerating the tempo of economic growth, the technique of performance budgeting has its advantages in as much as it serves to bring together the financial and physical implications of each programme, facilitating thereby better programming, decision-making, review of the progress and control for the management, and for a more precise, purposeful and intelligible presentation of government activities to the legislature and the electorate.

Phases of Performance Budgeting :

The process of performance budgeting involves four broad stages : (1) planning or establishing performance; (2) estimating of determining quantum of physical resources, like personnel materials, services, facilities, etc. In order to accomplish these objectives, and the amount of financial resources involved in that; (3) reviewing or ascertaining that the basic objective, resources requirements and resources availabilities are clear and accurate and conform to overall guides and limits; and (4) operating or accomplishing approved objectives with the appropriation voted by the legislature.

PREREQUISITES OF PERFORMANCE BUDGETING

Important pre-requisite for the introduction and operation of 'performance budgeting are that, as first step. It's desirable to emphasize the programme formulation aspect and to establish a clearly defined and meaningful pattern of organizational responsibilities in doing so the budget classification could be closely related to projects included in a development plan. The next logical step would be to bring the system of accounting and financial management in line with budget classification. "In the early stages, emphasis could be placed on planning and on providing prompt financial and related information for use in performance reporting so as to enable a comparison of actual results with original plans. As progress is made towards these, objective, the introduction of accrual accounting and the solution of more complicated accounting problems might be considered. Accrual or cost accounting could be applied either to all types of programmes or of such operations as commercial or industrial activities. The third step consists of the introduction of a system of measuring physical progress and performance. This would depend largely on the availability of relevant statistical data. Each programme would present the own problems in terms of determining proper-units of measure and meaningful indicators of performance. Fourthly, the system of performance budgeting, because of its significant role in the management of governmental operations, demands. Specially qualified personnel for its successful operation. "The most Important consequence of performance budgeting, is that it increases' the responsibility and accountability of management. The performance budget ' enhance the role of management, but at a price-budgeting may no longer be treated as a peripheral assignment but is now at the centre of management responsibility. This should lead to an improvement in the quality and quantity of budgeting at the level of operations. "In its ultimate application, this approach involves it should budgetary operation, financial discipline, skilled and responsible manpower both for budget formulation and execution, a frequent and efficient system of recording and reporting financial and physical data, and close coordination between various governmental agencies and the central budget agency.

Firstly, it is sometimes contended that the performance budgeting involves only a quantitative and financial evolution of programmes and activities, it does not facilitate qualitative evaluation. This limitation is not, however, peculiar to this technique as no budgetary technique is capable of making qualitative evaluation which must depend on certain other appropriate devices.

Secondly, it is claimed that the usefulness of the technique is somewhat limited in the case of activities that are not subject to measurement in any precise manner, such as research,' law and order, defence etc. It is true that the technique may not be as effective as outlays on physical programmes, but even in such subjective areas, suitable norms can be developed to explain performance in a meaningful manner.

Thirdly, the success of performance budgeting depends upon well organised departments and agencies identifiable with programmes and activities. In practice, however precise categories of functions and programmes corresponding to organizational units are rather difficult to achieve. It is stage on the other hand that a synchronization of functions and programmes with organisations though desirable in the long run is neither a pre-condition to nor an essential ingredient of a performance budgeting system.

Self-Check Exercise-1

Q.1 the success of performance budgeting depends upon well organised departments and agencies identifiable with programmes and activities. True/False

Q.2 to emphasize the programme formulation aspect and to establish a clearly defined and meaningful pattern of organizational responsibilities in doing so the budget classification could be closely related to projects included in a development plan. True/False

11.3 DESIRABILITY AND SCOPE OF PERFORMANCE BUDGETING IN INDIA

The pattern of existing budgeting system in India (herewith referred to as the conventional budget) has been designed mainly to ensure legislative accountability and counting scrutiny. Its primary object is to ensure that the moneys are raised and disbursement made by the public authorities in accordance with the schemes sanctioned by the legislature. The cognitional budgets are framed by the various Ministries/ Departments with expenditures broken down into the broad objects constituting the primary units of appreciation., These, budgets are conceived largely in financial terms emphasising there by the financial aspects and not so much the physical accomplishments out of the proposed outlays. Precisely, the conventional budget is accountability-oriented and is intended, primarily, to facilitate its financial control.

Besides being the Principal instrument of providing accountability to the legislature and the means for ensuring financial correctness the budget is, in the context of State-oriented planned economic development, the chief instrument of fiscal policy, a principle device for the implementation of the projects set-out in the development Plans, a vehicle for carrying out the government s policies and decisions, a tool for better management of the governments operations, and chief sources of the data in order to facilitate the decisions of the government on fiscal and economic issues.

With the recognition that the primary object of a sound budgetary system in a planned economy must be to ensure the achievements of plan-objectives, the connotation than is understood from its conventional usage. In the context of planned economic development in which the public outlays are to play a dominant role, specific socio economic goals are derived, availability of resources is assessed, and alternative programmes are selected to attain those goals. As such, the accountability, instead confined to ensure that the moneys are spent as sanctioned and are kept within the limits laid down in the appropriations, must extend to ensure that the targeted physical results are achieved. It becomes essential, therefore, that the budget should reflect the pattern of development Plans in content and classification. The budget should reflect and reveal as to what was planned to be done in term of physical targets, the output to be aimed at or services, to be provided as envisaged in this development plan and what has actually been achieved both in financial and physical system. More specifically, by having a common classification for both the plan as well as the budget, the instrument of budget could be made; an operational document for carrying out the plan objectives.

It is in this context that an assessment has to be made about the usefulness of the present budgetary system and identify its legal accountability, but this usefulness of the system can be enhanced considerably it could be devised to give a comprehensive account of the total efforts of the government in the financial aspects the economics of its activities, the physical results that flow from them, and exact relationship between inputs and outputs'. The conventional budgetary system does not link the financial and physical aspects of programmes and activities nor does it provide an adequate amount of information of the effectiveness of money spent on such programme and activities. It does not throw sufficient light for an overall view of the financial and physical aspects of such programmes and activities, and the accomplishments.

The question of introducing performance budgeting in the Indian context could, therefore, be viewed from two angles: (a) by pointing out the deficiencies in the conventional budgeting and considering the merits of the performance budgeting and (b) by a consideration of the various arguments against the introduction of the technique of performance budgeting; Approach (a) has briefly been conversed in the preceding paragraphs. As regards (b) various doubts and misgivings about the introduction of performance budgeting are detailed below:

1. Quite a number of the purposes designed to be served by the technique of performance budgeting are presently being already served - by the techniques and processes of economic planning in certain ways and consequently introduction of the technique of performance budgeting would amount to duplication of effort.
2. Sufficiently comprehensive data and information is now given in the budgetary document on both the financial and physical aspects of governmental programmes and activities, supplemented by the annual reports of the Ministries/Departments annual report on the workings of commercial and industrial undertakings of the government etc.
3. The financial and legal accountability of the executive government to the legislature will be imparted by the introduction of performance budgeting.
4. A bulk of the disbursements undertaken by certain Union Ministries/ Departments e.g., agriculture, education, etc., consist of grants to the states and other organizations. As such their performance may not be capable of measurement at Union level.
5. In the present institutional structure, a performance budget can, at best, be only supplementary to the existing conventional budget and can not in any way supplemental.
6. The utility of performances budget may be greater in the context of the relationships between the executive and the legislature as they exist in the U.S.A. in the Indian context where the initiative in budgetary decision-making vests in the executive, the legislature being mainly concerned with sanctioning the policies formulated by the executive, the system may not be capable of achieving that degree of success as may be anticipated.

The working Group examined these points and had come to the following conclusions:

1. Commenting on the point that performance budgeting is largely a technique for planning, implementation and reporting, both in financial

and physical terms, and that this is obtaining, in some measure, in our planning process, the Working Group remarked that prima facie, the contention seems to be an over simplification both of concept of performance budgeting as also of the virtues of the planning process. The techniques of performance, budgeting is something more than a mere bridge between the financial and physical aspects of a programme, in so far as the planning process is concerned, the experience during the last decade or so has indicated the inadequacy of the link between the two. It is also observed that because of the absence of a rapport between the financial and physical aspects of a programme, budgetary' estimates were often either under pitched of over pitched with consequential impact on the allocation of resources. It has also, in turn contributed in some measure to the gap between the physical targets and financial outlays. To write programme, targets, outlays, etc., exist in the planning process, there is a lacuna in the existing system in that there is no well-organized operational framework. To the extent that such a framework would be supplied by performances budgeting it would be greatly strengthening the existing planning process.

2. The argument is advanced that progressively increasing data and information about the various programmes and activities of the government, financial as well as physical, is now given in the 'budget and the various documents attached to it. It is correct that the Explanatory Memorandum, Notes on important Scheme furnished in the Demands for Grants, the Economic Survey the Economic Classification of the Budget, to provide the legislature and the public at large substantial amount of information. While these development have been in the right direction, it is to be recognised that unless these somewhat disjointed efforts are coordinated and brought into a well-knit, purposeful and cohesive whole at one place they are not likely to be of much help either in the formulation of programmes or in the evaluation of performance. It has thus to be seen that though there were various development welcome in themselves, yet in the absence of a comprehensive scheme for budget reform and also because they were often the result of attempts at meeting the requirements from different quarters, they tended to be diffused and were thus inadequate."

3. The contention that under performances budgeting as emphasis 'is shifted to programmes and activities and their cost-benefit analysis, the legal and financial accountability of the executive government will be affected, appears to be based on erroneous impression. This contention may not be well- founded because for technique of performance budgeting could be formulated in such a way that the Ministries/Departments organisations may retain their identity and the Demands for Grants can continue to be in terms of subject of expenditure (i.e. units of appropriation) under the several programmes

and activities of the Ministries/Departments/Organisational. The legal and financial accountability of the executive management would not, therefore, be compromised, rather important aspects of accountability with result will be secured.

4. As regards the difficulties concerned for the evaluation of the results out of loans and grants given by Union Ministries. Departments it is a matter of detail regarding the form and content of performance begetting rather than the principles underlying it.

5. The fifth argument relates to the form in which the performance budget is to be prepared and presented. The issue involved is whether it should be a supplementary document to the conventional budget or should replace the latter. That the performance budget should be a supplementary document to the conventional budget is supported on two points (a) it may not be desirable to change an established practice; and (b) it would not be possible to prepare a performance budget within a period of three months that now terms the crucial period during which the budget is prepared and presented. It is contended, however, that 'it would not be sufficient to have the performance budget document as a supplementary one to the existing set of documents, as in that case it will not have an impact whatsoever on the existing system. For one thing the performance budget is being evolved to overcome the deficiencies in the existing budgetary process and framework and not to supplement it. The idea of a supplementary document in which a context would inevitably mean the constitution of the existing procedure, financial practices, accounting classification, etc., with their inadequacies. Instead, performance budgeting is not made an integral part of the budgetary process, but only an additional exercise, unconnected with the main process, the advantages that are expected of it would not materialize. Secondly, performance budget is not merely a matter of form; it represents a change in concept that the significant effects of the approaches to the budget and the decision-making practices. The form is only the culminating point of the various processes forwards better management and control. The form of the document has no special significance apart from the presentation effect. The performance budget as a supplementary document would be somewhat of a fifth wheel to the coach. The appropriate method in the circumstances would be to adopt, evolve and introduce performance budgeting in such a way that it would fit in without conditions and mitigate the transactional difficulties involved in the Switch over, while continuing, at the same time, to serve the purpose expected of it."

As regards the practicability of preparing a performance budget within a period of three months referred to above it is contended that "In our pl anning process, both the implementation of programmes and the evolving of new ones are a continuous process throughout the year.

Thus, in a way, budgeting would also be an all-the-year round process with the final stage of consolidation being reached in the period referred to above. Moreover, even under the present system, the administrative departments and organisations are enjoined' upon to forward their budget proposals quite early in the financial year, "'beginning with July. Information on programmes, activities, targets achievements and other work-load data will be available continuously all through the year through a performance reporting system.

6. Coming to the executive legislature relationship, it may be pointed out the need for the performance budgeting does nothings on the character of such relationship.

Self-Check Exercise-2

Q.1 The pattern of conventional budgeting system in India has been designed mainly to ensure legislative accountability and counting scrutiny. True/False

Q.2 In the present institutional structure, a performance budget can, at best, be only supplementary to the existing conventional budget and can not in any way supplemental. True/False

11.4. SUMMARY

It may be concluded that the introduction of the technique of performance budgeting is needed more than over for integrating the plan and budget-in' process, for building up an integral edifice outlays and accomplishment for each administrative agency for qualification of the results from government outlays, for enabling a more purposive audit and preliminary review and control, and thus serving as a window, so to say, to every citizen of the country on the government activities.

11.5. GLOSSARY

- **Conventional Budgeting :** it involves adding funds to the previous year's budget to expand or complete projects.
- **Performance Budgeting :** it is based on the relationship between program funding levels and expected result from that programme.

11.6. ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

11.7. REFERENCES/SUGGESTED READINGS

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11.8. TERMINAL QUESTIONS

(a) Trace the evolution of performance Budget.

(b) Discuss about the Desirability and Scope of performance Budgeting in India.

ZERO-BASE BUDGETING

Structure

12.0. Introduction
12.1. Learning Objectives
12.2. Zero-Based Budget : Meaning, Process, Definition
Self-Check Exercise-1
12.3. The Decision Package, Ranking & Advantages of Zero Base Budget
Self-Check Exercise-2
12.4. Summary
12.5. Glossary
12.6. References/Suggested Readings
12.7. Terminal Questions

12.0. INTRODUCTION

The budget system, it will be observed, is the means by which financial administration is expressed broadly and therefore, what has been said about the general characteristics of a good system of financial administration appeals equally to the budget system.

The budget system consequently, must provide for unity an centralization; for control at all stages of budget procedure; for simplicity; promptness and regularity; and for efficiency of functioning. The traditional budget procedure is based on incremental budgeting where most organisations start with the current Operating and expenditure levels as an established base. These traditional budgeting is a static tool, weighted down by masses of detailed numbers for every conceivable t3rpe of expenditure.

Another kind of budgeting known as zero-base budgeting (ZBB). ZBB is different from traditional budgeting method. It is a private sector system in use in Unites States private sector ZBB is sought to be applied to the public sector. Under this method the entire budget for the last year is taken as zero. It requires identification and redefining of objectives, examination of various alternative ways of achieving those objectives and then selecting the one best alternative through cost benefit analysis and cost-effectiveness analysis privatization of objectives and programmes; switching of resources from programmes with lower priority to those with higher priority; and identification and elimination of programmes which have outlived their utility.

In ZBB, a Ministry/Department or an organisation is required to justify not only the new proposals and the funds therefore but also the ongoing activities and the funds for them. Hence, under ZBB approach, the existing programmes are not treated permanent but will be examined afresh as to their continues utility and effectiveness thereby making resources available for new programmes.

In India, the then Finance Minister, V.P. Singh told a Parliamentary Consultative Committee that the government would be introducing ZBB at first in a small way in 1986-87 and then in full in budget formulation from 1987-88. However, it is easier said than done. ZBB's applicability to the public sector is fraught with many difficulties.

12.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand about meaning and concept of "Zero Base Budgeting"
- To analyze about advantages of Zero Base Budget.
- To define Decision units

12.2. ZERO-BASED BUDGET: MEANING, PROCESS, DEFINITION

Meaning

The zero-base approach required each organization to evaluate and review all programmes and activities systematically, whether current or new. It involves review of activities on the basis of output or performance as well as cost to (1) emphasize managerial decision-making, (2) number-oriented budgets, and to emphasize analysis.

ZBB has been defined as a systematic method of reviewing either all or selected number of organizational activity or the purpose of reallocating resources to improve operational effectiveness. The results of ZBB would lead to the restoration of the budget within a range of zero per cent to hundred percent or even more. There is a constant review depending upon the usefulness of a particular service, unit or function.

