Executive Summary

INTRODUCTION

Delhi is a union territory with a legislature. Created under the provisions of the *Constitution (sixty-ninth) Amendment Act, 1991* and the Government of *National Capital Territory of Delhi Act, 1991*, Delhi is uniquely positioned in the demographic, economic, and fiscal set-up of the country. Delhi is overwhelmingly urban with strong trends towards further strengthening of its urban base. Its per capita income of Rs. 21. 175 in 1995–96 was 78–90 percent higher than the all-India average and about 35–45 percent higher than the average for the five high income states. Delhi is endowed with a vibrant small scale manufacturing and a buoyant trade and distribution sector, which contributes most of its gross small domestic product (GSDP). The share of agriculture and other primary sector activities in Delhi's GSDP is only 2.8 percent.

At the same time, the incidence of poverty as measured by the calorie intake criterion is widespread in Delhi, and has, in fact, risen from 12.41 percent in 1987–88 to 14.69 percent in 1993–94. Non-food poverty as indicated by approximately 30 percent of households living in slum and squatter settlements and large proportion of households who have no access to water supply, basic sanitation, and electricity, together with pollution levels which are among the highest in the country are a matter of serious concern, particularly in the context of Delhi's high density and pattern of settlements. These also underlie the relatively high birth and death rates, high infant mortality rates, and an illiteracy level of 26 percent.

Delhi has a special functional and fiscal arrangement with the central government which imparts to it certain fiscal advantages. Under the arrangement, the central government continues to shoulder expenditure responsibilities in respect of public order, police, and land. With Delhi enjoying essentially the same tax jurisdiction as is available to states under the constitutional division of tax powers and a grant in lieu of a share in central taxes, Delhi has been able to maintain a surplus on revenue account. Owing to Delhi being a union territory, it is permitted to borrow only from the central government. Although perceived as a fiscal disadvantage, this arrangement has helped the Government of Delhi to keep its debt burdens within sustainable limits. The finances of Delhi are thus vitally influenced by its unique position in the Indian union.

Besides the Government, the three major public utilities, namely, the Delhi Transport Corporation (DTC), the Delhi Vidyut Board (DVB), and the Delhi Water Board (DWB), and the two local bodies of the Municipal Corporation of Delhi (MCD) and the New Delhi Municipal Committee (NDMC) play vital roles in the governance of this territory. The importance of public utilities and local bodies in Delhi's socio-economic development can be gauged by the fact that in 1996–97 their combined recurring expenditure formed 9.8 percent of GSDP which was a shade higher than the revenue expenditure of the Government of NCT. Although there are seventeen corporations that are concerned with a large array of subjects, their overall impact on Delhi and Delhi's finances is marginal.

THE FINANCES OF THE NATIONAL CAPITAL TERRITORY

For the reason that Delhi's expenditure responsibilities exclude public order, police, and land, the total budgetary expenditure of Delhi is of a lower order compared with other states. In 1996–97, it formed 12.8 percent of Delhi's GSDP or Rs. 2,984 on a per capita basis.

Delhi's fiscal performance is characterised by—

- A moderate and moderately rising component of capital expenditure as distinct from trends in other states which have uniformly observed a fall in capital expenditure, often at the cost of rising revenue expenditure.

- A surplus of 2.78 percent of GSDP on revenue account in 1996–97, explained essentially by a relatively higher revenue base in relation to expenditure responsibilities.

- A fiscal deficit of 2.52 percent of GSDP in 1996–97, generally attributable to the fact that Delhi's borrowing powers are regulated by the central government.

- A significantly lower own revenue to GSDP ratio for Delhi as compared to own revenue to non-agricultural GSDP ratios for other states, suggesting that Delhi has not capitalised on the vast economic opportunities for purposes of revenue raising.

- A virtual non-existence of the non-tax component of revenues, raising questions about the government's capacity to forge better cost-price linkages for the numerous services that it provides.

- Persistence of a large underexploited sales tax sector, notwithstanding a series of measures that have been taken by the government to simplify and rationalise the system of taxing the sales transactions.

- Falling buoyancies of such sources of revenues as state excise, stamp duties and taxes on motor vehicles, pointing out to substantial weakness in their administration and enforcement.

- Insufficient investment in roads, urban development, and environment sectors, and absence of policies and strategies towards (a) the role of roads in economic development; and (b) slums. In the development of the existing policy framework, environment does not enjoy the order of priority that it deserves.

THE FINANCES OF PUBLIC UTILITIES

The finances of the Delhi Transport Corporation (DTC), the Delhi Vidyut Board (DVB), and the Delhi Water Board are in a dismal state. In 1996–97, their combined losses amounted to Rs. 2,708 crore or 9.8 percent of GSDP.

