Fiscal Reforms at the Sub-National Level: The Case of Punjab

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Abstract

The importance and need for sub-national fiscal reforms is all too obvious in India where the States are facing severe fiscal imbalances since the beginning of the nineties. A decade of political strife in the eighties, followed by populist economic policies in the nineties led to a massive fiscal deterioration in Punjab, hampering its overall growth process. The Fiscal Reform Programme in the state was initiated in 1999 with the signing of a Memorandum of Understanding between the Government of India and the Punjab government. This was followed by the setting up of various committees and commissions to look into the problems of revenue mobilisation, expenditure management, public enterprises and the power sector. The more recent effort towards fiscal consolidation has been the enactment of *Fiscal Responsibility and Budget Management Act, 2003*. The assessment of the entire fiscal reform effort of the state reveals that the Punjab government is seized of the seriousness of the situation, admits the gravity of consequences but lacks the grit and determination to implement certain hard decisions for fiscal restructuring. The government is very much caught up in the web

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of populist policies and succumbs readily to political pressure against certain unpopular decisions for attaining fiscal stability. The success of the fiscal reform programme depends only on the administrative competence and political will of the government towards achieving long-term fiscal consolidation and restoration of fiscal balances in the state.

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Introduction

State governments play an important role in economic activities in a federal setup like India. The critical role of state finances in the realignment and restoration of the macro balance in the economy is well recognised particularly in the context of economic restructuring. In a liberalised economic environment, sub-national governments will have to play a relatively more important role than in the past. Fiscal decentralisation is necessary in the wake of empowerment of rural and urban local bodies. This would essentially require the state governments to substantially augment their resources.

Fiscal reforms are a necessary, though not a sufficient condition for enabling the state governments to be more effective agents of development. Improving the efficiency, effectiveness and transparency of government's operations is equally important. Reforms at the centre in the early nineties paved the way for sub-national reforms. Unfortunately, this reform process did not pick up until the second half of the nineties when the state level fiscal crisis set in. Several states witnessed a slowdown in their growth rates relative to the level of the eighties. Competition for private investment by the states led to competitive tax concessions and incentives leading to fiscal imbalances in the nineties. Populist policies like free power and irrigation to the farm sector compounded the problem. The states are unable to increase the tax ratio as also improve the productivity of non-tax revenue. Political compulsions do not allow the states to increase user charges (Rao, 2002). The Fifth Pay Commission award in 1997 further led to fiscal deterioration on account of substantial pay increase. The states were also hit by higher interest rates on two counts: the interest rate on loans from Government of India (GoI) to the states was raised towards market rates and states became increasingly dependent on ‘small savings’ loans, a relatively expensive form of debt.

The deterioration in the fiscal position of the states (and its peaking in 1998-99) is also reflected in the ways and means advances and overdraft position of the states with the Reserve Bank of India (RBI). State governments resorted to overdraft and Ways and Means Advances (WMA) much more frequently than prior to 1997-98. The central government was unable or unwilling to limit the borrowings of the state governments. The debt of states as a result has gone up and sound fiscal management at state level has become an urgent agenda of reforms. There has been a considerable increase in the off-budget liabilities of the states. Also the states have paid very little attention to state level public enterprise reforms; instead, they use them for raising loans from the capital market without central government permission. state governments began to arrange for enterprises to borrow on their behalf with a commitment to meet debt service obligations in full from the budget, thus further reducing the scope of central government control over borrowing behaviour (Howes *et. al.*, 2003). The inefficient and unmanageable state electricity boards continue to be a major financial burden on the exchequer in the absence of power sector reforms. This has resulted in fiscal imbalances faced by almost all states of India including prosperous ones like Punjab, Maharashtra, and Gujarat.

The present study is an assessment of the fiscal reforms initiated and implemented in Punjab in the backdrop of a fragile political history of the state. Section II discusses the setting in of fiscal crisis in the state and its likely causes. Section III brings to focus the recent (1998-2003) fiscal scenario in Punjab. Sections IV and V deal with the implementation of the reform process and its assessment respectively. The conclusions of the study are summarised in the last section.

II. Fiscal Crisis in Punjab

Punjab, a predominantly agricultural economy, has the highest per capita income among all the major Indian states. It has the lowest poverty ratio of 6.2 percent as against an all- India average of 26.1 percent (*Economic Survey*, 2003-04). It seems that it is becoming increasingly difficult to maintain the pace of growth that Punjab witnessed in the seventies and the eighties. There has been a considerable slowdown in the nineties with the rate of growth of the economy coming down to less than 2 percent as against an all-India average of nearly 5 percent per annum, whereas it was 6.4 percent during the seventh five year plan when the all-India growth rate was 5.65 percent (*Statistical Abstract*, Punjab, 2003). The main reason for the declining growth rate of the economy has been the decade-long civil strife in the eighties coupled with a slowdown of the agricultural sector. The average rate of growth of the primary sector was 5.5 percent in the Sixth plan which has come down drastically to 1.8 percent during the Ninth plan. The performance of this sector has been erratic during the last one decade.

There are several reasons for the faltering performance of the Punjab economy in the post-reform period when other states of India began to perform better than before. The fiscal crisis is a manifestation of various political, economic and administrative failures of the government during the period of militancy when the civil administration was non-functional, ineffective and non-accountable. No effort in the post-militancy period was made by the elected governments to put the economy back on the path of economic development; attributing the deteriorating fiscal situation of the nineties to the decade of political strife in the state was considered enough.

Punjab has been under fiscal stress since 1984-85, when it became a revenue deficit state. In 1990-91 Punjab had the dubious distinction of being amongst the states with the highest fiscal deficit. There was minor fiscal consolidation in the mid-1990s but the position in the late nineties once again deteriorated. According to the *White Paper on State Finances (2002),* the factors which have adversely impacted the state's fiscal situation during the 1990s are ever increasing salaries and wage bills of the employees, mounting debt burden, heavily subsidised social and economic services, slow growth of revenue and loss making public sector undertakings (PSUs). All this is compounded by the lagged effect of terrorism on the growth of the state. This adversely affected the buoyancy in tax revenue. During the prolonged spell of President's rule in the state, no additional resource mobilisation measures were taken. The state had to incur a huge expenditure on combating the menace of terrorism. The government of Punjab in the later years of 1990s followed the populist path and allowed free power to the farm sector and abolished octroi, house tax, and land revenue. Vast losses incurred by the State Electricity Board, low irrigation charges, uneconomic transport fares have all combined to produce unduly low returns on decades of past investments, which in turn have adversely affected further investments in infrastructure and have also hurt the required expansion in education, health, and other social services.