ZBB is an approach and not a fixed procedure to be applied uniformly to all the organisations. The process must be adapted to suit the specific needs of each organisation. It heavily depends upon a number of techniques developed in the early 1960's Peter A. Phyrr's name is closely associated with ZBB approach.

ZERO-BASED BUDGETING: PROCEDURE

Unlike the traditional budgeting method, which typically involves building on previous budgets, Zero-Based Budgeting (ZBB) requires starting from scratch, justifying every expense from the ground up. This approach involves breaking down an organization's functions and evaluating each one annually, regardless of its history or whether it is a long-standing activity or a new proposal.

In ZBB, the budget is divided into units known as decision packages, which are created by managers at various levels. These packages include an analysis of the purpose, costs, performance measures, benefits, alternative actions, and the consequences of rejecting the proposal.

The ZBB process involves four main steps:

Identification of decision units

Analysis of each decision unit through a decision package

Evaluation and ranking of decision packages by priority

Preparation of detailed operating budgets that reflect the decision packages approved for funding.

DEFINING DECISION UNITS:

The goal of ZBB is to guide management in evaluating activities and making decisions based on careful analysis. Therefore, every relevant component must be clearly defined so that it can be assessed and acted upon. In many organizations, defining decision units is straightforward, as they often align with the budget units used in traditional budgeting systems.

Decision units may be defined at the sub-programme level if there are distinct organizational units associated with each programme element. The decision packages at this level can then be grouped to assess the broader programme. Similarly, decision packages for individual programme elements can be grouped for the evaluation of the entire programme.

Self-Check Exercise-1

Q.1 ZBB attempts to focus management's attention on evaluating activities and making decision. True/False

Q.2 Incremental approach of budgeting is also known as conventional budgeting. True/False

12.3. THE DECISION PACKAGE, RANKING & ADVANTAGES:

DECISION PACKAGE

It is the building block of zero-based concept. It is a document that identifies and describes each 'decision-unit in such a manner that the management can evaluate it and rank it against other decision units competing for funding and to decide whether to approve it or disapprove it.

The content and format of the decision package must provide management with the information it needs to evaluate each decision unit. This information may relate to:

1. Purpose
2. Description of actions
3. Costs and benefits

4. Work load and performance measures
5. Alternative means of accomplishing objectives
6. Various levels of efforts

The most important aspect of developing decision packages is the formulation of meaningful alternatives. The types of alternatives that should be considered in developing decision packages are alternative methods of accomplishing the objectives or performing the operation and identifying different levels of effort of performing the operation. The identification and evaluation of different levels of efforts in probably the most difficult aspect of zero base analysis, yet it is one of the key element of the process.

THE RANKING PROCESS :

This process' provides management with a technique to allocate the limited resources. It then identifies the benefits to be gained at each level of expenditure and studies the consequences of not approving additional decision packages ranked below the expenditure level.

The ranking process establishes priorities among the incremental levels of each decision unit. The ranking therefore display a marginal analysis. The key to an effective review and ranking process lies in focusing top management's attention on key policy issues and discretionary expenditures.

ADVANTAGES OF THE ZERO-BASED BUDGETING APPROACH

There are several distinct advantages to implementing an effective Zero-Based Budgeting (ZBB) approach, including the following:

Shifting the focus of the management process towards in-depth analysis and decision-making, rather than just dealing with numbers—addressing the what, why, how, and how much of each expenditure.

Merging planning, budgeting, and operational decision-making into a cohesive process.

Encouraging managers to thoroughly assess the cost-effectiveness of their operations, ensuring that both new and existing programmes are carefully examined and clearly defined, rather than being hidden within broader functions.

Providing a framework that enables a balance between long-term and short-term needs, while also offering a tool to track costs and performance throughout the year.

Facilitating rapid adjustments to the budget or resource allocations during the year, especially in cases where revenue falls short. ZBB allows for quick, rational modifications to goals and expectations to align with what is financially feasible.

Highlighting similar functions across different departments, which allows for easier comparison and evaluation.

Promoting broader management participation and training in the processes of planning, budgeting, and decision-making.

Through ZBB, low-priority programmes can be reduced or eliminated, improving overall programme effectiveness. High-priority programmes can receive increased funding by reallocating resources within the organization. Ultimately, the goal of ZBB is to ensure that taxpayers' money is spent wisely, with each expenditure being fully justified.

Self-Check Exercise-2

Q.1 With the help of ZBB approach low priority programmes can be eliminated or reduced. True/False

Q.2 One of the advantages of the ZBB is forcing managers to evaluate in detail the cost-effectiveness of their operations. This includes specific programmes - both new and old - all of which are clearly identified rather than functionally buried. True/False

12.4. SUMMARY

ZBB is no miracle' in financial administration. It would be dangerous to regard ZBB as a sure remedy for financial laxity. The success of ZBB in American industry is largely due to profit motive and organisational resilience. Both of these factors do not usually operate in the governmental setting. Moreover, the bureaucratic temperament is conditioned by the growth impulse which clamours for larger budgets rather than for more challenging assignments. Also, the powerful 'impact of political pressures on financial decision-making makes the prospects of ZBB very uncertain. In fact, the very nature of government decision-making is muddling through is ill suited for ZBB.

The advocates of ZBB regard it as. a pragmatic approach which offers an extremely flexible management tool. It can lead to substantial savings.' Low priority programmes can be eliminated or reduced. Programme effectiveness can be drastically improved, although it may or may not have a budgetary impact. High impact programmes can obtain increased financial allocation by shifting resources within an agency and tax increase can be checked with all its much evaluated benefits. ZBB's application to public finance looks a doubtful starter. More conventional methods of sound budgeting should not be sacrificed for the sake of blind limitations for an ideal system.

12.5. GLOSSARY

- **Zero-Based Budgeting :** a method of budgeting in which all expenses must be justified for each new period.

12.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

12.7. REFERENCES/SUGGESTED READINGS

Laxmikant, M. 'Public Administration' Fifth Edition, Tata McGraw-Hill Publishing Company Limited, New Delhi, 2016.

Gupta, B.N. Indian Federal Financial and Budgeting Policy, Chaitanya Publishing House, Allahabad, 1970.

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Mahajan., S.K. & Mahajan., A. P. Financial Administration in India, P.H.I, New Delhi.

12.8. TERMINAL QUESTIONS

(a) What do you understand by Decision units.

(b) Discuss about from basic steps of ZBB approach.

Chapter-13

PLANNING PROGRAMMING BUDGETING SYSTEM

Structure

13.0. Learning Objectives

13.1. Introduction

13.2. Objectives, Elements/Features of PPBS

Self-Check Exercise-1

13.3. Importance of PPBS

Self-Check Exercise-2

13.4. Summary

13.5. Glossary

13.6 Answers to Self-Check Exercises

13.7. References/Suggested Readings

13.8. Terminal Questions

11.0. INTRODUCTION

The Planning Programming Budgeting System (PPBS) is a comprehensive management approach that emphasizes using analysis for making program decisions. The goal of PPBS is to give management a more analytical foundation for making program decisions and to implement those decisions by integrating the functions of planning, programming, and budgeting. In this context, "management" refers to the overall leadership and administration of an organization. Program decision-making, which is central to management, involves determining the direction of an organization's efforts and allocating resources to achieve those objectives. This process involves defining the organization’s goals, choosing the strategies to achieve them, and implementing the selected actions.

PPBS is focused mainly on major decision-making activities, particularly those that precede operational execution. An organization can be simplified into five key phases: (1) planning, (2) programming, (3) budgeting, (4) operations, and (5) evaluation. PPBS addresses the first three of these phases, each of which plays a distinct but interconnected role in the overall functioning of the organization.

1. **Planning** involves analytical activities aimed at selecting the organization’s objectives and assessing different courses of action to achieve these goals. It

essentially asks whether a specific action is the most effective way to move the organization toward its objectives compared to other alternatives.

2. **Programming** translates plans into actionable schedules for the organization. It includes developing detailed resource requirements and determining the steps needed to implement the plans.
3. **Budgeting** focuses on preparing and justifying the organization's annual budget. Its primary role is to ensure adequate funding to implement the program effectively.
4. **Operations** refers to the actual execution of the organization's program, with all previous phases preparing the groundwork for these activities.
5. **Evaluation** assesses the success of the organization's programs in achieving its goals. It measures the effectiveness of current operations and provides insights that can guide modifications to current programs or inform the planning of future ones.

13.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To know about the evolution of PPBS.
- To know about objective and features of PPBS.
- To Comprehend the importance of PPBS.

13.2. OBJECTIVES, ELEMENTS/FEATURES OF PPBS

A key goal of the Planning Programming Budgeting System (PPBS) is to integrate the functions of planning, programming, and budgeting. In PPBS, planning—carried out through analysis and research—becomes an essential part of the program development process. The research conducted during the planning phase helps identify the most appropriate actions to guide the organization's overall program. Additionally, the annual budget is directly linked to the approved program and financial plan of the organization. While planning, programming, and budgeting each serve distinct roles, they are structured as sequential phases of a unified process aimed at steering the organization toward its goals.

PPBS seeks to minimize the independence of planning, programming, and budgeting, ensuring that the procedures and workflows under this system establish clear connections between these core functions. Emphasis is placed on research to aid in selecting the most effective courses of action for the organization. The planning phase lays the foundation for the development of the program, which in turn informs the budget preparation. Therefore, the creation of the program directly stems from the planning outcomes, and the budget is developed based on that program, ensuring that all activities are interconnected and aligned.

ELEMENTS/FEATURES OF PPBS

Defining PPBS is challenging, as there is no universal agreement on its precise meaning. This difficulty arises because PPBS encompasses several distinct features, each emphasized to varying degrees depending on the specific context in which it is applied. The Planning Programming Budgeting System is fundamentally made up of five key components:

1. A structured program framework,
2. A formalized program document with future projections,
3. A decision-making process,
4. The application of analysis for informed decision-making, and
5. An information system tailored to support PPBS needs.

Disagreements about the definition of PPBS often occur when too much focus is placed on one element while neglecting others. However, all five components—the program structure, the program document, the decision-making process, the analytical approach, and the supporting information system—are essential to the system's success. The most effective PPBS incorporates all of these elements because they are interconnected and work together to enhance overall system effectiveness. For instance, the program structure is linked to the decision-making process, and issues for analysis are framed within the program's classification. Additionally, analysis is integrated into the decision-making procedures, and the information system underpins all other components.

Although these elements are interrelated, it is still possible for an organization to implement individual aspects of PPBS. For example, the use of analysis in decision-making can be valuable on its own, even without the other components. Similarly, creating a program with clear goals and actions over a long-term period can be beneficial. However, the full potential of PPBS is only realized when all elements are combined.

SELF-CHECK EXERCISE-1

Q.1 A major objective of the PPBS is to unify the planning, programming and budgeting functions. True/False

Q.2 **Programming** is the process of turning plans into a detailed action plan for the organization. It involves identifying the resources required and outlining the steps necessary to carry out the plans. True/False

13.3. IMPORTANCE OF PPBS

A program structure refers to a classification of possible actions an organization can take to achieve its goals. This structure is designed to support decision-making and the allocation of available resources within the organization. The program data, including benefits and resource allocations, should be presented within the organization's multi-year program and financial plan according to this structure. The structure also provides a framework for creating program memoranda, which are used to justify proposed programs. These documents will be further elaborated upon below.

The program structure offers a perspective on the organization's activities that aligns with the needs of program analysis and decision-making. A key aspect of the program structure is its alignment of major agency objectives with the corresponding actions selected to reach those objectives. This feature prompts fundamental management questions about what the agency aims to achieve and what steps are being taken to meet these goals. By structuring programs around objectives, the agency ensures that its goals remain central to program analysis and decision-making.

SELF CHECK EXERCISE-2

Q.1 **Budgeting** involves the process of preparing and justifying the annual financial plan for the organization. The primary purpose of budgeting is to ensure that adequate funds are available to implement the program. True/False

13.3. SUMMARY

For the purposes of PPBS, organizational goals or objectives must be defined clearly enough to ensure they can be directly aligned with the actions that contribute to their accomplishment. The structure ensures that there are clear connections between goals and the methods used to achieve them. Therefore, the definitions of goals should be specific enough to allow for the consideration of alternative actions. These goals should provide precise direction to evaluate different courses of action.

At the top level of the program structure are the major organizational goals. These are referred to as Major Programs and represent the highest tier of the program classification. Depending on the specific adaptation of PPBS, this level may be referred to using different terms, such as program categories, program packages, or program accounts, all signifying the higher level within the classification.

13.5. GLOSSARY

11.7.1. **Planning Programming Budgeting System :** It is to set certain major objectives to define programmes essential to these goals, to identify resources to the specific types of objectives and to systematically analyze the alternative available.

13.6. ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

13.7. REFERENCES/SUGGESTED READINGSS

Laxmikant, M. 'Public Administration' Fifth Edition, Tata McGraw-Hill Publishing Company Limited, New Delhi, 2016.

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Mahajan., S.K. & Mahajan., A. P. Financial Administration in India, P.H.I, New Delhi.

13.8. TERMINAL QUESTIONS

(a) Give reasons about the importance of PPBS?

(b) The PPBS is Concerned Primarily with major decision-making process. Elaborate.

Chapter-14

SUNSET BUDGETING

Structure

14.0. Introduction

14.1. Leaning Objectives

14.2. Termination Innovation & Voting-Assumption in Sunset Legislation

Self-Check Exercise-1

14.3. Relationship between Sunset Review and Politics, features & need

Self Check Exercise-2

14.4. Summary

14.5. Glossary

14.6. Answers to self check exercises

14.7. References/Suggested Readings

14.8. Terminal Questions

14.0 Introduction: Sunset budget is structured to 'self-destruct' within a given pre-set duration to make expenditure is stopped by an already fixed date. The fundamental difference between with and without a sunset clause is the default rule of termination. Legislation without defaults to legislation that effectuates in perpetuity, while legislation with a sunset budgeting legislation that effectuates until termination. Obviously, these are defaults and can be with further legislative action by extending sunset legislation or repealing permant.

SUNSET LEGISLATION AND THE FEDERAL GOVERNMENT USA

Even though many efforts were made for budgetary reform, federal budgeting incremental process in which the most important factor in deciding an agency's budget amount of the previous year's budget. Legislators look only at additions or increments new budget is formulated and last year's programmes continue to receive funding with no review.

The Sunset Act was introduced, as mentioned earlier while tracing its origin and by Senator Edmund Muskie m 1976, designed to eliminate incremental budgeting. Act carried with it the assumption that every federal program will automatically unless there is a vote to continue it. Instrumentalism would be replaced with a procurement evaluation of each federal programme before continued funding could' be approved promise of budgetary reform. Sunset Legislation was never approved by the Congress felt that the work involved in viewing all federal- programs would create '.tremendous would be conducted by congressional oversight committees that are biased in favour of the continued funding of the only programmes with low funding and weak constituencies nomination and if these agencies were meant to be terminated to' set legislation.

Sunset Legislation never was adopted by the federal government in the USA, dewed sunset as one of the most significant.

14.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand Sunset Budgeting
- To trace the termination and innovation is Sunset Legislative
- To Comprehend the relationship between Sunset Review and Policies
- To discuss about the features of Sunset Budgeting.

14.2. TERMINATION, INNOVATION & VOTING-ASSUMPTION IN SUNSET LEGISLATION

Defined as an idea, perceived as new, by an individual. It is adopting it, no matter how old the idea may be or how opted it. In this respect, Sunset Legislation is an innovate ratification, no matter how many states have previously adore vanes is the adoption proneness of an entity that has the simply means that the idea may have been tied earlier but if it concept of innovation.

TERMINATION AND OF SUNSET

Act assumes that every federal program will terminate unit Instrumentalism would be replaced with a performance before consumed funding would be approved. Under the would be reviewed once every eight years. Implicit in Sunset termination.

