# Lesson – 29

# Government and the Budget


## Summary

A government budget is an annual financial statement where an itemized estimate of revenue expected and expenditure anticipated are listed for the current fiscal year which runs from April 1 of one year to March 31 of the next year. In India, government budget is normally presented in the Parliament in the month of February every year. Before the budget is presented, for many days there are speculations among people about the expected changes in various taxes. Are the rates of income tax going to be increased or decreased? Let us discuss about structure of 'Govt. Budget'.

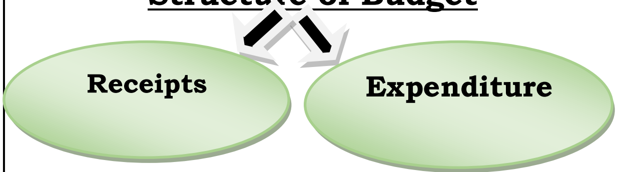

## What is Government Budget

"A budget is a consolidated financial statement prepared by government on expected public expenditure and public revenue during a financial year."

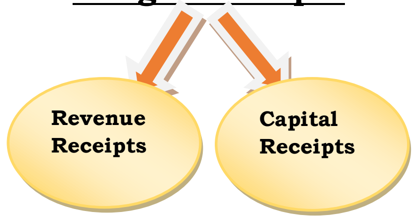
Three main features of a government budget-

- One, it is a consolidated financial statement of expected expenditures and various sources of revenue of government.
- Two, it relates to a financial year
- Three, the expenditures and the sources of revenue are planned in accordance with the declared policy objectives of government.

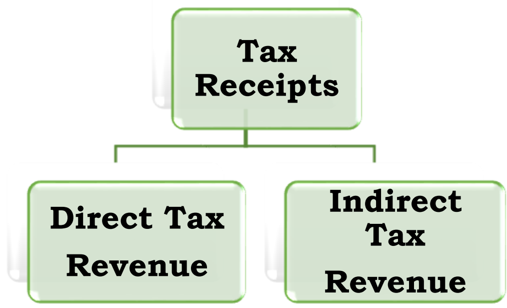
**Structure of Budget**




**Budget Receipts**




**Revenue Receipts**


**Direct Tax Revenue –**

Direct taxes, the liability of payment and the burden of the tax falls on the same person.

Example of Direct Taxes –

- Income tax: the tax on incomes of individuals
- Corporation tax : the tax on corporate profits
- Wealth tax: the tax on wealth of individuals
- Gift tax: the tax on gifts given

**Indirect Tax Revenue**

Unlike direct taxes, indirect tax is not levied on the income, revenue or profit of the taxpayer and can be passed on from one individual to another.

Example of Indirect Taxes –

- Value added tax
- Excise duty: the tax on goods manufactured in factories
- Customs duty: the tax on imports and exports
- Service tax: the tax on the services provided

**Non-Tax Receipts**

The incomes accruing to government from sources other than taxes are non-tax revenues. The major sources of non-tax revenues of the central government of India are – **Commercial Revenue and Administrative Revenue.**

**Commercial Revenue** - It is received by government in the form of prices paid by people for goods and services that government provides e.g. people pay for electricity and for services of Railways, postal stamps, toll etc.

**Administrative Revenue -** It arises on account of administrative services of the govt. They are as follows -

- Fees in the form of passport fees, government hospital fees, education fees, court fee, etc
- Fine and penalites: charged by government on law-breakers for disobeying rules and regulations
- Licence fee and permit
- Escheat : Income that government get by taking possession of property which has no legal claimant or legal heir
- Interest receipts
- profits of public sector

**Capital Receipts**

Capital receipts are those receipts of the government which either create liability or cause any reduction in the assets of the government.

**A. Borrowing**

There are two sources from which the central government borrows. They are –

**Domestic Borrowings –**

Government borrows from people through various deposit schemes such as Public Provident Fund, Small Savings Schemes, and National Savings Scheme etc. These are borrowings of the government within the country.

**External Borrowings**

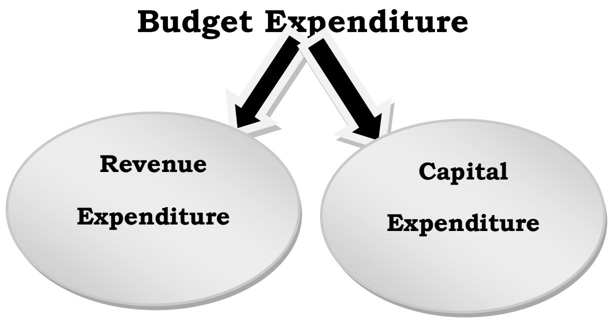
Government also borrows from foreign governments and international bodies like International Monetary Fund (IMF), World Bank etc.

