DO YOU KNOW?

What is Fiscal Responsibility and Budget Management Act ?

The Fiscal Responsibility and Budget Management (FRBM) Act was enacted by the Parliament in 2003. Its objective is to institutionalise fiscal discipline, reduce fiscal deficit and improve macro economic management. This law aims at promoting fiscal stability for the country on a long-term basis. It emphasises a transparent fiscal management system and a more equitable distribution of debts over the years. This law also gives flexibility to the Reserve Bank of India to undertake monetary policy to control inflation.

Government needs resources for funding various kinds of developmental schemes and routine expenditures. Resources are raised through taxes and borrowing. The government can raise funds by borrowing from the Reserve Bank of India, financial institutions or from the public by floating bonds. Fiscal deficit is the total expenditure minus the revenue receipt, loan recoveries and receipts from disinvestment etc. It is a measure of the government borrowing in a year.

However, uncontrolled fiscal deficit is considered harmful for the health of economy. FRBM Act was notified in 2004 in response to the need felt to curb large fiscal deficit. The FRBM rules specify annual reduction targets for fiscal indicators. Originally, the act envisaged revenue deficit to be reduced to nil in five years beginning 2004-05. Fiscal deficit was required to be reduced to 3 percent of GDP by 2008-09. The Act also provides exception to the government in case of natural calamity and for national security.

The implantation of the act was put on hold in 2007-08 due to global financial crisis and the need for fiscal stimulus. There was a need for increased government expenditure to create demand to fight off the financial downturn and hence the government moved away from the path of fiscal consolidation for this period. This law also prohibits borrowing by government from the Reserve Bank of India and purchase of primary issues of central government securities after 2006. The act asked the Central government to lay in Parliament three statements in one financial year about the fiscal policy. To enforce fiscal discipline at the state level, the Twelfth finance commission provided for incentives to states through conditional debt restructuring and interest rate relief.

In 2012, the FRBM was amended and it was decided that the FRBM would target effective revenue deficit in place of revenue deficit. Effective revenue deficit excludes capital expenditure from revenue deficit and thus gives space to the government to spend on creation of capital assets.

The critics of this law feel, it would curb the government's social sector spending but there is no denying the fact that the need for fiscal sustainability cannot be ignored. The original document of FRBM Act can be seen on: http://finmin.nic.in/law/frbmact2003.pdf.

What is GST?

The Goods & Services Tax (GST) is an indirect tax reform measure which will replace all other indirect taxes such as Central Sales Tax, Octroi, excise duty, Service Tax and Value Added Tax (VAT) at the central and state levels. India will have a 'dual GST' system where states and the centre both would have power to levy taxes on goods and services. Exports would be an exception and GST will not be imposed on them. Under the GST, no distinction is made between goods and services for purpose of levying tax. GST is a value added tax where the person paying tax on his output is also entitled to get input tax credit on the tax paid on its inputs.

The idea of GST was first proposed in the budget speech of 2006-07 which had set out the deadline of 2010 for its introduction in the country. To implement such a tax regime a constitutional amendment would be needed as the Centre as well the States are involved in this issue. The government expects that the legislative process for the enactment of the GST would be started in the next few months. The Finance Minister has expressed the hope that the two tax reforms – the GST and Direct Tax Code (DTC) will be implemented soon.

The objective of GST is to make the taxation simple and to broaden the tax base. It will also help create a common market throughout the length and breadth of the country. The GST has the advantage of redistributing the burden of taxation equitably between manufacturing and services. The rate of taxation is also likely to come down with the introduction of GST. Goods of basic importance will have lower tax rates. Better compliance and increased tax collection will boost the tax to GDP ratio. Economic growth is also likely to get an impetus through GST. A report of National Council of Applied Economic Research has estimated an increase of 0.9 percent to 1.7 percent in the economic growth with the implementation of GST. Exports will also increase according to this study. ❑

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