Its promise of budgetary reform, Sunset Legislation was it was felt that reviewing all federal programs would creating administrators and might lead only to a wrong evaluation to meet was viewed as one of the most significant movements of the.

RELATIONSHIP BETWEEN SUNSET REVIEW AND POLICIES

Parliament's capacity for adopting innovative policies depends on outdated policies, the most innovative States should be. States that adopt Sunset legislation and are reviewing and programs must have a new policy or program that mil replies relationship between sunset review and policy innovation can be three hypotheses;

States that adopt sunset are more, innovative than States that his state's most innovative in adopting sunset, with lower add innovative in adopting other policies.

Unanending sunset after initial adopting Mark Ross Daniels, the first hypothesis is true to quite an extent. Research and statistical analysis, he concluded that there is a statistically significant between general policy innovativeness and adoption of Sunset Legislation on two innovation indices. This falls short of demonstrating a causal relationship between to the adopt a Legislative termination mechanism and the tendency to embrace new pickly. The results show that only sunset adopting States have a greater tendency policy innovativeness than non-adopting states. While this can be seen as a connection termination and innovation, it can also be seen as further evidence that a State's imitativeness reveals a willingness to adopt all new policies, including the policy review.

In this sense, sunset adoption may not be so much an enactment of termination loping of yet another new policy or a new innovation.

SECOND HYPOTHESIS

The second hypothesis results report that there is a statistically significant relationship general policy innovativeness and the speed of Sunset Legislation adoption. However, the relationship is inverse States that quickly adopt other innovation, the octant to adopt sunset. States that are _ usually slow in adopting other innovation, they are most innovative when it comes to adopting Sunset Legislation. The speed of ensured by a State's adoption and the order of adopting being the same. States slow in adopting other policies were among the early adopters of sunset. There terous studies and researches on this issue.

THIRD HYPOTHESIS

Trading the third hypothesis, data analysis reveals no relationship between general activeness and repeal/suspension or retention of Sunset. Although, it has been Legislatures have a tendency to repeal or suspend Sunset review, there is no evaluate states are generally less innovative than states that retain Sunset.

Self-Check Exercise-1

Q.1 Sunset budget is structured to 'self-destruct' within a given pre-set duration to make expenditure is stopped by an already fixed date. True/False

Q.2 Senator Edmund Muskie in 1976, designed Sunset budgeting to eliminate incremental budgeting. True/False

14.3. NEED AND FEATURES FOR SUNSET CLAUSE

It termination rules in a wide range of Legislation, for example, a patent exploit reward an innovator or a protective tariff expiring to force an industry to compete.

Intrinsic Necessity: Intrinsic necessity means that sunset clauses may be brings into force when a parliamentary objective is time bound. If Legislatures law must end so that a pre-decided identified aim is accomplished, they law with default termination. In the US, the reward theory, supported, by 'the, Constitution, states that it is the job of an intellectual property to reward people are active in innovating otherwise there would be no incentive to do so.

Information Rationale : The informational rational explains how are used between government and private actors to produce information transaction costs. If the law is about to be terminated, the legal environment change too by updating the law. In such a situation, the Legislature will avoid the transaction costs of repealing or amending the law.

Political Requirement : Sunset clauses are ' used between lawmakers as a bargaining since sunset clauses affect a law, the sunset can favour one politician more than other.

Taucrtic Uses : Sunsets may be brought in to reinforce the time limits. Firstly, it an interim law giving the Legislature more time to create a permanent law. An law is a stop-gap, an incomplete solution. So, sunsets may be used to permit Legislature more time to create a permanent law. The British Labour M.P., Nick ford said that the Bill could have an interim characteristic tackling the current problems but not the far-reaching problems.

Legitimacy Legislation : Sunsets may be introduced as a Stop-Gap Legislation, sometimes termed as emergency legislation. A law maybe created by the Legislature a gap which it understands to be an emergency gap. It often attributes a sunset law as it wishes to come back to the issue. This happens in the situation where concerned issue needs to be examined extensively before the Legislature passes.

Temporary Social Problem Responses: The United Kingdom's Better Regulation Force suggests utilizing a sunset clause to initiate controlled steps taking into the market conditions or authorizing an economic regulation which can be estimated once the markets develop.' Here, a policy decision in this situation portrays final decision that the law will need elimination, not modification. Sometimes, even though the Legislature feels some uncertainty, the Legislators presume that situation improve with such surety that the law will become absolute, for example, in 1933, Agricultural Adjustment Act was made to stabilize falling prices by, in the interim, thereby reducing agricultural production in Franklin D. Roosevelt's New Deal.

FEATURES OF SUNSET BUDGETING

Featuring has the following features:

Termination : The notion behind the theory of sunset provides for programs and agencies to terminate automatically agreeing to a predetermined timetable unless clearly renewed by law. Sunset provisions generally comprise of two components:

12.8.1. An action-forcing system, with the eventual risk of elimination, and

12.8.2. A structure or a design for the systematic review and assessment of past outcomes.11

Emphasis on Goals : Sunset budgeting techniques will allow you to take a look at operating budget, not in comparison with what your totals were last year, but with what your goals are. Ultimately, that kind of budgeting approach is necessary, because, when all is said and done, there are only two kinds of money-new money old money. New money is what you get from romance who has never given any.

Self-Check Exercise-2

Q.1 Sunset budgeting techniques will allow you to take a look at operating budget, not in comparison with what your totals were last year, but with what your goals are. True/False

Q.2 Intrinsic necessity means that sunset clauses may be brings into force when a parliamentary objective is time bound. True/False

14.4. SUMMARY

Sunset legislation is a formal policy process designed to phase out outdated, redundant, or unnecessary programs. According to K.H. Handa, it represents the idea of self-terminating government programs by setting expiration dates for their statutory authority. This is accomplished by including time limits within legislative acts, ensuring that programs automatically end on a specified date unless they are actively renewed by the legislature following a comprehensive review.

14.5. GLOSSARY

- **Sunset Legislation :** It is a formal process of policy review for eliminating the undesired, outdated, redundant, and irrelevant programmes.
- **Sunset Budget :** Designed to self destruct within a prescribed time period to ensure the cessation of spend in by a determined date.

14.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

14.7. REFERENCES/SUGGESTED READINGSS

- Laxmikant, M. 'Public Administration' Fifth Edition, Tata McGraw-Hill Publishing Company Limited, New Delhi, 2016.
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14.8. TERMINAL QUESTIONS

(a) Critically analyse advantages and disadvantages of sunset budgeting.

(b) Why we do have need for sunset clause?

BLOCK-III

Unit-15

TAX ADMINISTRATION IN INDIA

Structure

15.0 Introduction

15.1 Learning Objectives

15.2 Tax Revenue — Concepts and Classification, Direct Taxes, Indirect Taxes before 2017

Self-Check Exercise-1

15.3 Non-tax Revenue

Self-Check Exercise-2

15.4 Summary

15.5 Glossary

15.6 Answers to Self-Check Exercises

15.7 References/Suggested Readings

15.8 Terminal Questions

15.0 INTRODUCTION

The mobilization of resources is essential for the planned economic development of an economy, serving as a key driver of growth. Resource mobilization goes beyond just taxation, encompassing income from public services, enterprises, and utilities. For a development plan to succeed, it must prioritize generating sufficient surpluses from the government's current revenues, departmental units, and public enterprises. As the economy grows and incomes rise, it should be able to generate additional resources through public borrowings and small savings. In some cases, deficit financing may also be used to accommodate the increasing demand for money, driven by rising incomes and the growing monetization of the economy. However, care must be taken to ensure that such financing does not lead to inflation. Additionally, external financial assistance may be required if domestic resources are insufficient to support development programs.

This unit primarily focuses on two key revenue sources—tax and non-tax revenues—for resource mobilization. We will explore the components of both and provide examples, such as the provisions related to resource mobilization in the 1991-92 Budget.

15.1 LEARNING OBJECTIVES

By the end of this unit, you should be able to:

- Define the concepts and categories of tax revenue
- Explain the various components of non-tax revenue

15.2 TAX REVENUE — CONCEPTS AND CLASSIFICATION

- Government income can be defined in two primary ways: broadly or narrowly. In the broadest sense, public receipts encompass all forms of income or revenue that the government receives, including borrowings and asset sales. However, when referring to government **revenue** in the narrower sense, it specifically refers to the money that the government earns from taxes and other regular sources that contribute to its budget.
- The most significant source of government revenue is **taxes**, which are compulsory payments imposed by public authorities. These are usually levied on individuals, businesses, or goods. A tax is not meant to penalize a person for wrongdoing (as penalties do), but rather to generate revenue for the government. Penalties, on the other hand, are imposed as punishment for breaking the law, with the goal of deterring undesirable behavior. Taxes, however, are imposed to fund government services and infrastructure without necessarily linking the amount collected to the specific services provided to the taxpayer.
- The main categories of taxes are **direct taxes** and **indirect taxes**:
- Direct Taxes
- Direct taxes are those where the tax burden falls directly on the person or entity being taxed, and the liability cannot be transferred or shifted to another. These taxes are based on an individual’s or corporation’s ability to pay, as they are directly assessed based on income or wealth.
- **Examples of Direct Taxes:**
- **Income Tax**:
- Income tax is a tax imposed on an individual’s or entity’s income after deductions and exemptions. In India, the first Income Tax Act was introduced in 1886, and several amendments have been made since, with the most recent comprehensive changes made under the Income Tax Act of 1961. Income tax covers all types of earnings, including salaries, profits from business, capital gains, and benefits like perquisites. However, agricultural income is exempt from income tax.
- The tax rates are subject to change each year during the Union Budget, with income slabs for individuals and tax rates being adjusted accordingly. Some income sources are also fully exempt from tax, such as certain contributions to provident funds, gratuities, and scholarships.

- **Corporation Tax**:
- Corporation tax is levied on the income of companies, based on the profits they generate. Companies are required to pay this tax on their earnings, while the shareholders receive dividends after tax deductions. The government periodically adjusts the tax rate for corporations. For example, in the 1991-92 Budget, the rate for widely held domestic companies was reduced from 50% to 40%. Additional deductions were also introduced for companies setting up new industries.
- **Capital Gains Tax**:
- This tax applies to the profits made from selling capital assets such as land, property, or shares, when the selling price exceeds the original purchase price. Capital gains tax varies depending on the type of asset and the length of time it was held. However, certain items like consumables and raw materials are exempt from capital gains tax.
- **Wealth Tax**:
- Wealth tax is levied on the net wealth of individuals, Hindu Undivided Families (HUF), and closely held companies. Agricultural land is excluded from the calculation of wealth tax. The tax is assessed based on the value of assets such as properties, investments, and savings. The wealth tax threshold and rates have changed over time, with exemptions and deductions applied to the total wealth of individuals.
- **Estate Duty**:
- Estate duty is a tax that was imposed on the total value of a deceased person's estate, including their properties, cash, and assets. In 1985, estate duty was abolished for agricultural land. The Estate Duty (Amendment) Act of 1984 and 1985 removed the tax on most property transfers, except for those occurring before certain dates.
- **Gift Tax**:
- The gift tax is levied on the value of gifts given by individuals, Hindu Undivided Families (HUFs), and corporations. If the value of gifts exceeds a specific amount (such as Rs. 20,000), the giver must pay the tax. However, certain gifts, like those given to charitable institutions or a spouse, are exempt from this tax.
- Indirect Taxes
- Indirect taxes are those that are imposed on one person but can be shifted to others. This typically happens in the form of taxes on goods or services where the buyer pays the tax, but the seller is responsible for remitting it to the government. Examples include **sales tax**, **excise duties**, and **Value Added Tax (VAT)**.
- While direct taxes primarily focus on the income or wealth of individuals and corporations, indirect taxes are often associated with consumption and the movement of goods.
- Revenue Sharing with States
- Although taxes like income tax and wealth tax are collected by the central government, a portion of the tax revenue is shared with state governments based on established provisions in the Constitution. This sharing of tax revenue

ensures that states have the necessary resources to carry out their responsibilities, such as public services, infrastructure development, and welfare programs.

- The direct tax revenue of state governments typically includes the **state's share of income tax** (a portion of the total income tax collected), **estate duty**, and **land revenue**, among others. States also levy their own taxes, such as **property tax** and **sales tax**, to fund their operations.

Self-Check Exercise-1

Q.1 What is distinction between taxes and penalities?

Q.2 What is Gift Tax?

15.3 Indirect Taxes (Before 2017)

After covering the various types of direct taxes, which serve as a key source of revenue for the Central Government, we now turn our attention to **indirect taxes**. The Indian tax system places significant emphasis on indirect taxes, which contribute approximately 83% of the total revenue.

Indirect taxes encompass a wide range of taxes, including **sales tax**, **excise duties**, **entertainment tax**, and **customs duties**, among others. A major reason for the growing contribution of indirect taxes is that, given the increasing financial needs of the government, it is often simpler and quicker to adjust and implement indirect taxes compared to direct taxes.

Customs Duty

Customs duties are taxes imposed on goods crossing the border, either entering (import duties) or leaving (export duties) a customs area. Import duties apply to goods entering the country, while export duties are levied on goods being exported.

There are three broad categories of customs duties — **import duties**, **export duties**, and **cesses on exports**.

(i) **Import Duties**: These duties are determined based on the rates specified in Schedules I and II of the Indian Tariff Act of 1934. The Act outlines various import duties on different commodities, with luxury goods often carrying higher duties to deter their import, while essential goods face lower rates.
In 1990-91, the estimated customs revenue was Rs. 20,800 crore, and Rs. 26,410 crore in 1991-92, with some revisions based on changes under the Finance Act of 1990. The revised estimate for 1990-91 was slightly lower, reflecting decreased revenue from specific imports, like electrical machinery and motor vehicles, although this was offset by higher import duties on petroleum products and machine tools.

(ii) **Export Duties**: Initially, export duties were primarily introduced to generate revenue. After World War II, their role expanded to include regulating domestic prices and shielding domestic markets from global inflation.
Historically, export duties formed a substantial share of indirect taxes, especially when India enjoyed a near-monopoly in certain commodities. However, as competition increased, these duties were progressively reduced and, by the end of the Third Plan, many were abolished. By 1966, export duties were reinstated on several products due to changing market dynamics. Over time, these duties have become less significant in the tax structure, particularly as excise duties gained prominence.
The revised estimate for export duty collections in 1990-91 was Rs. 1 crore, significantly lower than the original estimate of Rs. 6.15 crore, with a further reduction in the 1991-92 budget estimate.

Union Excise Duties

Excise duties are levies imposed on goods manufactured within the country. In India, excise duties are under the jurisdiction of the Union Government, except for items like alcoholic beverages and narcotics, which are taxed by the state governments.
Excise duties can be **specific** (charged per unit of the product) or **ad valorem** (calculated as a percentage of the product's monetary value).
The **Central Excises and Salt Act of 1944** governs most excise duties, and various commodities are grouped into 139 budget heads for taxation. However, several commodities are exempt from these duties.
In the fiscal year 1990-91, excise duty receipts were estimated at Rs. 24,500 crore, slightly below the original estimate due to reduced revenue from sectors such as petroleum and iron and steel.

Other Taxes and Duties

In addition to the major taxes outlined above, there are various smaller taxes such as **foreign travel tax**, **inland air travel tax**, **foreign exchange conservation tax**, and **water cess**, among others. These are grouped under a broader category of 'other taxes'.

(i) **Foreign Exchange Conservation Tax**: This tax is levied on individuals who draw foreign exchange for travel purposes abroad. The rate is set at 15% of the equivalent rupee value of the foreign exchange granted. Certain travel categories, including medical treatment and pilgrimages, are exempt from this tax.

(ii) **Foreign Travel Tax**: Introduced in 1971 and amended in 1989, this tax applies to passengers traveling abroad, with a fee of Rs. 300 for international journeys and Rs. 150 for travel to neighboring countries. A small percentage of the tax collection is paid to the carrier as a handling fee.