The state's own tax revenue has shown a continuously declining trend. Tax revenue to Gross State Domestic Product (GSDP) ratio declined over a period of time. However, it increased from 6.75 percent in 1991-92 to 7.62 percent in 1994-95. Thereafter, there was a steep decline to 6 percent in 1998-99. State's non-tax revenue to GSDP ratio was only 1.35 percent in 1990-91, increased to 5.88 percent in 1994-95 and consistently declined till 1998-99 when it was 2.77 percent. A study of non-tax revenue reveals that user charges continued to be sub-optimal and in fact the subsidies on most of the social and economic services provided by the state increased in the post 1993-94 period. Input subsidies which were to the tune of Rs. 409 crore in 1990-91, went up to Rs. 2,000 crore in 2000-01. The capital expenditure to GSDP ratio fell from 3.8 percent in 1990-91 to 1.7 percent in 2000-01. This has affected the quality and reliability of the services provided to the people.

An exogenous factor contributing to smaller resource availability with the state government is the decline in the Punjab's share in the transfers from the Government of India according to the recommendations of successive Finance Commissions. It was 1.712 percent under the Ninth Finance Commission and came down to 1.461 percent under the Tenth Finance Commission. The Eleventh Finance Commission also heavily penalised the relatively developed states. This resulted in further reduction in Punjab's share to 1.147 percent. It is estimated that reduction in Punjab's share by the Eleventh Finance Commission has resulted in decreasing the transfers from GoI by Rs.1550 crore during 2000-05 (Government of Punjab, 2002b).

The revenue expenditure of the Punjab government comprises both developmental and non-developmental expenditure of which the share of committed expenditure consisting of wages and salaries, pensions and interest payment has registered a steep rise. Committed expenditure as a percentage of revenue receipts was 76.99 percent in 1991-92, which sharply increased to 142.13 percent in 1998-99. The poor growth in receipts and rapid growth in committed expenditure have resulted in a reduction in the share of capital expenditure. Capital outlay as a proportion of GSDP has remained consistently below 2 percent, falling below 1 percent in certain years. Also the composition of revenue expenditure has shifted from the productive sectors in favour of general services. The share of development expenditure i.e. expenditure on social and economic services in total revenue expenditure declined from 65 percent in 1990-91 to 46 percent in 1999-2000. This composition of expenditure is far from conducive for supporting the growth of physical and social infrastructure, so essential for reviving buoyant growth in the state.

Revenue deficit of the state has been increasing implying lower availability of funds for developmental/capital works. The revenue deficit as a percentage of GSDP was 2.11 percent in 1991-92 and came down to 1.17 percent in 1995-96. It increased sharply to 4.83 percent in 1998-99. The gap in revenue deficit is filled by high cost borrowing by the state. This has led to more expenditure on interest payments and higher debt burden. Borrowed funds are not used for productive purposes to create capital assets which generate income to service the debt. Primary deficit of the government, indicating the proportion of borrowing that goes towards meeting expenditure other than interest payments, has also shown a deteriorating trend. It was Rs.790 crore in 1991-92 and rose to Rs.1,463 crore in 1998-99.

The state has been heavily relying upon debt to augment its resources. The debt of the state government, which was 36.38 percent as a proportion of GSDP in end-March 1991 and rose to 40.66 percent of GSDP in end-March 2001, was highly unsustainable and needs to be capped. Most of the debt raised in the state is used for meeting the revenue expenditure and day-to-day needs of the state. The entire plan financed through loans and revenue expenditure is also financed through borrowing. The high and growing volume of debt has resulted in increasing liability for servicing the debt. Interest payment, is a committed liability, accounts for a large part of the use of government receipts. Proportion of revenue receipts spent on interest payments was 15.47 percent in 1991-92 and touched an all time high of 47.63 percent in 1998-99.

The state governments also stand guarantees for loans raised by PSUs and other state institutions. In the event of inability of the organisation to repay the loan and interest thereon, the guarantee can be invoked and the state has to bear the burden of the loan. In the case of Punjab, the government has been standing guarantees for loans indiscriminately and without assessing the repayment capability of the organisation. Since the PSUs in Punjab are sinking into a debt trap, it is almost certain that the liability of loans generated will devolve upon the State government in the near future.

The severity of the fiscal stress is further highlighted by the number of days that Punjab was availing of WMA and was in overdraft with the RBI. In the first half of the nineties the State's overdraft increased somewhat from 6 days during the year 1992-93 to 26 days during 1994-95 while the number of days that it was availing WMA went up from 5 to 20. After 1995-96, however, there was a sharp increase and during 1998-99 the number of days the state was in overdraft went up to 225 days with the state availing of WMA on 130 days. Thus, there were only 10 days in the entire year when the state had a positive cash balance.

The *Constitution (Seventy Third) Amendment Act, 1992* on *panchayats* and the *Constitution (Seventy Fourth) Amendment Act, 1992*, on municipalities, provided for setting up of a State Finance Commission to review the finances of these local bodies and suggest measures for their revenue augmentation. The first Punjab Finance Commission was constituted, accordingly, on April 22, 1994, to cover the period from 1996-97 to 2000-01. It identified the problems confronting the *panchayats* and municipalities in generating sufficient funds and suggested the augmentation of the resources by levy of user charges for the services rendered by them and levy and collection of taxes under their purview. The Commission also suggested that no exemption be provided from octroi by the state government.

The Second State Finance Commission was set up in September, 2000 covering the period 2002-03 to 2005-06. The Commission submitted an interim report for the year 2001-02. The Commission recommended the restructuring of certain taxes, improvements in tax administration and prevention of evasion of taxes of *Panchayati Raj* Institutions (PRIs) and Urban Local Bodies (ULBs). The recommendations of the two State Finance Commissions remain unimplemented in so far as the imposition of local taxes as well as devolution of funds to ULBs and PRIs is concerned. There has been a large shortfall in the transfer of funds to the local bodies as compared to the amounts due to them in accordance with the recommendations of the First Finance Commission as accepted by the state government. The ULBs received nearly 43 percent of the total assigned amount between 1996-97 and 2000-01 and the PRIs got only 35 percent of the budgeted provisions. The state government also did not give any grant to the financially weak local bodies or incentive grant as reward for their internal revenue effort. Even after the commitment of the government towards strengthening of ULBs and PRIs in the budget of 2002-03, full amount of their share was not transferred to them. This shows the disregard of the government not only towards its own commitments but also its constitutional obligations.

III. Fiscal Scenario in the Recent Past (1998-99 to 2002-03)

The fiscal scenario in the recent past in Punjab has been rather dismal. Despite the government admitting to the need for fiscal correction, sectoral reforms and reduction of deficits, very little has been achieved on this front. Various parameters like revenue, expenditure, debt, indicators of fiscal imbalances etc. are studied below to assess the actual position. The tables are based on the data from the budget documents of the Punjab government for various years, unless otherwise specified.

Revenue receipts (RR) of the government increased from Rs. 5,755 crore in 1998-99 to Rs. 11,071 crore in 2002-03, at an average trend rate of 13.15 percent per annum. There were, however, significant inter year variations in the growth rates. Of particular significance were the decline in 2001-02 and an impressive upturn in the subsequent year to nearly 24 percent. This happened due to 18.5 percent increase in tax revenue and 36.35 percent increase in the non-tax revenue.

