Budget : Concepts and Terminologies

Happy Pant

BUDGET OF a government is a comprehensive statement of government finances relating to a particular year. Every Budget broadly consists of two parts- (i) Expenditure Budget and (ii) Receipts Budget.

The amounts of intended expenditure by the Government in the next financial year are expressed in the Expenditure Budget.

The entire Expenditure Budget can be divided into two distinct categories, viz.

i) Capital Expenditure- those expenditures by the government that lead to an increase in the assets or a reduction in the liabilities of the government. It is however not necessary that the assets created should be productive or they should even be revenue generating. Only the charges towards the construction of the asset are counted as Capital expenditure, while the subsequent charges for its maintenance are considered as Revenue expenditure. Most capital expenditure is non-recurring.

- Examples of Capital Expenditure causing 'increase in assets': construction of a new Flyover, Union Govt. giving a Loan to a State Govt.
- Examples of Capital Expenditure causing 'reduction of a liability': Union Govt. repays the principal amount of a loan it had taken in the past.

ii) Revenue Expenditure- those expenditures by the government that do not affect its asset-liability position. Most kinds of revenue expenditures are seen as recurring expenditures. The entire amount of Grants given by the Union Government to States is reported in the Union Budget as Revenue Expenditure, even though a part of those Grants get utilized by States for building Schools, Hospitals etc. This is so because the ownership of the schools or hospitals built from the Central grants would not be with the Union Government.

- Examples of Revenue Expenditure are: expenditure on Food Subsidy, Salary of staff, procurement of medicines, procurement of text books, payment of interest, etc

Total government expenditure can also be divided into another set of categories, viz.

i) Plan Expenditure

Plan expenditure refers to government expenditure, which is meant for financing the programmes/schemes formulated under the ongoing/previous Five Year Plan

ii) Non-Plan Expenditure

Expenditures of the government, which are not included under the Plan Expenditure are called Non Plan Expenditure. It includes some of the important types of government expenditure, eg: interest payments, pension, defence expenditure, spending on law and order, spending on legislature, subsidies, and salary of regular cadre teachers, doctors and other government officials.

The Receipts Budget presents the information on how much the Government intends to collect as its financial resources for meeting its expenditure requirements and from which sources, in the next fiscal year. This can also be divided into two categories:

i) Capital Receipts- those receipts that lead to a reduction in the assets or an increase in the liabilities of the government.

- Capital Receipts that lead to a 'reduction in assets': Recoveries of Loans given by the government and Earnings from Disinvestment;
- Capital Receipts that lead to an 'increase in liabilities': Debt.

ii) Revenue Receipts- those receipts that don't affect the asset-liability position of the government. Revenue Receipts comprise proceeds of Taxes (like, Income Tax, Corporation Tax, Customs, Excise, Service Tax, etc.) and Non-tax revenue of the government (like, Interest receipts, Fees/ User Charges, and Dividend & Profits from PSUs).

Government revenue through taxation can be divided into Direct Taxes and Indirect Taxes.

Direct Taxes: Those taxes for which the tax-burden cannot be shifted are called Direct Taxes. Examples of Direct Taxes are:

i) Corporation Tax This is a tax levied on the income of registered companies in the country, whether national or foreign, under the Income Tax Act, 1961.

ii) Personal Income tax- This is a tax on the income of individuals, firms etc. other than Companies, under the Income Tax Act, 1961. This head also includes other Taxes, mainly the 'Securities Transaction Tax', which is levied on transaction in listed securities undertaken on stock exchanges and in units of mutual funds.

iii) Wealth Tax- This is a tax levied on the benefits derived from the ownership of property, under the Wealth Tax Act, 1957. Wealth tax has virtually been abolished in India.

Indirect Taxes: Those taxes for which the tax-burden can be shifted are called Indirect Taxes. Any person, who directly pays this kind of a tax to the Government, need not bear the burden of that particular tax; he/ she can ultimately shift the tax-burden to other persons later through business transactions of goods/ services. Indirect tax on any good or service affects the rich and the poor alike! Unlike indirect taxes, direct taxes are linked to the tax-payee's ability to pay and hence are considered to be progressive. Examples of Indirect Taxes are:

i) Customs Duties-In this, the taxable component is import into or export from the country.

ii) **Excise Duties:** It is a type of tax levied on those goods, which are manufactured in the country and are meant for domestic consumption. It is a tax on manufacturing, which is paid by the manufacturer, but he passes this burden on to the consumers.

iii) **Sales Tax:** It is levied on the sale of a commodity, which is produced/imported and being sold for the first time. If the product is sold subsequently without being processed further, it is exempt from sales tax. Before the introduction of VAT, sales tax used to be levied under the authority of both Central Legislation (Central Sales Tax) and State Government's Legislation (Sales Tax)

iv) **Service Tax:** It is a tax levied on services provided by a person and the responsibility of payment of the tax is cast on the service provider. However this tax can be recovered by the service provider from the service receiver in course of his/her business transactions.

v) **Value Added Tax (VAT):** VAT is a multi-stage tax, intended to tax every stage of sale of a good where some value has been added to the raw materials; but taxpayers do receive credit for tax already paid on the raw materials in earlier stages.

Debt and Deficit

A Debt is a kind of receipt that necessarily leads to an increase of the government's liabilities. The government incurs a Debt only for meeting the gap created by excess of its expenditure over its receipts for that year, which is called Deficit.

Fiscal Deficit

It is the gap between the government's total Expenditure (including loans net of repayments) and its Total Receipts (excluding new debt to be taken). Thus Fiscal Deficit for a year indicates the borrowing to be made by the government that year.

Revenue Deficit

The gap between Total Revenue Expenditure of the Government and its Total Revenue Receipts is called the Revenue Deficit

Distribution of financial resources between the Centre and the States

A Finance Commission is set up every five years to recommend measures for sharing o resources between the Centre and the States, mainly pertaining to the Tax Revenue collected by the Central Government. Presently the recommendations made by the 13th Finance Commission are in effect (from 2010-11 to 2014-15), whereby 32 percent of the shareable /divisible pool of Central tax revenue is transferred to States every year and the Centre retains the remaining amount for the Union Budget.

Tax-GDP Ratio

Gross Domestic Product (GDP) is an indicator of the size of a country's economy. In order to assess the extent of government's policy interventions in the economy, some of the important fiscal parameters, like, total expenditure by the government, tax revenue, deficit etc. are expressed as a proportion of the GDP. Accordingly, a country's tax-GDP ratio helps us understand how much tax revenue is being collected by the government as compared to the overall size of the economy. A higher tax to GDP ratio in a country is a positive sign meaning that the government is collecting a decent amount of tax revenue as compared to the size of its economy. ❑

(E-mail:happy@cbgaindia.org)