(iii) **Inland Air Travel Tax**: This tax, introduced in 1989, was initially levied at 10% of the basic air fare, but now it is imposed on the full fare amount.

(iv) **Water Cess**: Under the **Water Cess Act of 1977**, industries and local authorities are taxed for their use of water. The proceeds from this tax are deposited in the Consolidated Fund of India and then distributed to state water pollution control boards.

Indirect taxes also contribute to the revenue of state governments, which include their share of union excise duties, state excise duties, **general sales tax**, **motor vehicles tax**, **entertainment tax**, and other taxes.

NON-TAX REVENUE

Non-tax revenue for the Union Government comprises various sources, including administrative receipts and the net contribution from public sector undertakings, such as Railways, Posts and Telegraphs, and others. It also includes revenues from forests, irrigation, and electricity, among others.

Administrative Receipts include loans advanced by the Centre to states. As per the Ninth Finance Commission's recommendations, state plan loans were consolidated with an interest rate of 9%. The interest from these loans was estimated at Rs. 5,576.53 crore in 1990-91 and projected to rise to Rs. 6,789.5 crore in 1991-92. Interest on loans to Union Territories, such as the Union Territory of Pondicherry, was estimated at Rs. 16 crore in 1990-91, with a slight increase in 1991-92.

Interest Receipts from loans provided to public sector enterprises and other statutory bodies are also a part of non-tax revenue. These contributions come from a variety of sources, including port trusts, cooperatives, and other commercial undertakings.

India’s participation in the Special Drawing Rights (SDRs) system of the IMF also generates revenue, with a net cumulative allocation of SDR 327 million in 1990-91.

State governments, similar to the Union Government, also generate non-tax revenue through administrative receipts, contributions from public sector undertakings, and other grants.

Self-Check Exercise-2

Q.1 What are custom duties?

Q.2 What is estate duty?

15.4. SUMMARY

As mentioned earlier, direct taxes serve as a significant source of revenue for the Central Government. While some of these taxes are collected by the Union

Government, the proceeds are often shared between the Union and the states. The specific distribution arrangements will be discussed in Section 13.4 of this unit. For state governments, direct tax revenues typically include their share of income tax, estate duty, land revenue, urban property tax, and other related taxes.

15.5. GLOSSARY

• **Customs Duties**: These taxes are levied on goods that either enter (import duties) or leave (export duties) a customs zone.

• **Gift Tax**: This is a tax charged on gifts made by individuals, Hindu Undivided Families, and corporations, based on the value of the taxable gifts they provide during the year.

15.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 The key difference between taxes and penalties lies in their purpose. Taxes are primarily levied by public authorities to generate revenue, whereas penalties are intended to discourage certain behaviors or actions.

Q.2 The Gift Tax was introduced in India in 1958. It is levied on the value of gifts made by individuals, Hindu Undivided Families, and corporations during the year.

Self-Check Exercise-2

Q.1 These taxes are applied to goods that either enter (import duties) or leave (export duties) a customs zone.

Q.2 The Estate Duty was introduced in India in 1953. It was charged on the entire estate of a deceased person, covering all property that passed or was considered to pass upon their death.

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15.8. TERMINAL QUESTIONS

(a) Critically analyse Indirect Taxes before 2017.

(b) What are the non tax sources of revenue?

CHAPTER-16

TAX ADMINISTRATION : PART II

Structure

16.0 Introduction

16.1 Learning Objectives

16.2 Sharing of Receipts with States & Resource Mobilisation over the Years

Self-Check Exercise-1

16.3 Indirect Taxes after 2017: GST

Self-Check Exercise-2

16.4 Summary

16.5 Glossary

16.6 Answers to Self-Check Exercises

16.7 References/Suggested Readings

16.8 Terminal Questions

16.0 INTRODUCTION

The Goods and Services Tax (GST) is considered one of the most significant tax reforms since India's independence. It represents a transformative indirect tax change aimed at establishing a unified national market by eliminating barriers to interstate trade. GST has incorporated various indirect taxes that were previously imposed by both central and state governments.

Originally introduced in France in 1954, GST has now been implemented by around 160 countries worldwide over the course of 62 years. While many countries use a single GST model, Canada and Brazil have adopted a dual GST system. India, too, has chosen a dual GST structure, with the tax being levied simultaneously by both the central and state governments.

16.1 OBJECTIVES

After studying this unit, you should be able to:

- explain how revenue is shared with states; and
- outline the evolution of tax administration over time to understand the concept of GST.

16.2 SHARING OF RECEIPTS WITH STATES

The Indian Constitution adopts a quasi-federal structure, with a three-tier system of government: the central government, state governments, and local governments. Since local authorities fall under the jurisdiction of state governments, they are not granted independent taxation rights. To minimize conflicts between the central and state governments regarding tax matters, the Constitution includes specific provisions.

1. Taxes are divided so that no single tax can be levied by both the central and state governments. For instance, customs duties and corporate taxes are under the central government, contributing significantly to its tax revenue (approximately 50%). States are empowered to levy taxes like sales tax, land revenue, state excise duties, and entertainment tax to fund their activities.
2. Certain taxes are imposed by the central government, but the revenue is shared between the central and state governments. These include union excise duties and income taxes, excluding agricultural income. The Finance Commission determines the basis for dividing these revenues.
3. Some taxes are solely levied by the central government, but the proceeds are distributed to states. These include estate duties on non-agricultural property, railway freight duties, and terminal taxes on goods and passengers. Additionally, stamp duties (outside the Union list) and excise duties on items like drugs and cosmetics are collected by the state, even though they fall under central jurisdiction.

The need for decentralization is essential for fostering local initiative, enhancing decision-making speed, and increasing administrative efficiency. This decentralization approach allows for tailored solutions to diverse regional needs and ensures resource mobilization in line with a national vision. This framework is in harmony with the federal nature of India's Constitution.

According to 1991-92 budget, current situation of sharing of receipts with states is as

Table 3

Tax Revenue

Budget 1990-91		**Revised 1990-91**	**Budget 1991-92**
Total Tax Revenue	59,778.57	58,916.01	66,217.73
Less states share:			
Taxes on income	4,064.31	4,120.48	4,467.91
Union Excise Duties	10,361.44	10,414.00	11,175.47
Total States Share	14,425.75	14,534.91	15,643.38
Less : Transfer of Union territory taxes and duties to local bodies	58.83	63.25	79.43
Centre's Net Tax Revenue	45,293.99	44,317.85	50,494.92

Source : Budget 1991-92

There is often tension between the financial transfers made according to the Finance Commission's recommendations and those made by the Planning Commission. To resolve this issue, the Finance Commission should be established as a permanent statutory body, with its role and functions expanded through constitutional amendments.

Revenue transfers from the Centre to the states should align with economic considerations, administrative efficiency, and practicality, ensuring that a national minimum standard of living is met. An effective approach to achieving this is to redistribute resources from wealthier to poorer states. In this process, factors such as population, climate, rainfall, and the state of economic development should be considered.

The central government should refrain from offering direct loans to states. Instead, state governments should be encouraged to raise funds by borrowing directly from the public, to the extent possible.

A notable issue in recent times concerning the Centre-State financial relationship is the use of unauthorized overdrafts by states from the Reserve Bank of India. This is often driven by temporary cash flow issues and long-term imbalances between state responsibilities and available resources. Additionally, the repayment of past loans, along with interest, has placed a significant strain on state budgets. Many projects that states have funded through borrowing from the Centre have not generated the expected returns, making it necessary to address inefficiencies in public sector initiatives. Some non-plan loans have become burdensome debts that need to be reconsidered.

A thorough review and adjustment of Centre-State financial relations is necessary. States must learn to operate within their financial limits while maximizing their resource utilization.

RESOURCE MOBILISATION OVER THE YEARS

India has made significant progress in tax collection over the years. When the planning process began in 1950-51, the ratio of Tax-Net to National Product (NNP) was just 6.4%. Since then, it has steadily increased and currently stands at around 25%. This achievement is particularly impressive for a developing nation like India, which began with a low per capita income and has grown at a modest rate (approximately 1% annually in NNP per capita). By international standards, India's success in generating tax revenue is commendable. Most of India's major taxes, except for personal income tax and land revenue, have shown growth rates greater than unity. In recent years, the buoyancy of excise duties and sales tax has reached 1.51% and 1.41%, respectively, leading to a more efficient mobilization of resources through taxation. There remains potential to raise additional tax revenue, particularly if agricultural incomes, currently outside the tax net, are taxed.

In addition to tax revenues, resource mobilization involves generating non-tax revenues, reducing current government expenditures, and increasing surpluses from public sector enterprises.

In the 1990-91 budget, additional measures were anticipated to generate Rs. 1,790 crore, of which Rs. 550 crore would come from direct taxes and Rs. 1,240 crore from indirect taxes. The states' share of the additional resource mobilization, after accounting for the Rs. 170 crore loss due to income tax concessions, was estimated at Rs. 3 crore.

The Railway Budget for 1990-91 proposed hikes in goods traffic rates, passenger fares, and parcel rates, with an expected additional revenue of Rs. 892 crore. Increases in postal and telecommunications tariffs were expected to add Rs. 645 crore. Combined, these revisions were projected to generate an additional Rs. 3,327 crore in revenue.

Central government public enterprises saw a substantial increase in net profits, rising from Rs. 2,994 crore in 1985-89 to Rs. 3,782 crore in 1989-90. The rate of return, measured by net profits to capital employed, increased to 4.5% in 1989-90, the highest in the decade. However, the majority of these profits, Rs. 2,900 crore, came from the petroleum sector, while the non-petroleum sector contributed only Rs. 882 crore. Despite this improvement from the previous year's profit of Rs. 430 crore, the return on capital in non-petroleum enterprises was a mere 1.3% in 1989-90. This highlights a significant opportunity for improving financial performance in non-petroleum sectors. In the first half of 1990-91, Central Government public enterprises made a net profit of Rs. 481 crore, compared to Rs. 1,103 crore in the same period of the previous year.

The Seventh Plan aimed to generate Rs. 23,013 crore in internal resources and Rs. 11,490 crore through additional resource mobilization at 1984-85 prices to finance plan expenditures. In reality, public enterprises generated gross internal resources of Rs. 37,715 crore at current market prices, with approximately 32% of central public enterprise investments funded by net internal resources during the Seventh Plan period.

While the outlook for resource mobilization is challenging, it is not insurmountable. The resource imbalances accumulated over time cannot be fixed quickly. In the current context, soft options have limited or no impact on addressing macroeconomic imbalances. Measures introduced in 1990-91, aimed at improving revenue collection and reducing public expenditure, have had modest effects, as evidenced by the revised budget deficit being significantly higher than initially estimated. To address this, the government must take decisive actions, such as strictly controlling expenditure, particularly non-plan and revenue expenditures, rationalizing subsidies to better target the poor, and improving revenue collection. Ongoing efforts could lay the foundation for a more sustainable resource mobilization framework in the coming years.

Self-Check Exercise-1

Q.1 Apart from tax revenue other important aspects of resource mobilisation are generation of non-tax revenues, restricting of current government expenditure and raising of surpluses of public sector enterprises. True/False

Q.2 The devolution of revenues from centre to states should be in conformity with economy, administrative convenience and efficiency. True/False

16.3 Indirect Taxes (After 2017): Introduction and Overview of GST

GENESIS OF GST IN INDIA

2004: The concept of GST was introduced in India following the recommendations made by the Kelkar Task Force.

2007: During the presentation of the Union Budget (2007-08), Finance Minister Shri P. Chidambaram announced that GST would be implemented in India.

2014: The NDA government introduced the Constitution (122nd Amendment) Bill, which was a step toward the implementation of GST.

2016: The President of India granted assent to the Constitution (101st Amendment) Act on 8th September, 2016, formally clearing the path for the implementation of GST in the country.

2017 (March): The Central Goods and Services Tax Bill, 2017, the Integrated Goods and Services Tax Bill, 2017, the Union Territory Goods and Services Tax Bill, 2017, and the Goods and Services Tax (Compensation to States) Bill, 2017 were introduced and passed in the Lok Sabha. These bills received the President's assent on 12th April, 2017. Following this, individual states enacted their own respective GST laws.

2017 (July): GST was officially rolled out across India, effective from 1st July 2017.

CONSTITUTIONAL AMENDMENT FOR GST

The Constitution (101st Amendment) Act, 2016, was enacted on 8th September 2016, bringing about several important changes:

Both Parliament and state legislatures now have concurrent powers to create laws regarding the taxation of goods and services.

GST will be applicable on all goods and services, with the exception of alcoholic liquor for human consumption.

Parliament has the exclusive authority to legislate on the goods and services tax concerning inter-state supply (i.e., movement of goods or services between states).

The Parliament is responsible for determining the principles regarding the place of supply and the occurrence of supply during inter-State trade and commerce.

As per the explanation to Article 269A of the Constitution, the import of goods and services will be regarded as a supply under inter-State trade and commerce.

For certain items, Central Excise duty will apply to their production, while respective states will impose sales tax on their sale. These items include:

Petroleum crude

High-speed diesel

Motor spirit (commonly known as petrol)

Natural gas

Aviation turbine fuel

Tobacco and tobacco products

Article 279A of the Constitution empowers the President of India to form the Goods and Services Tax (GST) Council, chaired by the Union Finance Minister. This council is responsible for advising on various aspects of GST, including:

The GST rate

Valuation and fundamental rules

Exemptions

Future modifications

Returns and registration\

LEGISLATIVE FRAMEWORK

India has a total of 35 GST-related Acts, which include:

The Central Goods and Services Tax (CGST) Act, 2017: This Act imposes CGST on the intra-State supply of goods and services.

31 State Goods and Services Tax (SGST) Acts, 2017: These Acts enable each state to impose SGST on the intra-State supply of goods and services.

The Union Territory Goods and Services Tax (UTGST) Act, 2017: This Act applies to five Union Territories without their own legislative assemblies (Andaman and Nicobar Islands, Lakshadweep, Dadra and Nagar Haveli, Daman and Diu, and Chandigarh), allowing for the levying of UTGST on goods and services supplied within these territories.

The Integrated Goods and Services Tax (IGST) Act, 2017: This Act governs the levy of IGST on inter-State transactions involving the supply of goods and services.

The Goods and Services Tax (Compensation to States) Act, 2017: This Act was introduced to levy GST Compensation Cess for compensating states for any revenue loss they incur due to the implementation of GST.

STRUCTURE OF GST

GST is applied on the supply of goods and services throughout India, including Jammu and Kashmir. It is a unified tax that covers all stages of the supply chain, from the manufacturer to the consumer. Under GST, taxpayers can offset taxes paid at earlier stages against the output tax.

GST is a destination-based consumption tax, meaning that the tax revenue (whether CGST, SGST, or UTGST) will go to the state where the goods or services are consumed.

Both the Centre and the States will impose taxes on goods and services at the same time. The Centre can now tax goods sales within a state, while states are authorized to tax services.

(1) Intra-State Supply of Goods and Services:

CGST: Payable to the Central Government.

SGST/UTGST: Payable to the respective State Government/Union Territory.

(2) Inter-State Supply of Goods and Services:

IGST: Payable to the Central Government.

The Centre will be responsible for administering CGST and IGST, while individual states and Union Territories will manage SGST and UTGST.

Imports will be treated as inter-state transactions, and IGST will be charged along with basic customs duties.

Exports are treated as zero-rated supplies under GST, meaning no IGST is charged.

GST is applied at the following rates: 0.5%, 3%, 5%, 12%, 18%, and 28%. Additionally, a compensation cess is levied on certain goods such as pan masala, coal, aerated drinks, and motor cars. There are no Education cess, Swachh Bharat cess, or Krishi Kalyan cess under GST.

GST is calculated based on the transaction value of goods or services supplied, with certain exceptions.

Suppliers making taxable supplies are required to register under the GST law.

Registered entities are entitled to claim credits for input tax paid, which can be offset against the output tax, subject to specific rules:

IGST: First used to pay IGST; any remaining balance can be applied to CGST or SGST/UTGST.