Table 1: Revenue Receipts of the Punjab Government

	1998-99	1999-2000	2000-01	2001-02	2002-03
Revenue Receipts (RR) (in Rs. crore)	5755	7468	9377	8929	11071
Percentages of Revenue Receipts					
Own Taxes	56.68	52.85	52.20	53.98	51.58
Non-Tax Revenue	26.19	31.63	31.30	33.15	36.46
Central Tax Transfers	10.20	8.56	7.68	6.84	5.86
Grant-in-aid	6.93	6.96	8.82	6.03	6.10
Rate of Growth of RR	-9.38*	29.77	25.56	-4.78	23.99
RR/GSDP	10.58	11.91	13.70	11.62	12.83

* 1997-98 has been taken as base year for calculating rate of growth.

While on an average around 85 percent of the revenue came from the government's own resources, central tax transfers and grants-in-aid together contributed nearly 15 percent of the total revenue. Contribution of grants-in-aid declined to 6.10 percent in 2002-03 from 6.93 percent in 1998-99 and contribution of central tax transfers continued to decline throughout the period and came down to 5.86 percent in 2002-03 from 10.20 percent during 1998-99.

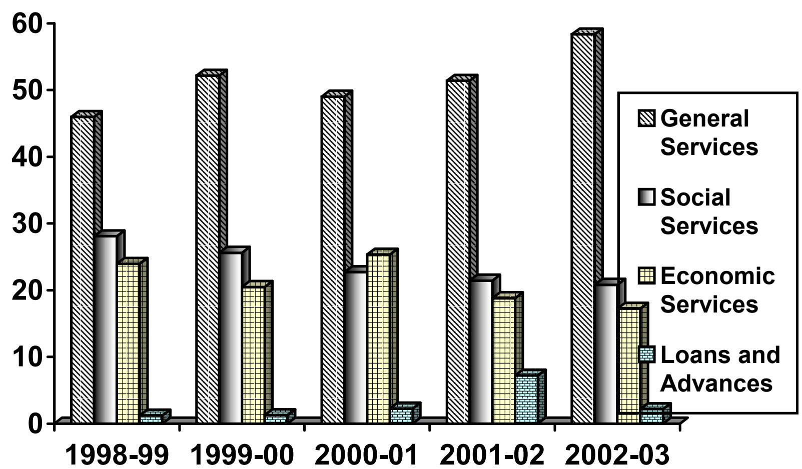
The total expenditure of the Government of Punjab increased from Rs. 9,642 crore in 1998-99 to Rs. 15,584 crore in 2002-03 at an average trend rate of 13.02 percent per annum. Leaving aside 2000-01, when the growth rate touched a whopping 24.48 percent, the growth rate has been hovering between 8 to 12 percent until 2002-03, when the growth of expenditure has been brought down to a more appropriate 5.58 percent, accelerating the rate of decline that began during the previous year. Consequently, total expenditure–GSDP ratio has also fallen from 19.59 percent in 2000-01 to 18.07 percent in 2002-03.

Table 2: Total Expenditure of the Punjab Government

	1998-99	1999-2000	2000-01	2001-02	2002-03
Total Exp. (TE) (Rs. crore)	9642	10771	13408	14760	15584
Per cent Rate of Growth	8.05	11.71	24.48	10.08	5.58
TE/GSDP	17.72	17.18	19.59	19.20	18.07

The relative share of activity components in total expenditure is indicated in the following chart:

Chart 1: Components of Expenditure - Relative share (in percentage)



The movement of relative share of these components of expenditure indicated that while the share of economic services and social services in total expenditure declined from 23.96 percent and 28.09 percent to 17.24 percent and 20.82 percent respectively during 1998-2003, the relative share of general services, which are primarily non-developmental in nature, increased from 45.98 percent in 1998-99 to 58.35 percent of total expenditure in 2002-03. Thus, the appreciable decline in the volume of total expenditure is not so appreciable after all; when viewed in terms of application to activity, it is the non-developmental general services which have gained at the expense of the developmental services. Interpreted in this light, reduced expenditure would denote a certain loss of developmental impetus in the important areas of governance.

Revenue expenditure (RE), which constituted the largest bulk (95.13%), was incurred to maintain the current level of services and did not represent a significant addition to the state's service network. Revenue expenditure, its rate of growth, ratio of revenue expenditure to state's GSDP and revenue receipts are indicated in the following table:

Table 3: Revenue Expenditure of the Punjab Government

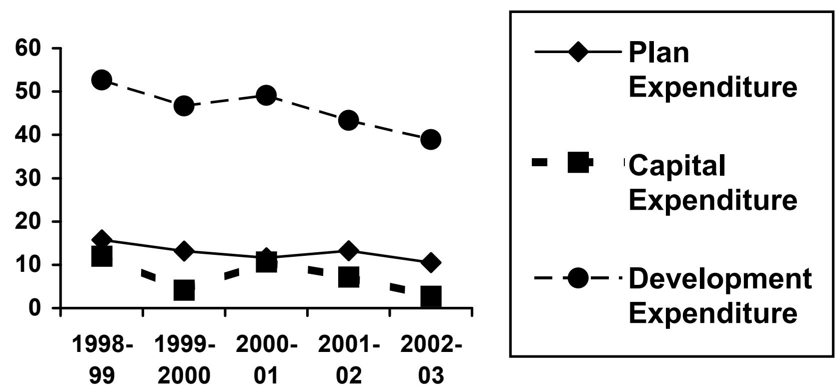
	1998-99	**1999-00**	**2000-01**	**2001-02**	**2002-03**
RE (Rs. crore)	8384	10195	11713	12710	14825
Per cent Rate of Growth	7.01*	21.60	14.89	8.51	16.64
RE/GSDP	15.41	16.26	17.11	16.54	17.19
RE/TE	86.95	94.65	87.36	86.11	95.13
RE /RR	145.68	136.52	124.91	142.35	133.91

* 1997-98 has been taken as base year for calculating rate of growth.

Revenue expenditure of the state increased from Rs. 8,384 crore in 1998-99 to Rs. 14,825 crore in 2002-03, at an average trend rate of 13.97 per cent per annum. The increase in the revenue expenditure during 2002-03 was mainly due to increase in expenditure on general education, pensions, state lotteries and interest payments. Though ratio of revenue expenditure to revenue receipts declined from 145.68 percent in 1998-99 to 133.91 percent in 2002-03, yet dependence of the government on borrowed funds persisted for even meeting the current expenditure primarily due to the fact that salaries, interest payments, pension dues and expenditure on state lotteries alone went 11 percent beyond the total revenue receipts of the state during the year.