**B. Recovery of Loans**

The loans recovered by the central government from state and local governments are capital receipts in the budget because recovery of loans reduces debtors (assets).

**C. Disinvestment** –

The selling of shares of public sector undertakings by the government is known as 'disinvestment of public sector undertakings'.




**Revenue Expenditure**

When government incurs expenditure that **neither creates any asset nor reduces any liability,** such expenditure is known as revenue expenditure.

For Example, payment of salaries to government employees, maintenance of public property, providing free education and health services to people, etc constitute revenue expenditure.

These do not create any public asset.

**Capital Expenditure**

When government incurs expenditure to **create assets** such as school and hospital buildings, roads bridges, canals, railway lines etc., or **reduce its liability** such as repayment of loan etc., such expenditure is known as capital expenditure.

**Plan Expenditure and Non-Plan Expenditure**

**Plan Expenditure**

Under planning, provisions were made in the government budget for expenditure that was to be incurred every year according to the priorities laid down in the five-year plans. Such expenditure is known as plan expenditure.

**Non-Plan Expenditure**

Government also incurs routine expenditure such as expenditure on police, judiciary, water supply, sanitation and health, legislatures, defence, various government departments, etc. Such routine expenditure is termed as non-plan expenditure.

## Balanced Budget Vs Deficit Budget or Surplus Budget

**Balanced Budget**

When the government expenditure is exactly equal to its receipts, the government has balanced budget.

Total Budgeted Receipt = Total Budgeted Expenditure

**Deficit Budget**

When the government expenditure exceeds its receipts, it is deficit budget

Total Budgeted Receipts < Total Budgeted Expenditure

**Surplus budget**

When the government revenue is greater than its expenditure, the government runs a budget surplus.

Total Budgeted Receipts > Total Budgeted Expenditure

## Types of Budget Deficit

**Revenue Deficit –**

It refers to the excess of total revenue expenditure of the government over its total revenue receipts.

**Revenue deficit** = Total Revenue expenditure – Total Revenue receipts

Or

Revenue deficit = Total Revenue expenditure – (Tax Revenue + Non Tax Revenue)

**Fiscal Deficit -**

Fiscal deficit is defined as excess of total expenditure over total receipts excluding borrowings during a fiscal year.

**Fiscal deficit** = Total budget expenditure – Total budget receipts excluding borrowings

Or

**Fiscal Deficit** = (Revenue expenditure + Capital expenditure) – (Revenue Receipts + Capital receipts excluding borrowings)

Fiscal deficit shows the borrowing requirements of the govt. during the budget year. Fiscal deficit reflects the borrowing requirements of the govt. for financing the expenditure including interest payments.

**Fiscal deficit** = Revenue expenditure + capital expenditure – Revenue receipts – capital Receipts excluding borrowings

Or

**Fiscal deficit** = Revenue expenditure + capital expenditure – Tax Revenue – Non Tax Revenue – recovery of loans – disinvestment

Or

**Fiscal deficit** = Total borrowing requirement of the government

**Primary Deficit -**

Primary deficit is defined as fiscal deficit minus interest payments. Primary deficit shows the borrowing requirements of the govt. for meeting expenditure excluding interest payment.

**Gross Primary deficit** = Fiscal deficit – Interest payments

And

**Net Primary deficit** = Fiscal deficit + Interest received – Interest payments

There are three ways by which the central government finances deficit. These are –

- Borrowing from Public and Foreign Governments
- Withdrawing Cash Balances held with the Reserve Bank of India (R.B.I.)
- Borrowing from the Reserve Bank of India (R.B.I)

**Budgetary Policy (Fiscal Policy**

**Objectives of Budgetry Policy**

- To promote economic growth
- To reduce income and wealth inequalities
- To provide employment opportunities
- To ensure stability in prices
- To correct balance of payments deficit
- To provide for effective administration

**Evaluate Yourself**

Q. Distinguish between revenue receipt and capital receipt with example.

Q. List out the objectives of budgetry policy.

Q. Define the following terms – Revenue Deficit, Fiscal Deficit, Primary Deficit with expression.

Q. Suggest three ways through witch budgetry deficit is financed by the government.