CGST: First used for CGST, with any balance applied to IGST.

SGST/UTGST: First used for SGST/UTGST, with any balance applied to IGST.

The GST system facilitates seamless credit flow for inter-state supplies, a feature not available in the pre-GST era. Under the new system:

The supplier in the exporting state can use credits of IGST, CGST, and SGST/UTGST to pay the IGST on inter-state supplies.

The buyer in the importing state can claim credits for the IGST paid on purchases against their output tax.

The exporting state transfers the SGST/UTGST credit used for paying IGST to the Centre.

The Centre transfers the IGST credit used for SGST/UTGST payment to the importing state.

A common platform has been established to verify claims and transfer funds between the Central and State Governments. The GST Electronic Portal (www.gst.gov.in) managed by the Goods and Services Network (GSTN) offers several services for taxpayers, including:

Registration facilitation.

Return forwarding to the relevant authorities.

IGST computation and settlement.

Matching tax payment details with the banking network.

Analysis of taxpayer profiles.

BENEFITS OF GST

GST offers multiple advantages for all involved parties, including businesses, government, and consumers. It is expected to lower the cost of goods and services, enhancing their competitiveness on a global scale. The key benefits of GST are outlined below:

- **Creation of a Unified National Market**: GST aims to transform India into a unified market with standardized tax rates and processes, removing economic barriers and creating a more integrated national economy.
- **Reduction of Cascading Effects**: By consolidating most of the central and state indirect taxes into a single tax system, GST eliminates the "tax on tax" effect. This allows businesses to claim tax credits for taxes paid on earlier stages of the production process, benefiting the industry by reducing costs.
- **Support for the 'Make in India' Initiative**: GST provides a significant boost to the government's 'Make in India' program, making domestically produced goods and services more competitive in both local and global markets.
- **Increase in Government Revenue**: By expanding the tax base and encouraging better compliance, GST is expected to enhance government revenue over time.

SELF-CHECK EXERCISE-2

Q.1 Centre and states will impose tax on goods and services simultaneously. Centre now can impose tax on sale of goods within State and States can impose tax on services. True/False

Q.2 The idea of GST was emerged in India from the recommendation of Kelkar Task Force. True/False

16.4. SUMMARY

The direct taxes mentioned earlier serve as a primary source of revenue for the Central Government. While the Union Government collects certain taxes, a portion of the revenue from these taxes is shared with the states. On the other hand, the direct tax revenues for State governments include their share of income tax, estate duty, land revenue, urban property taxes, and others.

16.5. GLOSSARY

Custom duties: These are taxes applied to goods that either enter (import duties) or leave (export duties) a customs territory.

Gift Tax: This tax is levied on gifts given by individuals, Hindu Undivided Families, or Corporations, based on the value of taxable gifts provided during the year.

16.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

16.7. REFERENCES/SUGGESTED READINGS

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15.8. TERMINAL QUESTIONS

(a) Critically analyse Indirect Taxes after 2017.

(b) Discuss the GST in detail.

Chapter-17

PRINCIPLES OF TAXATION

Structure

17.0 Introduction

17.1 Learning Objectives

17.2 Role Of fiscal system In Economic Development

Self-Check Exercise-1

17.3 Main Aspects of India’s Tax Structure

Self-Check Exercise-2

17.4 Summary

17.5 Glossary

17.6 Answers to Self-Check Exercises

17.7 References/Suggested Readings

17.8 Terminal Questions

17.0. INTRODUCTION

In India's federal financial structure, there are three levels of government, each with distinct areas of responsibility and revenue sources. These levels include:

The Central (Union) Government

The State Government

The Local Government

17.1 LEARNING OBJECTIVES

After going through this lesson, the students will be able to

- Know he role of fiscal system in economic development

- Know the main aspects of tax structure of India

17.2 ROLE OF FISCAL SYSTEM IN ECONOMIC DEVELOPMENT

The core of a fiscal system lies in managing the financial affairs of the government. This involves: (i) assessing the financial needs of the State, (ii) determining how to generate revenue, and (iii) overseeing the allocation and effective use of funds to meet the State's goals. The fiscal system primarily focuses on: (a) generating revenue, and (b) government spending. These aspects are consolidated in a document known as the budget. Whether at the union, state, or local level, the budget reflects the projected financial receipts (as well as the actual receipts from the previous year) and their distribution (along with the actual expenditure from the prior year). It breaks down the relationship by various departments, programs, and initiatives. As such, the budget plays a crucial role in economic planning and policy formulation.

OBJECTIVES OF BUDGETARY POLICY

In a developing economy, fiscal policy, or budgetary policy, plays a crucial role in shaping economic progress. Its primary objectives include: (i) fostering economic growth by encouraging productive investments in both public and private sectors; (ii) generating optimal resources for investment while considering the returns on those investments, with the aim of increasing both marginal and average savings rates within the economy; (iii) ensuring a level of economic stability necessary to achieve sustainable growth; and (iv) redistributing the national output to promote balanced development across regions.

LIMITATIONS OF BUDGETARY POLICY

Several factors can hinder the successful implementation of budgetary policy objectives in a developing economy. Key challenges include: (a) the inflexibility and limited scope of the tax structure, which makes it difficult to create a cohesive and integrated tax policy; (b) the absence of accurate and reliable data on income, spending, savings, investment, and employment, complicating the task for public authorities in formulating an effective budgetary strategy; and (c) insufficient administrative infrastructure to properly collect revenues and ensure their efficient allocation and use.

UNION FINANCES

The annual budgets serve as the foundation for analyzing government finances. In this section, we will briefly discuss: (i) the key components of the budget, (ii) the different types of deficits in budgeting, and (iii) the trends observed in India's Union Budgets.

COMPONENTS OF UNION BUDGET

The Union Government's budget is categorized into two sections: (i) the revenue budget and (ii) the capital budget. The revenue budget includes recurring items, while the capital budget focuses on the acquisition and disposal of capital assets. Each budget has two main components: receipts and expenditures.

Receipts in the revenue budget include items that do not require repayment, such as tax revenue and surpluses. On the other hand, receipts in the capital budget mainly comprise internal and external borrowings, net of repayments, as well as loan recoveries and proceeds from asset sales.

Expenditure in the revenue budget is classified into development and non-development categories. Development expenditure involves spending on social and community services (like education and healthcare) and economic services (such as agriculture, industry, and infrastructure). Non-development expenditure covers administrative costs, defense, and interest payments on public debt.

In general, revenue expenditure is focused on maintaining existing services, while capital expenditure is aimed at acquiring assets or expanding services. Ideally, a revenue surplus should be generated to fund capital expenditures.

CONCEPT OF DEFICIT

In a budget, there are three types of deficits: (i) revenue deficit, (ii) budgetary deficit, and (iii) fiscal deficit.

A revenue deficit occurs when there is a shortfall between the revenue receipts and the revenue expenditure. The budgetary deficit is calculated as the difference between the total of revenue receipts and capital receipts, and the sum of non-plan and plan expenditures.

A fiscal deficit is defined as the difference between the total expenditure (which includes both plan and non-plan expenditures) and the combined value of revenue receipts plus non-debt capital receipts. This indicates the total borrowing required by the government to meet its overall expenditure needs.

The fiscal deficit can be further divided into two components: primary deficit and interest payments. The primary deficit reflects the difference between the fiscal deficit and the government's interest payments. Additionally, the primary deficit can be broken down into revenue deficit and capital deficit. The primary deficit related to revenue would be equal to the revenue deficit minus interest payments, while the primary deficit related to capital would be calculated as capital expenditure minus loan repayments.

STATE FINANCES

State finances, like Union budgets, have also witnessed a growing trend in revenue deficits. In response to this, both the Union and State governments have devised a strategy to address the fiscal challenges faced by the states. This approach involves a combination of financial assistance provided by the central government and a structured time-bound plan for implementing medium-term fiscal reforms by each state.

These programs include several key measures aimed at improving fiscal health, such as:

- Reducing non-plan revenue expenditure by downsizing government staff wherever feasible.
- Implementing pricing and subsidy reforms to ease the fiscal burden on the state while enhancing allocative efficiency.
- Introducing institutional reforms to improve the effectiveness of public service delivery.
- Minimizing the government's involvement in non-essential areas through decentralization, disinvestment, and privatization.
- Establishing an Incentive Fund to encourage the states to adopt fiscal reforms.
- Creating a model fiscal responsibility framework for states, which most states have since adopted, providing flexibility to tailor specific details.
- Introducing a debt swap program to help states retire high-cost debt by utilizing small savings and market loan initiatives.

Self-Check Exercise-1

Q.1 A debt swap initiative was introduced to allow states to pay off expensive debt by using small savings and market loan options. True/False

Q.2 A revenue deficit refers to the gap between the revenue receipts and revenue expenditure. True/False

17.3. MAIN ASPECTS OF INDIA'S TAX STRUCTURE

The key features of India’s tax system can be summarized as follows:

- **Rising Significance of Tax Revenue**: Tax revenue from both the Central and State Governments has grown substantially, from Rs. 460 crore in 1951-52 to Rs. 10,17,107 crore in 2008-09, with an average annual growth rate of 13.9%. However, the proportion of total revenue from taxes has decreased from 88.6% in 1951-52 to 84.1% in 2008-09. This suggests either a reduced reliance on tax revenue or a faster rise in non-tax revenue sources. Given the overall growth in tax collection, the latter inference seems more probable. Additionally, the percentage of national income derived from tax revenue has consistently risen.
- **Tax Revenue as a Share of GDP**: The tax-to-GDP ratio increased from 6.7% in 1950-51 to 19.2% in 2008-09. While this is a notable increase, it remains lower than the 25-45% range observed in developed nations. However, considering India's status as a low-income country, a tax-to-GDP ratio of around 20% can place a significant burden on its population. This makes understanding the structure of the tax system crucial.

- **Tax Structure**: Taxes are broadly categorized into **direct taxes**, such as income, corporate, and wealth taxes, and **indirect taxes**, such as VAT, service tax, excise duties, and import duties. Over time, the Indian tax system relied more on indirect taxes, as they allowed for broader collection. However, recent reforms aimed at simplifying the tax structure have led to a reduction in the share of indirect taxes, with a focus on improving tax administration and compliance.
- **Shift in the Importance of Taxes**: Over the years, there has been a shift in the relative importance of different taxes. In the 1950s, corporate and income taxes were major sources of revenue for the Union government, but excise and customs duties gradually gained prominence. Similarly, at the State level, sales tax replaced land revenue as the primary source. This shift reflected changes in the economy due to industrialization and export growth. Following economic reforms in the 1990s, personal income and corporate taxes have regained importance, while customs and excise duties have declined.
- **Progressive Tax System**: India's tax structure has been designed to be progressive, ensuring that those with higher income or wealth contribute more. The direct tax system has evolved to account for factors such as a service-driven economy, the rise of small businesses, industrialization, and a growing taxpayer base. In indirect taxes, consumption of luxury goods is taxed more heavily, targeting wealthier individuals. Taxation, therefore, serves not only as a revenue source but also as a tool for achieving socio-economic objectives.

EVALUATION OF THE TAX SYSTEM

The evaluation of India's tax system can be approached through four essential criteria, which are crucial for achieving the goals of planned economic development:

1. **Adequacy and Productivity**: In contrast to earlier periods, India's tax system has shown notable growth in recent years, with tax revenue steadily increasing alongside national income. However, despite this positive trend, the increase in tax revenue has not been sufficient to meet the growing needs of the developing economy.
2. **Efficiency**: The Indian tax system does not fully meet the efficiency standard. The complexity of laws and frequent changes to their provisions have led to a loss of simplicity and predictability in the tax structure. This has contributed to widespread tax evasion and avoidance, generating significant black money and causing distortions in both the economy and the sociopolitical landscape. Furthermore, taxpayers face high costs in compliance.
3. **Equity**: The tax system also falls short in terms of equity. While direct taxes are relatively progressive, the heavy reliance on indirect taxes undermines this progressivity. The exemption of agricultural income from taxation has further compounded inequities. Additionally, the unorganized sector, which has

expanded over time, remains largely outside the tax net, contributing to further imbalance.

4. **Certainty**: The Indian tax system has been subject to frequent changes, leading to instability. Constant revisions in tax exemptions, incentives, and concessions have resulted in uncertainty for both taxpayers and the government. Additionally, the goals of taxation have evolved over time. Initially, the focus was on broadening the tax base by increasing the number of taxes, but more recently, the focus has shifted towards reducing tax multiplicity and eliminating overlapping laws. Similarly, indirect taxes on commodity inputs were previously higher and more widely applied.

17.4 Summary: Currently, the focus of indirect taxes has shifted towards minimizing the cascading effects of taxation. A significant change in the tax approach in recent years is the shift in priorities from the primary goal of "avoiding concentration of income and wealth" to an emphasis on promoting thrift, productivity, and wealth accumulation. This marks a departure from the earlier approach. In the area of corporate taxation, there is also a tendency towards ad-hoc decisions. While the motives behind these changes are often positive, the frequent and sudden adjustments to tax policies should be replaced with a more stable and predictable system to ensure long-term consistency in tax administration.

Self-Check Exercise-2

Q.1 The aim of indirect taxes is to prevent the cascading impact of taxes. True/False
Q.2 The Indian tax system does not meet the efficiency standard due to its complex laws and frequent changes, which have undermined simplicity and certainty. True/False

17.5. GLOSSARY

- **Audit :** Examination of accounts with a view to determining their correctness.
- **Auditor :** Officer who are responsible for Audit.
- **Extravagance :** Over Expenditure

17.6 ANSWERS TO SELF-CHECK EXERCISES

Self-Check Exercise-1

Q.1 True

Q.2 True

Self-Check Exercise-2

Q.1 True

Q.2 True

17.7. REFERENCES/SUGGESTED READINGS

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17.8. TERMINAL QUESTIONS

(a) Discuss the various priniciples of tax administration in India.

Chapter-18

PARLIAMENTARY CONTROL OVER FINANCE

Structure

18.0. Introduction
18.1. Learning Objectives
18.2. Legislative Control & Financial Control
Self-Check Exercise-1
18.3. Committees to Ensure Parliamentary Control
Self-Check Exercise-2
18.4. Summary
18.5. Glossary
18.6. Answers to Self-Check Exercises
18.7. References/Suggested Readings
18.8. Terminal Questions

18.0. INTRODUCTION

Parliament is called upon to vote large sums of tax payer's money from time to time. It authorises the Government through the Appropriation Act to draw money from the Consolidated Fund and spend them as per the budgetary allocations. In the interest of taxpayers, it is expected that Parliament should satisfy itself that the moneys so voted are directed for the purposes intended and are spent prudently and economically.

It may be noted that the efforts of the administration itself can ensure efficiency and economy. But under the present set up of administration as it is here is a necessity to have some agency of the House itself to, assure it that its wishes are carried out, that Government is conducted honestly and faithfully, and that where business is not transacted efficiently, there is a fair chance that notice will be taken off. It is neither necessary nor practicable to defect every inefficient or unwise action, even if it was possible to say accurately on every occasion what is inefficient or unwise. But the House, through its own agency, as J. S. Mill long ago contended, is expected "to watch and control the Government to throw the light of publicity on its acts, to compel a full exposition and justification of all of them which any one considers questionable, to censure them if found condemnable."

Effective financial control involves scrutiny of the details of estimates and accounts. The Houses of Parliament, constituted as they are, though anxious to exercise rigid and reasonable control, are not suitable organs for going into such minute details. Neither House has the time or facilities for detailed examination of such complex and technical documents. Accordingly it has been felt necessary to delegate these duties, subject to their final control, to committees, estimated with the task of examining whether or how a process is being performed, and "by their conduct of this task they serve to provide the means of some sort of control over the carrying out of the process.