The quality of expenditure can be judged from the percentage of plan expenditure, capital expenditure and development expenditure in total expenditure of the state government. The chart below depicts the same:

Chart 2: Quality of Expenditure (percentage to total expenditure)

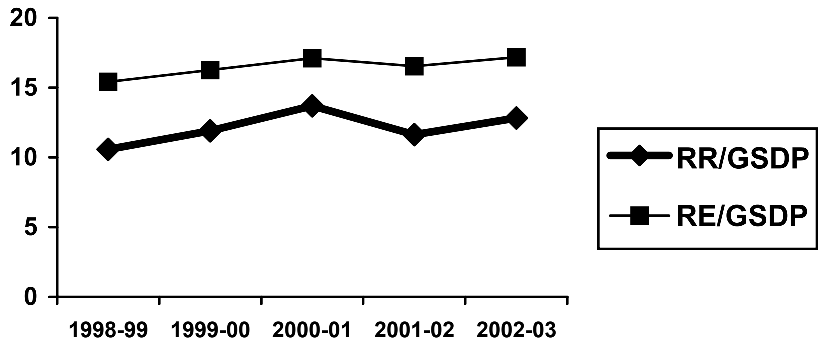


All the three components of expenditure show a relative decline during 1998-2003. Plan expenditure declined from 15.73 percent of total expenditure in 1998-99 to 10.53 percent in 2002-03. Similarly, capital expenditure also declined from 11.97 percent in 1998-99 to 2.76 percent in 2002-03. There was also a decline in the share of development expenditure from 52.69 percent in 1998-99 to 38.90 percent in 2002-03. The share of expenditure on these components decreased significantly in 2002-03 as compared to the level achieved in 1998-99. This further corroborates the decline in development works and service delivery in the State.

The deficit in the government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the government. Further, the manner in which the deficit is financed, and the resources raised are applied are important pointers to its fiscal health.

The chart below represents the gap between the revenue receipts and revenue expenditure as percentages of GSDP:

Chart 3: State Revenue Receipts and Expenditures (Percentage of GSDP)



The revenue receipts as percentage of GSDP increased marginally from 10.58 in 1998-99 to 12.58 in 2002-03 and the revenue expenditure as percentage of GSDP also increased correspondingly from 15.41 in 1998-99 to 17.19 in 2002-03. Thus, the gap between the two did not slim down during the period.

The revenue deficit of the state increased from Rs. 2,629 crore in 1998-99 to Rs. 3,754 crore in 2002-03. Out of the 5 years under study, the state had a nominal primary revenue surplus only in 2000-01. This reflects the inability of the state to match its current revenue to current expenditure. The fiscal deficit, which represents the total borrowing of the Government and its total resource gap, increased from Rs. 3,780 crore in 1998-99 to Rs. 4,410 crore in 2002-03. The state also had a primary deficit of Rs. 1,463 crore in 1998-99 which decreased to Rs. 976 crore in 2002-03. Table 4 shows the fiscal imbalances in Punjab.

Table 4: Fiscal Imbalances in Punjab

(Rs. crore)

	1998-99	1999-00	2000-01	2001-02	2002-03
Revenue Deficit (RD)	2629	2727	2336	3781	3754
Primary Revenue Deficit (PRD)	312	90	(-) 07	603	320
Fiscal Deficit (FD)	3780	3194	3904	4959	4410
Primary Deficit (PD)	1463	557	1561	1781	976
Per cent					
RD/GSDP	4.83	4.35	3.41	5.27	5.13
PRD/GSDP	0.57	0.14	(-) 0.01	0.84	0.44
FD/GSDP	6.95	5.09	5.70	6.91	6.03
PD/GSDP	2.69	0.89	2.28	2.48	1.33
RD/FD	69.55	85.38	59.84	76.25	85.12

The ratio of revenue deficit to fiscal deficit increased from 69.55 percent in 1998-99 to 85.12 percent in 2002-03 indicating further deterioration in the State finances. As a proportion to GSDP, though the revenue deficit has decreased marginally to 5.13 percent and fiscal deficit to 6.03 percent in 2002-03, yet large revenue and fiscal deficits year after year have corroded the financial health of the state.

The fiscal liabilities of the state increased from Rs. 21,705 crore in 1998-99 to Rs. 38,315 crore in 2002-03 at an average annual rate of 16.39 percent.

Table 5: Fiscal Liabilities of the State Government

	1998-99	1999-00	2000-01	2001-02	2002-03	Average
Fiscal Liabilities (Rs. crore)	21705	24804	28957	33921	38315	29540
Rate of Growth (percent)	21.55	14.28	16.74	17.14	12.95	16.39
Ratio of Fiscal Liabilities to: (percent)						
GSDP	39.9	39.6	42.3	44.1	44.4	42.4
Revenue receipts	377.2	332.1	308.8	379.9	346.1	346.7

The ratio of fiscal liabilities to GSDP increased from 39.9 percent in 1998-99 to 44.4 percent in 2002-03 and the fiscal liabilities were 3.46 times of the revenue receipts in 2002-03.

An important indicator of debt sustainability is net availability of funds after payment of the principal on account of the earlier contracted liabilities and interest. The table below gives the position of the receipt and repayment of public debt over the last five years. The net funds available were to the tune of 20.14 percent of total fresh loans in 2002-03. The major chunk of repayment has gone towards interest payment, being 80 percent in 1998-99 and coming down to nearly 70 percent in 2003-04.

Table 6: Net Availability of Borrowed Funds

(Rs. crore)

	1998-99	1999-00	2000-01	2001-02	2002-03
Total Public Debt Receipt	2920	3655	4738	6250	6246
Repayment (principal + interest)	2896 (80.00)*	3479 (75.79)	2947 (79.50)	4239 (74.97)	4988 (68.84)
Net Fund available	24	176	1791	2011	1258
Net fund available (percent)	0.8	4.8	37.8	32.2	20.14

*Figures in brackets are interest as percentage of repayment.

During the year, the state repaid the high cost loans and advances from Government of India (GoI) bearing coupon rates in excess of 13 percent per annum after borrowing funds from the open market at the weighted average rate of 7.14 percent. As a result, the net availability of funds was reduced to 20.14 percent from 32.2 percent in previous year. The maturity profile of the outstanding market loans as on March 31, 2003, indicated that nearly 25 percent of the loans are payable within five years while the remaining loans are required to be repaid during the next five years.

Punjab government had guaranteed loans of Rs. 13,734 crore availed by its Corporations and others as of March 31, 2003. The guarantees are in the nature of contingent liabilities of the state and in the event of non-payment, the state has to honour these commitments. The year-wise position of the maximum amounts for which guarantees were given by the state government to the end of March 2003 is shown in Table 7.

Table 7: Guarantees of the State Government

(Rs. crore)

Year	Maximum amount guaranteed	Outstanding amount of guarantees		Percentage to total revenue
		Principal	Interest	
1998-99	7408	3294	96	129
1999-00	12059	9861	90	162
2000-01	7331	8868	122	78
2001-02	10244	10244	340	115
2002-03	17720	13255	479	160

The amount of outstanding guarantees increased from Rs. 3,390 crore in 1998-99 to Rs. 13,734 crore in 2002-03 and amounted to 124 percent of the revenue receipt (Rs. 11,071 crore) of the state government in 2002-03.