Infrequent revision of bus fares, a large segment of population that receives subsidies in the form of concessional tickets, overstaffing, and accumulated interest liabilities underlie the losses of DTC. The DVB which purchases 60–70 percent of electricity from outside, suffers from large transmission and distributional losses, the Board's inability to adjust the tariff with the cost of electricity production and distribution, and poor management. The problems of the DWB are identical to that of the DVB: leakages and distributional losses, lagging water charges in relation to costs, and lack of investment in improving the internal network of water distribution.

THE FINANCES OF LOCAL BODIES

The Municipal Corporation of Delhi (MCD) and the New Delhi Municipal Committee (NDMC) together with the Delhi Cantonment Board are responsible for providing essential services to Delhi. The tax base of MCD is typically local, consisting of property taxes, a duty on transfer of property, tax on consumption, sale and supply of electricity, a tax on advertisement, and a tax on non-motorised vehicles. Property tax system which accounts for 63 percent of MCD's total revenues is clogged on account of its continued linkage with the *Rent Control Act*, obsolete exemption and rebate policy, and an absence of a mechanism to undertake periodic revaluation of properties, with the result that the yield from property taxes is a fraction of its potential. The rate structure of other taxes and fees is unrelated to the cost incurred on their administration and enforcement.

THE FISCAL CHALLENGE: THE NEXT FIVE YEARS

Unlike many states where the reform agenda aims to correct fiscal imbalances, Delhi's reform agenda is designed to shore up additional revenues for meeting the investment requirements of underfunded sectors, major overhauling of public utilities, and restructuring of the local finance system. Given the urban and economic base and Delhi's position as a trade and distribution node, it possesses the potential of setting a pace and direction for other states to follow. The suggested reform agenda for Delhi consists of the following:

- Acceleration in the reform of sales tax system. Sales tax is the most important source of revenue for the Government of NCT. Beginning with rationalisation of the rate structure of sales tax, a series of steps to widen the network and simplification of registration system have been taken by the government to augment receipts from sales tax. In principle, the government have also accepted to introduce the value added tax (VAT) in Delhi. There is an urgent need to speed up the process of reform of this tax including the changeover to a system of VAT.

- Other tax sources of revenues, in particular, stamp duty and motor vehicle taxes are grossly underused and underexploited. The existing practice of a one-time motor vehicle tax and that too at an abysmally low level needs to be jettisoned in favour of first, a tax rate which is commensurate with market rates, and second, the frequency at which it is to be levied.

- Tax financing of activities which can be better financed by charges is strongly advocated for reducing subsidies and improving resource allocation. This task should be taken up in phases.

- Doubling of capital and revenue budgeted expenditure for roads and urban development, and dedicated allocation of 0.5 percent of GSDP for environment. This will significantly improve the long run productivity and competitiveness of this territory, and enhance the quality of life of citizens in Delhi. Simultaneously, steps need to be taken to formulate policies for these sectors.

- The reform agenda for DVB including privatisation and periodic tariff adjustment has long been under consideration. Success of the agenda, however, is dependent on reduction of distributional losses to technical levels. The same prescription would apply to DWB. The DTC has to be downsized to prescribed norms of 8 persons per bus, and provide for adjusting the bus fares by factoring in the cost of inputs, and allowing the private operators to function under appropriate regulations.

- While the report of the *Delhi Finance Commission* – a body set up under *Article 243 Y* of the Constitution, is under consideration, there is an urgent need to change the system of property taxation in a way that it is able to capture the appreciation in property values, and revise the rates of other taxes to cover at least the administrative cost.

Three sets of estimates have been developed to ascertain the impact of the reform agenda on the finances of the Government of NCT. The no-change option would reduce the surplus on revenue account to 2.11 percent in the terminal year of the projected period; a second no-change option would increase the fiscal deficit to 2.86 percent of GSDP form the present level of 2.52 percent. Acceptance of the reform agenda would mean that the government will need to mobilise additional revenues at the rate of 16.19 percent annually over the five year period, in order to double the expenditure on roads and urban development, assign 0.5 percent of GSDP to environment, and keep the revenue surplus and fiscal deficit at 1996–97 levels. It assumes that expenditure on wages and salaries will be contained at 1996–97 level.

Non-fiscal reform agenda includes a substantial review of slum policy and statutory provision in the *MCD Act* for the preparation of an annual report on environment in Delhi.

The Government of Delhi should immediately resume the preparation of economic and functional classification of finance accounts, with a view to understand the long run behaviour of expenditure on wages and salaries and interest payments. Non-availability of this data has hampered making any recommendation on this important component of expenditure.