Dr. Subhash C. Kashyap has pointed out that it is the duty of Parliament to review and approve the government's proposals for taxation and expenditure estimates. Despite the fact that nearly two months of the Budget Session are dedicated to this task, the discussions often lack depth and thoroughness. In an effort to address all matters, the debates often become general, repetitive, and formal. With limited time, discussions on several Ministries or Departments may not even take place, and the "guillotine" procedure is sometimes applied. This is where the Finance Committees of Parliament step in, undertaking a more detailed examination of government spending and performance to ensure accountability in financial matters.

The execution of a policy is more critical than its mere formulation. Without proper implementation, a policy may fail to achieve its intended objectives due to inefficiency or poor organizational structure. Therefore, it is essential to have bodies in place that scrutinize the practical application of policies, assessing the performance of government organizations in terms of both efficiency and economy. Administrative systems are not immune to issues like misuse of power, negligence, delays, indifference, and nepotism. It is difficult to assess these problems without comprehensive research and methodical inquiry into the practices of the concerned officials and ministries.

The Financial Committees play a crucial role as the overseers of Parliament. What sets them apart is their direct interaction with civil servants, which makes their control over the administration more continuous and thorough. These committees utilize a variety of tools, such as issuing questionnaires, obtaining memoranda from representative non-governmental organizations and experts, conducting on-site studies, and holding informal discussions, to scrutinize government actions.

The three primary Financial Committees of Parliament—(1) The Estimate Committee, (2) The Public Accounts Committee, and (3) The Committee on Public Undertakings—are instrumental in uncovering inefficiencies and waste in the implementation of policies and programs. Their recommendations are designed to improve administration, ensuring policies and programs are executed economically, efficiently, and quickly. Through their constant vigilance, these committees keep the administration in check and drive improvements in the execution of public initiatives.

Some of the fundamental features of parliamentary 'government are: (a) representative democracy on the basis of a broad base franchise, (b) parliament as the focus of power in the political system, (c) collective responsibility of the executive to the legislature, (d) pivotal role of the opposition in the scheme of government, and (e) political mentality of the head of state and that of civil service. The most significant characteristic of parliamentary government is the collective and the continuous responsibility of the cabinet to the directly elected those of the Parliament, and its continuation in office as long as it commands the support of the majority, in that House.

Article 75(3) of the constitution of India contains the following provision regarding the responsibility of the council of Ministers to Parliament. "The council of Minister shall be collectively responsible to the House of people." Despite this brief provision, it is clear that Indian legislative and executive apparatus is based on the parliamentary system of government and the parliamentary form of executive has been adopted in India it follows that a thorough grasp of the concept of parliamentary control over the executive and the nature, sphere and method of exercising such control is essential in understanding and the proper functioning of parliamentary government in India.

Modern governments are characterized by a phenomenal proliferation of states activities. The assumption by the state of welfare functions have resulted in an enormous increase in range and scope of governmental functions and responsibilities. The result of this growth in state activities has been a corresponding expansion in-administrative machinery and emergence of new political and administrative institutions. The spread of the modem welfare state and its activities are so vast and complex that the executive has also come to exercise far reaching functions of a quasi-judicial and legislative character. These developments have tended to upset the traditional balance between parliament and the executive and thrown into bold relief special problems in the process of parliamentary over executives.

The experience has shown that the working a parliamentary and welfare governmental has led parliamentary to conflict itself to the broad framework of policy. In the sprawling area of administration, parliamentary control has taken the form of export fact to supervision and control. The control of Parliament over the executive can be divided into the following categories:

a) Legislative Control;

b) Financial Control

c) General control over the policies and actions of the executive; and

d) Control over cabinet and administration.

In this lesson, we will be first concentrating on one aspect of control of Parliament over the executive, i.e. financial control.

18.1. LEARNING OBJECTIVES

After studying this lesson, the learner will be able:

- To understand about Parliamentary Control over Finance.
- To comprehend about evolution, composition, functions and procedure of Public Account Committee.

- To discuss about composition, function and methods of working of Estimate Committee.
- To describe composition, function and utility of the committee on Public Understating.

18.2 FINANCIAL CONTROL

One of the important ways in which Parliament "controls the executive is through its control on the exchequer. Parliamentary powers and procedures in this respect are defined by the constitution itself. Article 113(2) states that all the estimates other than these related to the expenditure, charged on the Consolidated Fund of India "shall be submitted in the form of demands for grants to the House of People and the House of People shall have power to assent, or to refuse to assent, to any demand subject to a reduction, of the amount specified therein." Parliament has the power both to grant supplies and control taxation and appropriations and to be assured that the appropriations are spent by the executive for purposes for which they are granted.

The Public Accounts Committee, the Estimate Committee and Committee on Public Undertakings make a detailed examination of the accounts and estimates of the ministers of Government of India and of the Public Undertakings and submit their reports to Parliament.

SELF CHECK EXERCISE-1

Q.1 The Public Accounts Committee (PAG) is the oldest financial Committee. As early as 1923, a PAC was set up by the Central Legislative Assembly. True/False

Q.2 The PAC is now constituted by members drawn from both houses of Parliament, it consists of 30 members (15 from Lok Sabha arid 15 from Rajya Sabha). True/False

18.3. VARIOUS COMMITTEES TO ENSURE PARLIAMENTARY CONTROL

The Public Accounts Committee (PAG) is the oldest financial Committee. As early as 1923, a PAC was set up by the Central Legislative Assembly. Consequently, the committee set of well established traditions.

Evolution

The PAC was set up under the Montage Chelmsford Reforms, 1919 in the year 1923. It functioned for three decades before it become a full-fledged Parliamentary Committee to be served by the Secretariat of Parliament. The Committee was to consist of elected members only from the year, consisted of elected members only from the year 1950. Till then it was a product of rules by the Governor-General-in-Council-with the sanction of Secretary of Slate. The Act of 1935 made a specific provision that the Accounts and Audit Report there on should be placed before the legislature. The Rules of Procedure then provided for the appointment of a PAC, to examine the Accounts and Audit Reports. The- constitution of India provides that the reports of the Comptroller and Auditor General (CAG) of India relating to the accounts of the Union shall be submitted to the President, who shall cause them to be laid before each House of Parliament and the Parliament has continued to constitute a PAC to scrutinize these reports.

Composition

The Public Accounts Committee (PAC) is currently composed of members from both houses of Parliament, with a total of 22 members (15 from Lok Sabha and 7 from Rajya Sabha). Before 1954, the committee had only 15 members, all of whom were elected from Lok Sabha. The PAC operates under the oversight of the Speaker of Lok Sabha. Members are selected through a proportional representation system, using a single transferable vote. Ministers are excluded from eligibility, and the term of each member lasts for one year. Since 1967, it has been a common practice to appoint a member from the opposition as the committee's Chairman.

Functions:

The primary responsibility of the PAC is to review the accounts of the government across all its financial transactions. Specifically, the committee scrutinizes the appropriation accounts and the reports of the Comptroller and Auditor General (CAG). It must ensure that:

- The funds disbursed are legally available and applied to the intended service or purpose.
- The expenditures comply with the governing authority.
- Any re-appropriations have been made in accordance with the relevant rules set by the competent authority.

The PAC is also tasked with reviewing:

a) The financial statements of state corporations, trading, and manufacturing entities, including their balance sheets and profit-and-loss accounts, as required by the President or under statutory regulations. The committee also looks at the CAG's report related to these entities.

b) The financial statements of autonomous and semi-autonomous bodies audited by the CAG under the President's directions or relevant legislation passed by Parliament.

c) Reports from the CAG in cases where the President directs the audit of specific receipts or the examination of accounts for stores and stocks.

If the government has spent more than the allocated amount for a specific service during a financial year, the PAC examines the circumstances that led to the excess expenditure. Based on the findings, it makes appropriate recommendations.

Procedure

The Committee works methodically. The Committee usually conducts its examination by putting questions to the witnesses. They cross examine the witness with full knowledge that they are extracting information from the official experts. The Chairman takes the major part in the conduct of committee's deliberations. The committee also appoints subcommittees to make any specific study of any problem.

On the basis of facts before it the committee formulates its findings and makes its recommendations and present them to the Houses of Parliament in the form of a report. A convention has been developed that the most of the recommendations are accepted by the Government and implemented.

Even through the Committee conducts a post mortem examination of the accounts after having been audited by CAG and the Auditor-General yet it has been serving a useful purpose by detecting cases of misappropriation and suggesting economics.

THE ESTIMATES COMMITTEE

The Estimates Committee came into being in 1950. Its predecessor was the Standing Finance Committee which was constituted in 1921. This committee depended on the will of the executive. It has no statutory status its functions were not clearly defined and its deliberations were not satisfying to the selected representations of the Legislative Assembly.

Composition

The Estimates Committee consists of not more than 30 members who are elected by Lok Sabha every year from the amongst its members according to the principle of proportional representation by means of the single transferable vote. The rules prohibits ministers from being members of the Committee. Another important feature of the Estimates Committee is that unlike the PAC. the members of Rajya Sabha are not associated on the ground that as the speaker explained. "Under: the Constitution the Rajya Sabha has no right to interfere with or cut down any item of budget.

Rule 258 provides that the chairman of a committee shall be appointed by Speaker amongst the member of the committee, if the Deputy Speaker is a member of committee, he shall be appointed automatically Chairman of the committee. It may be noted that while the chairman is nominated as in other committees, the members of the committee are elected by the House.

Functions

The functions of the Committee have been laid 'down in the rules of procedure and directions by the speaker issued from time to time. The rules here provide that the Committee shall examine in general, such of the estimates as may seem to be fit or as are specifically referred to it by the House or the speaker. In general the functions of the Committee are :

to report v/hat economics, improvements in organisation, efficiency or administrative reform, consistent with the policy underlying the estimates may affect;

to suggest alternative policies in order to bring about efficiency- and economy in administration, to examine whether the money is well laid out within the limits of the policy implied in the estimates; and

to suggest the form in which the estimates shall be presented to Parliament.

Method of Working

Once a decision is taken as to the estimates to be examined, the committee collects and collates material required for an adequate examination of the expenditure. It interviews officials, issue questionnaires to the concerned Ministries/Departments call witness, calls for papers, records and files, and so on. If the disclosure of any document is not in public interest, the matter is referred to the speaker for his guidance. The committee submits its reports to the house. The draft report is shown to the speaker before finalization.

The recommendations of the Estimate Committee relates to:

improving the organisation and working of the department;

effecting economy; and

general espects.

Based on the analysis made by the committee or the Study Group, a draft 'Action Taken Report' is prepared which consists of the following chapters :

1. The Repot.
2. Recommendations and suggestions, etc, agreed to by the executive government and implemented:
3. Recommendations where it has not been, possible, for the Ministry/Department to implement; for reasons; stated by them and which the Committee on reconsideration think should not be pressed.
4. Recommendations which the executive government is unable to accept for reasons given by them but which the committee feels should be implemented.

5. Recommendations on which final replies of the executive government have not been received.

The report after finalization is presented to the House and it is left to the House to r take any further actions may be thought necessary.

COMMITTEE ON PUBLIC UNDERTAKINGS

The Industrial Policy Resolution of 1955 gave a new orientation and meaning to the role of the state in Indians economic and industrial development. As a consequence of this resolution and the ideals of a welfare state embodied in the Directive Principles of State Policy, the Government has undertaken to speed up industrialization by developing and operating industrial enterprises.

The industrial development of the country is a talk to be implemented by executive, but Parliament exercise control on the operation and' progress of the public industrial enterprises through its power to sanction grants as well as through its Committee on Public Undertakings.

The Committee on Public Undertakings was established on May, 1964 and is the third financial committee of the Parliament.

Composition

The Committee consists of ten members from the Lok Sabha and five members from the Rajya 3abha elected by the respective Houses according to the principle of proportional representation by means of the single transferable vote; The chairman of the Committee is appointed by the Speaker. The term of office of the member is one year.

Functions

The functions of the Committee on Public Undertakings are :

to examine the reports and accounts of such public undertakings as have been specifically allotted to the committee for this purpose;

to examine the reports, if any, of the CAG on public undertakings;

to examine, in the context, of the autonomy and efficiency of public undertakings, whether the affairs of public undertakings are being managed in, accordance with sound business principles and prudent commercial practices, and

to exercise such other functions vested in PAC and the Estimates Committee in relation to the public undertakings specified' for the Committee as are not covered by clauses (a), (b) and (c) above and as may be allotted to the Committee by the speaker from' time to time.

Provided that the Committee shall not examine and investigate following matters :

(i) matters of major government policy as distinct from business or commercial functions of the public undertakings;

(ii) matters of day to day administration; and

(iii) matters for the consideration of which machinery is established by a special statute under which a particular undertaking is established.

The examination of the public undertakings by the Committee on Public Undertakings is, therefore, in the nature of evaluation of the performance of undertakings which covers all aspects," viz. implementation of policies, programmes, management, financial performance, etc.

Working of the Committee

At the beginning of the year, the committee decides upon the subjects or the undertakings proposed to be examined during the year. The examination by the Committee may be comprehensive or limited to the working of an undertaking which is considered to be topical interest. The chairman of the committee is authorised to ascertain full details of required information from the undertaking concerned without prior reference to the Committee.

The sources of information utilized by the Committee may be as follows:

1) preliminary and detailed information submitted by the Ministry/ Department or Undertaking concerned with the subject to be examined;

2) memoranda on the subjects under study submitted by non-official organizations such as chambers of, commerce, trade organizations, professional consultants, trade unions, etc;

3) evidence given by officers of the undertaking. Ministry/Department; and

4) audit reports (commercial) and the 'Memorandum of important Points submitted by the CAG.

The draft of the committee is sent to the undertakings, Ministry/Department, Ministry of finance and the CAG for factual verification. The report is finalized after the factual verification. The final report is submitted to the Parliament.

Utility

The Committee has rendered valuable service and secured effective accountability of the public undertakings to Parliament. The Government and the Public Undertakings have accepted a majority of its recommendations. The management has: acknowledged that the guidance given by the Committee through its recommendations has been helpful.

SELF CHECK EXERCISE-2

Q.1 A key responsibility of the Committee on Public Undertakings is to review the reports and financial records of public undertakings assigned to the committee for examination. True/False

Q.2 The Estimates Committee is made up of a maximum of 30 members, who are selected annually by the Lok Sabha from among its members using the system of proportional representation with a single transferable vote. True/False

18.4. SUMMARY

It can be observed that formal excellence of financial machinery is a prerequisite for smooth and harmonious operation of financial administration, the growth of the democracy and the consequent changes in the role of the government in the sphere of economic and social development which has resulted in an enormous growth in public expenditure. Financial control of Parliament over executive is one such tool with the help of which control over public expenditure can be exercised.

18.5. GLOSSARY

- **Apparatus :** The set of tools, instruments or equipments used for doing a job or as activity.
- **Fundamental** : Basic and important, from which everything else develops.
- **Proliferation :** The fact of something increasing a lot and suddenly in numbers or accounts.

18.6 ANSWERS TO SELF-CHECK EXERCISES

SELF CHECK EXERCISE-1

Q.1 True

Q.2 False

SELF CHECK EXERCISE-2

Q.1 True

Q.2 True

18.7. REFERENCES/SUGGESTED READINGS

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18.8. TERMINAL QUESTIONS

(a) What are the functions of the estimate committee?

(b) Describe about working of the committee on Public Undertaking.

AUDIT AND CAG: PART I

Structure

19.0. Introduction
19.1. Learning Objectives
19.2. Audit in India, Functions of an Auditor
Self-Check Exercise-1
19.3. The Comptroller and Auditor General of India & Independence of the CAG
Self-Check Exercise-2
19.4. Summary
19.5. Glossary
19.6. Answers to Self Check Exercises
19.7. Terminal Questions
19.8. References/Suggested Readings

19.0. INTRODUCTION

Audit plays a crucial role in ensuring effective financial management, particularly in allowing Parliament to maintain control over finances. It is employed worldwide to optimize the use of financial resources, with its scope and function varying across different nations. A robust audit system serves as a key safeguard, protecting against the misuse of public funds. There is no doubt that audit is an essential component of a modern democratic government, such as India's.