It is generally desirable that state's flow of resources should match its expenditure obligations. However, to take care of any temporary mismatches in the flow of resources and the expenditure obligations, the state has been increasingly relying on the WMA from RBI over the years. Normally these advances should be liquidated during the year. Any outstanding balances of WMA indicate mismatch in the revenue and expenditure. Resort to overdraft, which is over and above WMA limits, is all the more undesirable. The following table gives the WMA and overdraft position of the Punjab government as reported in the Report of the Comptroller and Auditor General (CAG) of India, March, 2003.

Table 8: Ways and Means and Overdrafts of the State and Interest paid thereon

(Rs. crore)

	1998-99	1999-00	2000-01	2001-02	2002-03
Ways and Means Advances					
taken in the year	1279.58	1851.66	2170.77	1976.61	3127.90
Outstanding	179.40	182.12	243.42	221.42	185.79
Interest paid	7.79	7.67	6.83	8.73	9.45
Overdraft					
taken in the year	3840.23	1178.22	1600.10	3826.70	640.74
outstanding	826.51	101.92	48.37	196.36	Nil
Interest paid	6.11	4.58	2.38	4.50	1.43
number of days state was in overdraft	225	84	107	119	53

Under an agreement with the RBI, the state government has to maintain with the bank a minimum balance of Rs. 1.56 crore on all days. If this balance falls below the agreed minimum on any day, the deficiency is made good by taking WMA and the maximum limit for ordinary WMA is Rs. 235 crore. Beyond this, the shortfall is bridged by special WMA, the limits for which vary from time to time and the further gap is filled by overdraft. During 1998-2003, Punjab has always overstepped its WMA limit many times over the prescribed amount and has been in overdraft for an average of 118 days. However, over a period of these 5 years, the dependence of the state government on RBI for cash management has declined from 225 days in 1998 to 53 days in 2003 but the dependence on WMA has increased.

It is evident from an overview of state finances in Punjab that the state has been continuously facing fiscal crisis and is heavily dependent on borrowed funds for meeting its general governance needs and development obligations. The fiscal stress on the state government has resulted in eroding its capacity to implement national programmes and even to take advantage of funds available from GoI and other national and international agencies. Therefore, the fiscal reforms at the state level have gained increasing focus in recent years.

IV. Fiscal Reforms in Punjab

The states have taken a number of corrective measures towards fiscal consolidation to restore fiscal stability and achieve a balanced revenue account, which is an important indicator of fiscal prudence. In view of the fiscal distress experienced by Punjab for over a decade now, it is imperative that the government takes some measures for fiscal reforms in the state. The fiscal restructuring measures are intended to address several long-term issues in revenue mobilisation, expenditure management, PSU reforms, infrastructure development and improvement in the funding of ULBs and PRIs.

Punjab's finances are afflicted both by structural problems and problems of cash flow management. One of the first major manifestations of this came in April, 1999, when Punjab's overdraft with the RBI was Rs. 775 crore for the 8th consecutive day, calling for urgent corrective action (GoP, 2002b). In pursuance of the decision of the GoI to provide assistance to the state governments in order to strengthen their financial situation, the Government of Punjab signed a Memorandum of Understanding (MoU) with the GoI. The agreement reached between Ministry of Finance, GoI and Government of Punjab is termed as Fiscal Reform Programme for Punjab. According to this agreement, the Ministry of Finance would provide immediate assistance to help the state government get out of the overdraft. The assistance comprised permitting state government to carry out market borrowing immediately and on priority basis, making advanced devolution and releases of Central Plan Assistance and WMA. These releases and permission were conditional in that the state government would raise its internal resources and agree to undertake time-bound action on the reform programme.

The MoU stated that in order to increase revenues and reduce expenditure, the state government would draw up an implementation plan, giving details of the various actions, the agencies responsible for carrying out these actions and a time frame within which the actions would be completed. The MoU listed certain measures for improving the fiscal situation. These were reduction in non-plan revenue expenditure, reduction in subsidies through improved cost recovery for both social and economic services, withdrawal of tax incentives to industries, disinvestment, reform of tax regime and improvement in management of public debt.

However, even after signing the MoU, progress towards fiscal consolidation was poor. The action taken report submitted by the Government of Punjab to the GoI in November 2000 indicated a lack of headway made on this front. The Punjab government continued to face financial problems. Non-plan expenditure, which was to be reduced by 5 percent in 1999-2000 from its level in 1998-99, actually increased by 7 percent during that period. The state government took certain policy initiatives in the state budgets of 2000-01 and 2001-02. The fiscal measures spelt out in these budgets included rightsizing the government, rationalisation of tax structure, compression of non-productive expenditure and revision of user charges. The institutional reforms announced included the constitution of Public Expenditure Reforms Commission and Public Sector Disinvestment Commission, preparation of MoU with the Government of India on power sectors reforms and notification of State Electricity Regulatory Commission. These budgets also took note of certain sectoral reforms to be undertaken.

Despite the set of measures announced by the government towards fiscal reforms, Punjab continued to face a severe financial crunch. The state was increasingly relying on the RBI to tide over its day-to-day crisis. The state's account with the RBI was running in an overdraft of Rs. 168.29 crore as on March 2, 2002. Faced with the precarious situation, the Punjab government had been using the guarantee route for solving its liquidity problems. In the process it impaired its own solvency.

The change of government in the state in February 2002 and the subsequent announcement of the various budgetary and fiscal reforms provided yet another opportunity for fiscal consolidation.

Realising the gravity of the financial crises the government brought out a *White Paper on the State's Finances* in March, 2002. The budget for the year 2002-03 focused on certain fiscal reforms including corrective measures for restoration of financial health of the state. The government committed itself to correcting institutional factors leading to economic and financial distortions.

A plethora of committees and commissions have brought out their recommendations regarding certain sectoral reforms in the state as well as improvement in management of state finances. Several studies have been carried out by NIPFP on behalf of the World Bank, New Delhi, to identify the malady as also to suggest solutions to it. An expert committee to suggest power sector reforms gave its recommendations, Disinvestment Commission for the Restructuring of the State-level Public Enterprises submitted its report in September 2002, and the report of the Public Expenditure Reforms Commission is available with the Government of Punjab since October 2002. All these documents have suggested the implementation of major structural reforms in the State finances and administration for resource augmentation and expenditure management. The most important and recent step in this direction has been the enactment of *Fiscal Responsibility and Budget Management Act* (FRBMA) in May 2003. The state government signed another MoU with the Ministry of Finance, GoI on July 23, 2003 to achieve fiscal sustainability in the medium term.

FRBMA attests the seriousness with which the government seeks to tackle the problems of revenue and fiscal deficits and the high ratio of public debt to GSDP. The primary motives of the act are:

> "To provide for the responsibility of the State government to ensure inter-generational equity in fiscal management and long-term financial stability by achieving sufficient revenue surplus, containing fiscal deficit and prudential debt management consistent with fiscal sustainability through limits on the State government borrowings, debt and deficits, greater transparency in fiscal operations of the State government and conducting fiscal policy in a medium-term framework and for matters connected therewith or incidental thereto" (Punjab Gazette, 2003).