Audit means the examination of accounts with a view to determining their correctness and of the transactions they undertake to quickly know everything and understand the profit and; loss. According to James C. Charlesworth, Audit means the process of ascertaining whether the administration has spend or is spending its funds in accordance with the terms of the legislative instrument which appropriated the money' it is a systematic examination of the books and records of a business or other organisation in order to ascertain or verify and to report upon the facts regarding its financial operation and the results thereof.

19.1. LEARNING OBJECTIVES

After studying this lesson, this learner will be able:

- To understand about the Audit system and their obj ectives in Indi a.

- To understand the genesis of the office of CAG.
- To know about terms, conditions, power and functions of CAG.
- To analyze the relations of CAG and Public Accounts Committee.

19.2. AUDIT IN INDIA

OBJECTS OF AUDIT

The main objects of Government Audit are to ensure :

a) That there is provisions of funds for the expenditure duly authorized by competent authority;

b) That the expenditure is in accordance with the sanction properly accorded and it incurred by an officer competent to incur it;

c) That payment has, as a fact been made and has been made to proper person, and that it has been so acknowledged and recorded that a second claim against Government on the same account is impossible that the charge is correctly classified and that it a charge is debatable to the personal account' of a contractor, employee or other individual, or is recoverable from him under any rule of order, it is recorded as such in a prescribed account.

d) That in case of audit of receipts, (i) sums due are regularly recorded and checked against demand and (ii)-sums reviewed are duly brought to credit in accounts;

e) That in the case of audit of stores and stock, where priced with reasonable accuracy, and that the rates initially fixed are reviewed from time to time, correlated with market rates and revised when necessary;

f) That the' articles are counted periodically and otherwise examined for verification of the accuracy of quantity balances in the books and the total of the valued account taken with the outstanding amount in general accounts and that the numerical balance of stock materials is reasonable with the total of value to the various classes of stores; and

g) That expenditure conforms to the general principles which has been recognized as standards of financial property.

Audit in India

In India, the authority for auditing is derived from Articles 148 to 151 of the Constitution of India, as well as the Parliament Act of 1971 (Duties, Powers, and Conditions of Service Act) and its amendments in 1976. The main features of India's audit system are as follows:

1. **Integrated Audit**
   The Comptroller and Auditor General (CAG) of India oversees the audit of accounts not only for the Union Government but also for the States.
2. **Quasi-Independent Audit**
   Audit is not placed under any ministry at the Union or State level. The audit reports are submitted to Parliament and State legislatures through the President or Governor, respectively. While in the UK, the CAG's reports go directly to the House, the Indian system is not fully independent, but is considered quasi-independent.
3. **Unified Functions**
   Though the CAG is expected to carry out both audit functions, in practice, the role primarily focuses on auditing expenditures. Some departments are authorized to draw funds through cheques without CAG's approval, unlike the UK where the CAG oversees both receipts and expenditures, and no funds can be withdrawn from the Exchequer without his consent.
4. **Limited to Legal Compliance**
   India's audit system mainly ensures adherence to established rules and regulations, seldom expanding to assess propriety or performance. In contrast, countries like Sweden conduct comprehensive audits, evaluating government performance to inform the public and measure the nation's financial health.
5. **Field Offices Across the Country**
   The audit organization in India is not centralized at the headquarters but has field offices across the nation.
6. **Separation of Audit and Accounts**
   Since 1976, audit functions have been separated from accounts at the Union level. The state governments have followed suit, ensuring complete separation of audit and accounts. Under this system, ministries have assumed responsibility for payment functions, which are managed by their own Pay and Accounts Officers.

FUNCTIONS OF AN AUDITOR

An annual audit should be done by one who is independent of executive control, and the agency performing the work of conducting independent audit should be responsible to the legislature.

Generally, the duties of the auditor are mainly

a) They should examine past transactions. The accounts and reports of all personal or agents having the receipt, custody or disbursement of public money should be examined to ensure proper accountability of fidelity.

b) The transactions of public funds that have been expended have been received, or that should have been received, should be examined with respect to the question of legality.

c) The auditor should report the result of such examinations to the legislature which is the branch of the government acting as a check upon the executive and administrative levels. The function of the comptroller on the other hand are the settlement of claims, either of or against the state, and in this connection the keeping of the central accounts of the state and the prescribing of the subsidiary accounting system in field offices and institutions.

These involve purely administrative duties. The CAG will make an administrative pre-examination of all claims for the purpose of determining their expediency, propriety.

Self-Check Exercise-1

Q.1 Accounts have been separated from audit at the union level in 1976. True/False

Q.2 Audit reports are submitted to the parliament and the state legislatures through the President or Governor respectively. True/False

19.3. THE COMPTROLLER AND AUDITOR GENERAL OR INDIA

Financial control is a cornerstone of parliamentary democracy, and an independent audit agency plays a vital role in ensuring that control. The Comptroller and Auditor General (C&AG) of India is established under the Constitution of India as a constitutional mechanism designed to maintain parliamentary accountability, federal oversight, and expert administrative management over government spending. The C&AG is appointed by the President of India to perform these critical functions.

The foundation of the parliamentary system lies in the executive's responsibility to the legislature for its actions. For the legislature to effectively enforce this responsibility, it must be capable of scrutinizing the executive's activities and assessing their validity. Some executive actions can be easily evaluated, while others, such as examining financial transactions, require technical expertise. Parliament, primarily composed of laypersons, is not equipped to thoroughly assess financial dealings. However, it is Parliament's responsibility to ensure that public funds are used appropriately. This is where the C&AG's expertise is indispensable, providing the necessary assistance to Parliament in making informed financial judgments. The C&AG, therefore, plays a crucial role in maintaining the smooth functioning of parliamentary government, making the office an essential component of India's democratic framework. The C&AG is regarded as one of the four fundamental pillars of the Constitution, alongside the Legislature, Executive, and Judiciary.

The C&AG operates as an independent constitutional authority, separate from Parliament. The office was created not only for auditing government transactions but also for overseeing public expenditure. This dual role is why the position is considered so significant. Dr. B.R. Ambedkar, in discussing the C&AG's importance, emphasized its independence and crucial function, asserting that the office should be even more autonomous than the judiciary to carry out its duties effectively. The C&AG's work is vital to ensuring transparency and accountability in financial matters, and interference from discontented legislators could undermine its efficient operation.

As noted by Asoka Chanda, the re-designation of the Auditor General to Comptroller and Auditor General in 1950 signified a shift toward greater control over government spending, an area that had previously lacked oversight. The change was a significant step in establishing the C&AG as a key institution in ensuring financial accountability in India.

In the Constituent Assembly, when K.T. Shah suggested that the C&AG should be a certified accountant, T.T. Krishnamachari opposed the idea. He argued that the role required more than accounting knowledge; it required a broad understanding of administration and governance, which could not be reduced to mere technical skills. This position was accepted, reinforcing the idea that the C&AG's responsibilities go far beyond simple financial calculations.

GENESIS OF THE OFFICE OF C&AG

The history of the Indian Audit Department is linked with the formation of three Presidencies of Bengal, Madras and Bombay. Each of these Presidencies had its independent accounting office and the accounts prepared by them were consolidated in the accounting office of the East India Company in London. These independent organisations were amalgamated in 1857 by, Lord Canning to form one imperial establishment under the control of an Accountant General to the Government of India. The purpose of this consolidation was to secure co-ordination and uniformity in the compilation and presentation of accounts.

In 1858, when the East India Company's administration was taken over by the Crown, the complimentary post of Accountant General at the India office was created to prepare the accounts of expenditure incurred in England. Simultaneously, an independent auditor was appointed by the Crown for the audit of these accounts. This pattern of separated accounts and audit offices was reproduced in the administrative structure of the reconstituted Government of India also. But this arrangement was short-lived and both auditing and accounting functions were amalgamated in 1860 and placed in charge of the Accountant General to the Government of India, who was now designated Auditor General.

The statutory' recognition of the Auditor General came, however, only in 1919, with the introduction of constitutional reforms. He was made independent of the Government of India, and was appointed by the Secretary of State and. held office as the administrative head of the Indian Audit Department during His Majesty's pleasure.

The Secretary of State for India-in-Council was the font of authority for all executive power, and the Administration in India merely exercised delegated authority derhed through statutory rules and executive orders. It was necessary, therefore, to have an agency in India independent of the executive and responsible to the Secretary of State, so as to ensure that the administration in India was exercising financial authority within the delegations made. This duty was discharged by the Auditor General who was required to submit of the Secretary of State reports dealing with the total expenditure in India in each year, through the Governor General-in-Council, with such comments of a general feature as he thought appropriate to make.

The Government of India Act, 1935, gave further recognition to the importance and status of this office. Thereafter his appointment was made by His Britannia Maj esty, and the conditions of his service were also determined by His Majesty in council. His duties and powers were prescribed by rules made under the order of His Majesty in council, with the provision that his authority could be subsequently varied or extended, by the Federal Legislature. His salary, allowances and pension were made chargeable on the revenues of the Federation. He could be removed from office only in the same manner and on the same grounds as a judge of the Federal Court. To make him completely independent of the executive in the exercise of his function, he was made ineligible to hold further office Under the Crown in India after he had demitted office.

The Comptroller and Auditor General of India : Appointment and Term of Office

The provisions regarding the appointment and conditions of service of the C&AG are laid down in Article 148 of the Constitution. The C&AG is appointed by the President by warrant under his hand and seal for a period of six years or upto the age of 55 years, whichever is earlier. Before he enters upon his office, every person so appointed as the C&AG takes an oath before the President or any other person appointed in that behalf by him, according to the form set out for this purpose in the Third-Schedule. He can be removed from office in like manner and on like grounds as in the case of a judge of the Supreme Court. The salary and other conditions of service of the Comptroller and Auditor General are prescribed, by Parliament by law, viz., the Comptroller and Auditor General (Conditions of Service) Act, 1953, as amended in 1971. Being equated with a judge of the Supreme Court, the C & AG draws the equivalent salary of Rs. 30,000 per month. He is entitled to receive pension after his retirement. In other matters, his service conditions are equivalent to those of a Secretary to the Government of India.

Professor M. V. Pylee observes, "The framers of the Constitution, realizing the importance of an independent agency for audit under parliamentary democracy, made the Comptroller and Auditor General fully independent so that he could discharge his functions efficiently and fearlessly."

INDEPENDENCE OF THE C&AG

The Constitution of India ensures the independence of the Comptroller and Auditor General (C&AG) through several key provisions:

1. The President of India appoints the C&AG through a warrant under his hand and seal, similar to how a Supreme Court judge is appointed.
2. To safeguard the independence of the office from the executive, the C&AG cannot be removed except for proven misconduct or incapacity. This requires an address from both Houses of Parliament, passed by a two-thirds majority of those present and voting, and a majority of the total membership of each House. The process mirrors that of removing Supreme Court judges as outlined in Article 124(4).
3. While Parliament determines the C&AG's salary and service conditions, once appointed, these terms cannot be altered to his disadvantage, including changes to salary, leave, pension, or retirement age.
4. The office's administrative expenses, including salaries and other costs, are charged to the Consolidated Fund of India, ensuring the office's financial autonomy.
5. After retiring or resigning, the C&AG is ineligible for any government office or profit, either with the central government or any state government.

Self-Check Exercise-2

Q.1 The office's administrative costs, including staff salaries, are paid from the Consolidated Fund of India. True/False

Q.2 Once the Comptroller and Auditor General retires or resigns, they are not eligible for any governmental office or financial benefits from the Government of India or any State Government. True/False

19.4. SUMMARY

The sum and substance of all those provisions is that the CAG is an officer of Parliament and is supposed to work for it without fear to favour and for this reason has been placed beyond the pale of any executive influence.

Asoka Chanda observes, "To protect his independence and to place him beyond a the pale of the influence and interference of the executive government, both the ban on his employment after retirement as well as his removal by a special parliamentary process, have been retained and elaborated in the Constitution."

19.5. GLOSSARY

- **Apparatus :** The set of tools, instruments or equipments used for doing a job or as activity.
- **Fundamental** : Basic and important, from which everything else develops.

- **Proliferation :** The fact of something increasing a lot and suddenly in numbers or accounts.

19.6 ANSWERS TO SELF-CHECK EXERCISES

SELF CHECK EXERCISE-1

Q.1 True

Q.2 True

SELF CHECK EXERCISE-2

Q.1 True

Q.2 True

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19.8. TERMINAL QUESTIONS

(a) What are the functions functions of CAG?

(b) How independence of CAG is ensured?.

CHAPTER-20

AUDIT AND CAG: PART II

Structure

20.0. Introduction

20.1. Learning Objectives

20.2. Duties and Powers of the CAG

Self-Check Exercise-1

20.3. Organization of Structure, The CAG and PAC, Role of CAG : Critical Review

Self-Check Exercise-2

20.4. Summary

20.5. Glossary

20.6. Answers to Self Check Exercises

20.7. References/Suggested Readings

20.8. Terminal Questions

20.0. INTRODUCTION

The Comptroller and Auditor General of India (CAG) leads the Indian Audit and Accounts Department (IA&AD) and holds his constitutional role as the auditor for both the Union and State Governments, as outlined in Articles 149 to 151 of the Constitution. The responsibilities, authority, and terms of service of the CAG are defined under the CAG's (Duties, Powers, and Conditions of Service) Act of 1971.

20.1. LEARNING OBJECTIVES

After studying this lesson, this learner will be able:

- To understand the genesis of the office of CAG.
- To know about terms, conditions, power and functions of CAG.
- To analyze the relations of CAG and Public Accounts Committee.

20.2. DUTIES AND POWERS OF THE COMPTROLLER AND AUDITOR GENERAL

Audit Responsibilities
The CAG's statutory responsibilities include auditing:

- The receipts and expenditures of both Union and State Governments, as reflected in their respective Consolidated Funds.

- Transactions related to the Contingency Funds (established for emergencies) and the Public Accounts (primarily for loans, deposits, and remittances).
- The trading, manufacturing, profit and loss accounts, balance sheets, and subsidiary accounts maintained by any Government Department.
- The accounts of stores and stocks managed by Government organizations, companies, and corporations that require audits by the CAG as per their statutes.
- Authorities and organizations that receive substantial funding from the Union or State Consolidated Funds.
- Any body or authority, even if not significantly funded by the Consolidated Fund, at the request of the President or Governor.
- Accounts of entities receiving government loans or grants for specific purposes.

A distinct process is in place for auditing Government companies, where the Union Government holds a 51% or higher equity stake. The primary auditors for these companies are Chartered Accountants appointed by the Union Government upon the CAG's advice. The CAG directs the Chartered Accountants on how the audit should be carried out and retains the authority to comment on or augment their reports. Furthermore, the CAG has the right to audit these companies' accounts and submit audit findings to Parliament and State Legislatures.

A key aspect of auditing Government companies and Public Sector Undertakings (PSUs) is the periodic, in-depth evaluation of their performance by Audit Boards formed by the CAG. These boards include experts in relevant fields for specific PSU operations and conduct thorough reviews of a selection of undertakings each year, with the results featured in the CAG's Commercial Audit Reports. Additionally, similar Audit Boards have been established in some States for auditing State Government PSUs.

Accounts Duties

The Constitution stipulates that the President, based on the advice of the Comptroller and Auditor General (CAG), determines the structure for the accounts of both the Union and State Governments. The CAG’s (Duties, Powers and Conditions) Act of 1971 grants the CAG the authority to establish guidelines for Government departments regarding general accounting practices and the broad principles applicable to the audit of receipts and expenditures. Additionally, the CAG plays a key role in overseeing federal financial relations. According to Article 279 of the Constitution, the CAG is responsible for determining and certifying the net proceeds from taxes levied and collected by the Union but either assigned to the States or shared between the Union and the States.

Beyond his auditing functions, the CAG also compiles the financial accounts for most State Governments, except for Goa. The Department is also responsible for compiling the accounts of Union Territories, including Chandigarh and Dadra & Nagar Haveli.

Furthermore, the CAG has the authority to approve the salaries and allowances for officers in certain State Governments. Additionally, the CAG authorizes the payment of pensions and retirement benefits to employees across many State Governments and Union Territories and manages their Provident Fund Accounts.

AUDIT REPORTS

In addition to certifying the Appropriation Accounts and Finance Accounts for both Union and State Governments and submitting separate audit reports for Statutory Corporations and other Autonomous Bodies where the CAG is the sole auditor, the CAG publishes several audit reports concerning both the Union and State Governments. The key categories of these reports include:

For State Government:

- Civil
- Autonomous Bodies
- Scientific Departments
- Post & Telecommunications
- Defence
- Railways

For Union Government:

- Civil
- Receipts
- Commercial
- Indirect Taxes
- Direct Taxes

Each year, the CAG communicates the significant findings and observations through these reports. These reports, along with the certified Finance and Appropriation Accounts, are forwarded to the President or Governors to be presented before Parliament or State Legislatures. Reports concerning Public Sector Undertakings and Autonomous Bodies are sent to the respective Ministries or Departments for presentation to the relevant legislative bodies.

As noted by Asoka Chanda, "The audit by the C&AG is not limited by any constraints. He can bring any executive action's impropriety to Parliament's attention, even if its legality is not questioned. Additionally, his tenure does not depend on the administration's will. The constitutional provisions not only emphasize his role as a servant of the people but also grant him the necessary authority to assess the country's overall financial management."

Some view the Comptroller and Auditor General (CAG) as the Parliament’s agent, stressing his central role in a parliamentary democracy. His responsibilities go beyond ensuring that parliamentary appropriations are not exceeded without supplementary votes or that expenditure aligns with established rules. The CAG also ensures, on Parliament's behalf, that financial decisions are wise, faithful, and economical.

One of the CAG’s crucial duties is to protect the Constitution and laws in financial matters, particularly by preventing any expenditure he believes violates the Constitution or breaches legal standards. An even more significant role is evaluating whether the sanctions granted by competent authorities align with their intended purposes. The CAG is empowered to challenge improper discretion and comment on the appropriateness of sanctions and expenditures. His function is to uphold the necessary independence, objectivity, and fearlessness to assess the executive’s actions impartially. As Ambedkar rightly pointed out, "The functions and authority of the Comptroller and Auditor General as an auditor are broader and more extensive than those of professional auditors."

Self-Check Exercise-1

Q.1 The C&AG is not a mere civil servant. He is also not a servant of Parliament. True/False

Q.2 One of the important duty of CAG is to audit the receipts and expenditure of the Union and the State Governments accounted for in the respective Consolidated Funds. True/False

20.3. ORGANIZATIONAL STRUCTURE & THE C&AG AND THE PUBLIC ACCOUNTS COMMITTEE

The CAG discharges his duties and functions through the Indian Audit & Accounts Department. The office of the CAG directs, monitors and controls the activities of various offices of the Department and is responsible for development of organisational objectives and policies, auditing standards and system laying down policies for management of man-power and material resources of the Department and final processing and approval of the Audit Reports to be laid before the Parliament and the State Legislatures.

The Public Accounts Committee of our Parliament plays a very important role as the watch dog of Parliament. However, the basic material from which the Committee draws its subjects for examination are the audit reports of the Comptroller and Auditor General of India relating to the accounts of the Union which are laid before each House of Parliament. The C&AG's report is usually prepared after giving each ministry an opportunity to offer explanations or comments on the relevant portions of the draft audit report. After the report is submitted to the House and com mitted to the Public Accounts Committee, the programme of action of the Committee is drawn up in consultation with the Auditor General. He is in a way, the eye, the ear and the tongue of the Committee. He guides the Public Accounts Committee in its labours, detects the points of questions, presents them with such information as he has obtained and leaves the Committee to pursue them further, to consider them and report on them. He is the ' acting hand' of the Committee and its guide, philosopher and friend.

REPORT OF THE COMPTROLLER AND AUDITOR GENERAL

The C&AG every year brings out a series of reports on the audit conducted by its staff on the accounts of ministries, departments and organisations of the Central Government. Accountant-Generals bring out their own respective reports. Reports of the C&AG are laid before Parliament. Likewise reports emanating from Accountant-Generals are laid before the respective State Legislatures! These are referred to the Public Accounts Committee, respectively, of Parliament and the State Legislatures. Public Accounts Committees are supposed to examine the deficiencies and irregularities pointed out in these-reports. Observations and directions of the Public Accounts Committees are passed on to the concerned departments and ministries for appropriate action.

Reports of the C&AG are quite bulky documents, containing findings defaults, omissions and commissions running into hundreds of paragraphs each of the reports. In these the audit parties of C&AG tiring out special instances of misuse and wastage of public funds. They cover a very wide rang dealing with operations of all departments, organisations and public sector enterprises of respective ministries. Normally considering the status according to C8sAG in the Constitution, and taking into account the nature of tax performed by this august organisation, one would expect that the findings and observations contained in the reports would receive urgent attention of the concerned officials and department; in practice, the fact is that when the respective paragraphs of C&AG's observations and finding reach the concerned departments, after they have been commented upon by the Public .Accounts Committee, they often get buried in files and remain on the shelves. They hardly even cause the stir that they are expected to create.

However, C&AG's reports serve a public purpose. A 1962 C&AG report indicted the then Defence Minister V. K. Krishna Menon for contractual lapse in the purchase of army jeeps. Even Rajiv Gandhi himself used the critical reports by the C&AG and the PAC to ask his Railway Minister, Ghani Khan Choudhury to resign. The C&AG report on the Befors issue was highly critical of the way in which the gun deal was made. Basically, three criticisms were leveled. First, the evaluation of competing guns was flawed in that no General Staff Evaluation Requirement (GSER) was prepared. Second, the Defence Research and Development Office (DRDO) itself felt that test firing of the guns was inadequate and the evaluation limited. And, third, between 1982-85, the Army Headquarters preferred a French gun, but for reasons not too clear initially, it reversed itself and instead recommended the Swedish Bofors guns in 1986.

In December 1996, the C85AG has censured the Himachal Pradesh Government for violation of various articles of the Constitution, while borrowing funds, on which even the State Legislature failed to, set limits. In one of its report, which was placed in the State Assembly, the C&AG has pointed out that the internal debt of the State Government has gone up by a whopping 327 percent. It was Rs. 104.50 crore in 1990 and soared to Rs. 446.41 crore by 1995 end. The report has pointed out that the Constitution prohibits raising of loans by the State Government if there was any outstanding loan which had been made to the State Government by the Government of India or in respect of which a guarantee had been given by the Government of India except with the consent of the Government of India itself. In the Himachal case, it has been pointed out that heavy loans were arranged through the Himachal Pradesh State Electricity Board (HPSEB) though not for any purpose related to the HPSEB operations. It has also been summarily pointed out that concurrence of the GOI was not obtained in the matter. Very recently the C&AG has established Bihar Chief Minister's direct involvement in the fodder scam by personally pursuing the' appointment and seeking service extension for three key officials of the scam.

The C&AG in its latest special audit report has concluded that irregularities have been committed by the Power Grid Corporation of India in the import of the controversial Emergency Restoration System (ERS) equipment. While the union power ministry' continued to drag its fact in ordering a full-fledged investigation into the ERS equipment import, the C&AG's report of January 14, 1997 says that the Power Grid Management has incurred an avoidable extra expenditure of Rs. 23.81 crores in the deal with US based Lindsey Manufacturing Co. Ltd." The Ministry of Petroleum 65 Natural Gas has been flayed by the C&AG in its report on the participation of private parties with Oil 85 Natural Gas Corporation (ONGC) in production of crude oil and natural gas in its Report No. 5 (Commercial) of 1996. The report pointed out that production sharing contracts did not provide for the past cost reimbursement of Rs. 676.52 crores to ONGC in respect of Panna-Mukta and Mid and south Tapti fields. The C&AG report on audit for Bihar has shown non-reconciliation of Rs. 1,659.17 crores during the year 1995-96. Of special significance is irregular mid fraudulent withdrawal under the head 20137'Council of Ministers' Test checks of 12 departments under this head has pointed out to excess drawl of Rs. 6.24 crores from Patna Secretariat Treasury between 92-96. Audit of the central and centrally sponsored schemes for SC/ST groups revealed misuse of Rs. 282.85 crores.

The CAG has censured the Railways for delay in completion of ongoing projects leading to whopping coast overruns, injurious expenditure on various heads and loss of revenue due to incorrect levy of freight charges.

THE COMPTROLLER & AUDITOR GENERAL OF INDIA : POSITION

This is an office about which Dr. Ambedkar said in the Constituent Assembly that it is "probably the most important office in the Constitution of India". About the duties of this office, Dr. Ambedkar said they are "far more important than the duties even of the judiciary" of its status he said it was deserving of "far greater independence than the judiciary itself."

Importance of the office of C85AG arises from the fact that he exercises supervision over the accounts of all expenditure incurred by the ministries, departments and organisations of the Centre which, in the aggregate, are of the order of Rs. 1,70,000 crore, equivalent approximately to the entire budget expenditure, besides exercising supervision over Accountant Generals of States who are responsible for accounts of all State Governments and Union Territories involving aggregate expenditure of the order of Rs. 2,00,000 crore. total staff of C&AG and Accountant Generals is about 30,000 officials, spread all over the country.

Thus C& AG of India is undoubtedly entrusted with unique responsibilities. He is responsible for ensuring and overseeing 'every year the audit relating to aggregate expenditure of nearly Rs. 4,00,000 crore, of the Central Government and the State Governments. He is also responsible for audit of provident fund accounts of millions of government employees. He is expected to personally approve about 150 bulky reports every year, each consisting of hundreds of audit paragraphs and all this task has to be performed within a period of not more than about four months every year.

The C&AG is not a mere civil servant. He is also not a servant of Parliament. It is a unique constitutional post, carrying unique powers and responsibilities. This was explicitly recognised by the Supreme Court in the Accountant General's Case (1981) which recognised the C&AG's "special position under the Constitution a high ranking authority who can be expected to act according to the needs of the service ... (as) the constitutional head of the most important department of state.

A distinguished Auditor General, Mr. A. K. Roy, opined in 1964 that the C&AG was free "to determine the extent and scope of audit in various kinds of transactions. His audit transcends the mere formal or legal aspects of audit and includes what may be called efficiency and propriety audit." Without such an audit, the Public Accounts Committee-by far the most important committee of Parliament would be powerless. This is recognised by several Public Accounts Committee reports, both in England and in India. The English formula for describing the range and scope of the Comptroller's powers are 'economy, efficiency and effectiveness'. Indian understandings of this role are no less wide ranging Consider the ascription of responsibility given by the Public Accounts Committee of the Third Lok Sabha in 1962 to the Comptroller and Auditor General: "When a particular course of administrative action has resulted in waste, extravagant or improper expenditure, it is certainly the duty of the audit to call specific attention to matters of that kind and to bring facts to the notice of Parliament."

This, then, is the Comptroller and Auditor General's job. It is variously described as 'efficiency-cum-propriety' audit; or, 'economy, efficiency effectiveness'; or a check on "waste, extravagance and improper expenditure'.

It is for all these reasons that the office of the CAG is of crucial importance and why its independence is so jealously guarded. The C&AG is totally forbidden to hold any office of profit after he has finished his appointment. There was an enormous row-and rightly so when Mr. Asoka Chanda, the former C&AG-in 1960 was appointed the Chairman of the Finance Commission. The Minister's reply that the post was not an office of profit was rightly denigrated in Parliament as being too 'casual' for as a Congress M. P. (Mr. Khadilkar) rightly stressed the Comptroller and Auditor General was one a of 'the pillars of the Constitution' and he "did not know what would happen to us if the pillars are corroded and the House topples on our head."

ROLE OF THE C&AG : A CRITICAL VIEW

The role and functions of the C&AG have recently sparked debate on two primary issues:

The first issue pertains to whether the C&AG, in performing his audit duties, has the authority to comment on issues of extravagance and recommend measures for economy, beyond merely assessing the legal authority behind specific expenditures. Traditionally, the view is that when a statute grants an authority the power to approve expenditure, the audit process should include evaluating not only the legality of that expenditure but also its propriety, particularly from an economic standpoint. However, government departments object, arguing that such oversight interferes with their responsibility for administering funds. This perspective is supported by scholars like Appleby, who contend that economic considerations are inherently tied to administrative efficiency, and since the C&AG lacks direct responsibility for administration, he is not qualified to make judgments on economic matters. Appleby asserts, “Auditors may not be well-versed in good administration practices. Their expertise lies in auditing, not in managing administration. Their influence is greatest among those with little understanding of administration. Auditing is crucial, but it is a function with a limited scope and relatively narrow application.”

Another issue is whether the audit of the C&AG should be extended in industrial and commercial undertakings carried on by the government through private limited companies, who are governed by the articles of their association or to statutory public corporations or undertakings which are governed by statute. It was rightly contended by former Comptroller and Auditor General that in as much as money is issued out of the Consolidated Fund of India to invest in these companies and corporations on' behalf of the Government, the audit of such companies must necessarily be right and responsibility of the C85AG, while, at present, the C8gAG can have no such power unless the articles of association of such companies or the governing statutes provide for audit by the Comptroller and Auditor General. The result is that the report of the C&AG does not include the results of the scrutiny of the accounts of these corporations and the Public Accounts Committee or Parliament has little material for controlling these important bodies, spending public money. This defect has been partially remedied by the Act of 1971 which enjoins the CAG to audit and report on the receipts and expenditure of 'Government Companies' and other bodies which are 'substantially financed' from the Union or State revenues, irrespective of any specific legislation in this behalf.

However, critics are of the view that the CAG's audit of public undertakings is an effective instrument of parliamentary control, but the form, content and the approach of this audit have affected the efficiency and profitability of the public undertaking in India."

Self-Check Exercise-2

Q.1 One of the key duties of the Comptroller and Auditor General is to ensure compliance with the Constitution and legal frameworks in financial matters, and to prevent any expenditure that he believes contravenes constitutional provisions or legal regulations. True/False

Q.2 Reports emanating from Accountant-Generals are laid before the respective State Legislatures. True/False

20.4. SUMMARY

The services provided by the Comptroller and Auditor General (C&AG) are invaluable in protecting taxpayer interests. As the chief overseer of government financial operations, the C&AG acts on behalf of Parliament. Unlike the Finance Ministry, the C&AG does not have control over public spending. Instead, it offers an impartial framework that facilitates public oversight of government expenses. The C&AG's report on the Bofors case caused significant controversy, with the government criticizing both the report and the office itself. For example, N.K.P. Salve, Deputy Leader of the Lok Sabha, argued against the report and personally criticized C&AG T.N. Chaturvedi in Parliament.

It is fitting to recall Jawaharlal Nehru's statement from November 19, 1952: "Criticizing the Comptroller and Auditor General on the floor of the House would undermine his special position under the Constitution and make it difficult for him to perform his duties impartially."

As public spending in India continues to rise each year, there is room to expand and intensify the C&AG’s role to further support the democratic principles in the Constitution. However, the C&AG's role should remain as a watchdog, not an overzealous investigator.

20.5. GLOSSARY

- **Apparatus :** The set of tools, instruments or equipments used for doing a job or as activity.
- **Fundamental** : Basic and important, from which everything else develops.
- **Proliferation :** The fact of something increasing a lot and suddenly in numbers or accounts.

20.6 ANSWERS TO SELF-CHECK EXERCISES

SELF CHECK EXERCISE-1

Q.1 True

Q.2 True

SELF CHECK EXERCISE-2

Q.1 True

Q.2 True

20.7. REFERENCES/SUGGESTED READINGSS

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20.8. TERMINAL QUESTIONS

(a) How CAG is related to Public Accounts Committe of the parliament?

(b) What are the powers and functions of CAG?