A recent study (Rajaraman, 2004) examines the fiscal responsibility legislations enacted by the governments of Karnataka, Kerala, Punjab and Tamil Nadu. The following table showing the features of FRBMA, Punjab, is an extract from this study.

Fiscal Responsibility and Budget Management Act, Punjab

Notified:	5 May, 2003, Act No. 11
Documentary Obligations:	MTFP-3 year Quarterly Review
Targets:	
RD:	Path: □5% RR fall/year Target: 0 (no year)
FD:	Path: □2% absolute increase / year Target: 3% GSDP (no year)
Modifiable for:	Calamity
Guarantees:	Cap: 80% of RR of the previous year
Total Debt:	40% of GSDP by March 31, 2007
Protection:	No fiscal sops six months before elections.

The appreciable design features of the *Punjab Act* are as follows:

- The quantified limits to revenue and overall fiscal imbalances are in general specified for a stated target year, 2006-07. Punjab has annual path limits as shown in the table above.
- The correction of the revenue deficit is sharper than the correction of the fiscal deficit, which permits high rate of increase in capital expenditure, but requires a sharp reduction in (non-interest) revenue expenditure.
- The single most effective element, the inflexible limit imposed on long term government guarantees, i.e., 80 percent of revenue receipts of the previous year, is a good design feature.
- The act clearly states that for the purpose of the definition of fiscal deficit, off budget borrowings shall be treated as borrowings by the state government, and the expenditure incurred on subsidies due to the enterprises in the power sector, whether paid or not, shall be treated as expenditure by the state government. This introduces transparency in borrowings and expenditure of the government.
- The act also ensures that government shall present before the State Legislative Assembly in each financial year, the medium term fiscal

policy statement along with the annual budget. This will include an assessment of sustainability relating to balance between revenue receipts and expenditure, use of capital receipts and market borrowings for generating productive assets, fiscal performance of the state and future prospects for growth.

- For ensuring that the government adheres to the programme, the act provides for corrective measures that are automatically to be undertaken once the actual deficits show signs of exceeding their targeted value in any year.
- The act protects against election year opportunism as it carries a specific ban on fiscal sops 6 months before elections.

Rajaraman emphasises that Punjab will have to exceed the annual path limits in order to meet the debt target. Also without added revenue effort, the fiscal compression imposed by the fiscal responsibility legislation will not be possible. The state is dependent on own revenues to a large extent, which implies that the revenue effort of the state has to be stepped up considerably without damaging the quality of public service delivery.

The Act should be effective in achieving the targets and should go a long way in making the budgetary process transparent. The government is required to lay on the table all cards relating to its perception of the emerging economic trends and the macroeconomic framework behind formulation of short term and medium term policies.

V. An Assessment of the Fiscal Reform Programme of the Punjab Government

The deteriorating finances of the Punjab government are a matter of concern as these are leading to compression of developmental expenditure and burgeoning non-developmental expenditure. All the institutional and sectoral measures suggested by the Government of India, Reserve Bank of India and other agencies to attain fiscal balances at the sub-national level have been adopted by Punjab over a period of time. Signing of MoU with the Government of India, Medium Term Fiscal Programme and enactment of FRBMA etc. suggest that the state government is seized of the situation and admits the gravity of the consequences of non-compliance to the reform programme.

An evaluation of the fiscal reform programme of the state over the last few years reveals that the Government of Punjab has not adhered to the recommendations of most of the committees and commissions and the financial targets laid down in various documents have not been achieved. No action to implement the recommendations of the Public Expenditure Reforms Commission for compressing government expenditure, improving the service delivery, restructuring of government departments and agencies, withdrawal of subsidies, and imposition of user charges has been taken by the government as reflected in the study of Action Taken Report on Fiscal Reform Measures (Annual Financial Statement, GoP, 2004-05). Most of the reforms in the power sector as committed by the Government of Punjab in the MoU signed in March 2001, between the Ministry of Power, GoI and Department of Irrigation and Power, GoP, have not been implemented so far (CAG, 2003). The commitment towards these reforms is reiterated once again in the Budget Speech of 2004-05, thus admitting its non-compliance.*

Recommendations of the Disinvestment Commission submitted in September 2002 and the government decision to disinvest in six PSUs are yet to be implemented. The report of CAG reveals that the government has failed to achieve the set target of Rs. 50 crore to be garnered through such disinvestments. No disinvestment and privatisation of PSUs has taken place during 2002-03. In the case of nine companies, notices were published at various points of time between May 1998 and March 2003 for their dissolution. But no definite orders have been issued so far. The merger of one company identified for the purpose was to be effective from 31 March, 2001, but no notification has been issued so far. Some of the working companies have been incurring losses for more than five consecutive years leading to their negative net worth. Besides, five companies could not commence business activities despite being in existence for more than eleven years. Sixteen out of 33 statutory corporations and government companies with an aggregate investment of Rs. 412.87 crore were running at a loss and the accumulated losses were Rs.1290.90 crore.

An in-depth analysis of the working of the government brings into focus certain practices, which reflect misallocation and misutilisation of funds by the government. Also, the lack of transparency in management of public funds is evident as brought out by the CAG. As per Article 205 of the Constitution of India, it is mandatory for a state government to get the excess over a grant/appropriation regularised by the state legislature. However, the excess expenditure amounting to Rs. 1849.63 crore for the years 1996-97 to 2001-02 had not been regularised by July, 2003. This was breach of legislative control over appropriations.

The financial rules require that government expenditure should be evenly distributed throughout the year. The rush of expenditure particularly in the closing months of the financial year is regarded as breach of financial rules. The expenditure pattern (revenue and capital) of most of the departments of Punjab Government for 2002-03 revealed that there was a tendency to utilise the budget to the extent of nearly 40 to 100 percent in certain cases at the end of the financial year.

Articles 266 and 283 of the Constitution of India provide that all receipts of the state should be credited to the Consolidated Fund of the State and withdrawal of money therefrom should be regulated by law made by the legislature of the state. Accordingly, fees/cess levied through acts of legislature of the state and sale proceeds of government lands should be credited to the consolidated fund of the state. It was noticed that in four Funds namely 'The Cattle Fair Fund' (CFF) (February 1968), The Punjab Education Development Fund (PEDF) (August 1998), The Punjab Infrastructure Development Fund (PIDF) (December 1998) and the Punjab Infrastructure Fund (PIF) (February 2001), receipts aggregating Rs. 527.27 crore realised during 1998-2003 on account of fees in cattle fairs, cess on sale of liquor, beer, petrol, and agricultural produce and sale proceeds of lands were credited to the respective funds rather than to the consolidated fund of the state which resulted in reduction in receipts deposited in the consolidated fund. Transfer of substantial money to various funds resulted in incurring of substantial expenditure without budgetary control of the state legislature.

During the period June, 2000 to December, 2001, immediately before the assembly elections in Punjab, the then Chief Minister started visiting various places for meeting the general public and disbursing funds to people under the name *Sangat Darshan Programme*. No separate budget/funds were provided by the State government for the programme. As reported by CAG, money was mainly withdrawn from Chief Minister's Relief Fund and other development funds of the state.

The money was irregularly disbursed without prior identification of purpose and without assessing the requirement of funds. Further money from various development funds was disbursed mainly for purposes not included under their respective acts. Contrary to the acts governing the funds, all administrative and financial powers were entrusted to the Chief Minister. Evidently, public money was unauthorisedly drawn and disbursed without approval of norms/procedures by the government.

Mandi fees and rural development cess are collected by the Mandi Committees and retained by the Mandi Board and Rural Development Board respectively. These proceeds are meant to be utilized for building infrastructure in the Mandis and rural areas. But, in the absence of a rigorous system of transparency and accountability, the proceeds have been used in an unauthorised and sub-optimal way.

There was an irregularity in the food account of the State since 1995-96. RBI sanctions a Cash Credit Limit to the State government for funding procurement of food grains. When the foodgrains move from the godowns and are paid for by the Food Corporation of India, the funds are to be passed on to the State Bank of India. But a closer scrutiny of the food account showed that these funds were not returned to SBI but stood out as debt of the State government. An amount of Rs. 2,360 crores was diverted from the food account to meet the committed expenditure of the government upto March 2002. The present government also continued the same practice and diverted Rs.1900 crores in a single year, i.e., 2002-03. The food account has been taken out of the State budget since April 1, 2003. This will hopefully put a stop to an improper access to this money that was leading to high debt burden. The State government has incorporated a separate undertaking, *viz*., Punjab State Grains Procurement Corporation Limited to undertake trade, purchase, storage, movement, including inter-State movement, distribution and sale of foodgrains and other foodstuffs. This is expected to introduce the much desired transparency in the management of food account.

A further scrutiny of the State government's budget reveals that there are variations between budget estimates, revised estimates and actuals. This deviation has also been pointed out by the Public Expenditure Reforms Commission, 2002. This is an evidence of poor fiscal marksmanship indicating that the budgeting process fails to provide a mechanism for appropriate expenditure management to ensure that the policy goals of the government are not undermined. The government has also flouted certain recommendations of various commissions regarding revenue mobilisation. The government reduced the rate of road tax in December, 2000 and again in January, 2002 resulting in a loss of Rs. 56.43 crore per annum. The government also does not make enough effort to mobilise arrears of revenue from various departments, which amounted to Rs. 3,004.85 crore at the end of 2002-03. CAG has brought several other cases of irregularity in release and utilisation of funds to light. Many instances of under assessment/short-levy/non-levy/incorrect computation and consequent loss of revenue have been identified. The abolition of octroi with effect from December, 2001, which constituted nearly two-third of the own revenues of the ULBs, starved these further for funds. This defeats the very purpose of the provisions regarding the setting up of the state finance commissions.

The state government stands guarantee for the borrowings of state PSUs. In consideration of guarantees given by the government, guarantee fee is charged by it from the recipient institutions. The recipient institutions, in many cases, have not paid the guarantee fee and in some cases it has been waived off. State government has also given guarantee for loss making units, adding to the risk of principal and interest thereon. The guarantees are extended for various institutions as a matter of routine without verifying their credit worthiness. Also, as per the MoU (1999), non-merit subsidies were to be reduced in a phased manner; but contrary to this objective, these subsidies increased from Rs. 407.47 crore in 1999-2000 to Rs. 589.64 crore in 2002-2003.

Fiscal consolidation and stability in the state can be achieved only if there is a realisation on the part of the government to shun populist policies and clamour for retaining power at all costs. A strong commitment is essential for taking hard decisions. The postponement of vital reform measures like implementation of value added tax (VAT), power sector reforms, restructuring of staff deployment in government departments, and disinvestment in state PSUs exhibit a complete lack of seriousness regarding the fiscal reform programme in the state. The sanctity and importance of the state budget for the members of the legislative assembly can be gauged from the fact that in June 2004, the state government budget for 2004-05 amounting to Rs. 30,000 crore was passed in only 23 minutes. This reflects the absence of deliberations on such an important document of the state. Also, the downsizing of the Punjab Cabinet in July 2004 as per the constitutional requirements was merely an eyewash. The purpose of limiting the number of ministers was to reduce the cost to the public exchequer, which was flouted with impunity. While the number of ministers was reduced, there has been a phenomenal increase in the number of Chairmen of State Public Enterprises and Parliamentary Secretaries. They enjoy almost the same salary and allowances as their ministerial counterparts and cost the exchequer as much. Another instance of gross misuse of political power against the interest of the state has been to grant certain concessions to some selected distilleries (a non-priority area). The excise concessions will be availed of in 10 years and will amount to a decline of about a fourth of the state's excise duty from distilleries. Besides excise concessions, these units have also received exemption from electricity duty for 5 years and stamp duty on land purchased for the unit. All this smacks of utter disregard for the government's own commitments towards fiscal prudence and austerity amounts to profligacy on the part of the state government.

Medium Term Fiscal Programme, 2003, of the Government of Punjab lays down certain objectives for reducing the revenue deficit as percentage of revenue receipts and fiscal deficit as a percentage of GSDP. The targets are compared with the achievements as brought out in Medium Term Fiscal Reform Programme, 2004, on the basis of actuals of 2002-03, revised estimates (RE) of 2003-04, budget estimates (BE) for 2004-05 and projected estimates for 2005-06 in the following table:

Table 9: Review of Fiscal Reform Programme

(figures in percentages)

Year	Objectives (MTFP 2003)		Achievements (MTFRP 2004)	
	RD/RR	**FD/GSDP**	**RD/RR**	**FD/GSDP**
2002-03	27.35 (RE)	6.05 (RE)	33.91 (Actuals)	6.03 (Actuals)
2003-04	24.45	6.05	25.88 (RE)	7.23 (RE)
2004-05	20.63	5.23	21.96 (BE)	6.79 (BE)
2005-06	16.72	4.47	22.60 (Projected)	6.07 (Projected)

The government has failed to reduce the revenue deficit as a proportion of revenue receipts in 2002-03, whereas it has been successful in reducing the fiscal deficit to GSDP ratio marginally. But the data for the subsequent years reflect that none of the objectives are likely to be met. This brings to focus the fact that the government is not paying much attention towards achieving the objectives laid down in the MTFP 2003. Also the objectives in MTFRP 2004 show that these have been revised upwards so as to create a favourable impression.

The report of the CAG corroborates that according to the MoU (April, 1999), the revenue deficit as a proportion of revenue receipts was to be reduced by 5 percent each year from 1999-2000. Accordingly, the revenue deficit of 37 percent during 1999-2000 should have been restricted to 32, 27 and 22 percent of revenue receipts during 2000-01, 2001-02 and 2002-03 respectively. The actual deficit, however, after a dip in 2000-01 (25 %) was much above the target and increased to 42 percent and 33.91 percent in 2001-02 and 2002-03 respectively.

A review of FRBMA shows that it does not provide any targets for time bound minimum improvements in investment in human resource development and infrastructure, which are crucial for both equity and rapid economic growth. However, it makes an allowance for not meeting the targets due to calamity declared by the central/state government. It only mentions about the estimate of non-compliance. It provides for an independent agency to carry out the periodic review for the compliance of the provisions of the act. The act does not seriously address the problem of financing public expenditure. In the context of the decline in the tax-GDP ratio during the nineties, targets for an increase in this rate should have been accorded top priority. Not only is there an absence of any such target, but also the need for effectiveness of tax administration and collection is not recognised in the act. The achievement of the targets of revenue and fiscal deficit and a cap on debt and guarantees as given in the FRBMA can be assessed only when the actual data for 2003-04 are available. However, an attempt is made to review the act on the basis of the revised estimates (RE) for 2003-04.

Table 10: FRBMA Compliance

(figures in percent)

	2002-03	2003-04	Change over previous year	Remarks
FD/GSDP*	6.03	7.23	Increase of 1.20	Non-compliance
RD/RR	33.91	25.88	Decline by 8.03	Compliance
Debt/GSDP	50.41	48.30	Decline by 2.11	Inadequate to meet the targets
Guarantees/ RR of previous year	153.80	122.56	Decline by 31.24	Far from 80% cap in the Act

*GSDP for the year 2003-04 has been projected at 11 % over 2002-03 (Quick estimates) as per MTFRP, 2004.

Except for compliance of revenue deficit as proportion of revenue receipts, the government has failed to even remotely adhere to the FRBMA. This reflects the non-seriousness of the government towards its own commitments.

For high growth along with the rapid elimination of the major ills plaguing the Punjab economy, it may not be enough to lay down targets for the revenue surplus and leave it to the government to choose the fiscal deficit it considers appropriate. The reasons brought out by Rakshit (2001) are valid as (i) the same amount of deficit can come about through a wide variety of scale and composition of the government budget, affecting the primary objectives differently; and (ii) given the close connection between fiscal deficit and revenue balances over time, the government may continue to opt for scaling down urgently needed expenditure rather than raise taxes and rationalise prices of publicly provided goods and services. In view of the government's responsibility relating to growth and human resource development, FRBMA could have fixed targets for expenditure in some critical areas with the provision that in case these targets and those of revenue balance are not met, the government must reduce its administrative expenses. At the same time it is also necessary to reduce wastage and plug leakages in the government's expenditure programmes.

The Government of India made a *Medium-Term Review of States' Fiscal Reforms Facility* for the period 2000-01 to 2004-05. Accordingly, on the basis of the performance of each state on a single monitorable indicator, i.e., revenue deficit as a percentage of revenue receipts, the states are divided into four categories. Punjab is placed in category III – initial improvement and then deterioration, on the basis of revenue surplus/deficit as percentage of revenue receipts. As per the given data, Punjab always had a higher revenue deficit as percentage of revenue receipts as against the all-India average between 1999-2000 and 2002-03. In 2001-02, the deficit of Punjab was double of that for all states. According to the formula used by the GoI, the 'non-special category' states whose ratio of consolidated debt to revenue receipts exceeds 300 percent are considered as 'highly stressed' states in terms of debt and debt servicing. Punjab, unfortunately, falls in this category.

RBI study of State budgets for the year 2003-04 ranks the states on the basis of various indicators of fiscal effort. The status of Punjab is given as follows:

- In terms of growth rate in RR and TE of 2003-04(B.E.) over 2002-03 (R.E.), Punjab has lower rate of growth in terms of both.
- Punjab figures in the highest category, i.e., above 25 percent in terms of interest payments to RR ratio (average for 1996-2002).
- Punjab falls in the medium range of 10-15 percent average annual rate of growth in debt during 2001-02 to 2003-04.
- However, the debt-NSDP ratio for 2001-02 is above 50 percent, i.e., Punjab falls in the highest category.

The Medium-term Review of States' Fiscal Reforms Facility and the RBI study affirm the critical fiscal situation in Punjab as already discussed in section III.

VI. Conclusions

A perusal of the finances of the Government of Punjab shows large revenue and fiscal deficit year after year indicating continued macro fiscal imbalances of the state. Increasing dependence on the RBI and the continuous application of borrowed funds largely on current consumption and debt servicing indicates unsustainability and reflects vulnerability of the state finances. An increase in the ratio of fiscal liabilities to GSDP together with a large revenue deficit indicates that the state is gradually getting into a debt trap. Thus the state needs to generate more revenue out of its existing assets. Only through reducing revenue/fiscal deficit by compressing non-developmental expenditure in a medium-term framework, prudential debt management, and transparency in fiscal operations, can long term fiscal stability be achieved.

The systematic failure in Punjab is discernible as reflected by its declining growth rate and unfavourable fiscal parameters. The assessment of the entire fiscal reform process in the state reflects that the government has failed to honour its own commitments from time to time and has also shown utter disregard for certain constitutional provisions. The non-transparencies in the utilisation of funds are all too obvious. So a mere enactment of acts and legislations is not enough to put the once glorious economy of Punjab on the path of socio-economic development so much associated with the state.

Fiscal imbalances in the state, to a great extent, have been the result of lack of transparency and accountability. Non-transparent tax concession, quasi-fiscal subsidies and off-budget spending all contribute to such imbalances. Fiscal transparency requires a high degree of fiscal marksmanship. It also consists of a transparent regulatory framework, open public procurement and employment practices, a code of conduct for officials and published performance audits. Restoration of financial discipline calls for bringing in all extra-budgetary transactions into the consolidated fund. The application of funds outside the consolidated fund should be subjected to the same rigours as the budgeting process through appropriate auditing mechanisms and periodic reviews. A restructuring of government expenditure needs to focus on its functional aspects and eliminate programmes that are no longer relevant. A reduction in subsidies by increasing user charges for services delivered is another step towards fiscal consolidation. Unless the state's finances are looked at in totality on a continuous basis and come up for close scrutiny in the legislature and outside, it will be difficult to ensure adequate transparency and accountability.

The state has to pursue the fiscal reform programme towards achieving fiscal balance and consolidation and generation of quality infrastructure and competitive environment. This will be met with stiff opposition from various quarters and will be an arduous task. But the success of the entire reform programme depends on how far the government is able to resist the temptation for populist measures. If the government continues to succumb to the populist political pressure, the fiscal crisis in Punjab will only deepen. The enactment of the legal and constitutional changes ensures some semblance of financial discipline on a sustainable basis. But the *Fiscal Responsibility and Budget Management Act* can be successful only if government is held to account by civil society comprising media, academics, and public. In order to achieve the desired goals, political will, administrative competence and good governance are necessary.

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