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The Government: Functions and Scope

COMPONENTS OF THE GOVERNMENT BUDGET

There is a constitutional requirement in India (Article 112) to present before the Parliament a statement of estimated receipts and expenditures of the government in respect of every financial year which runs from 1 April to 31 March. This 'Annual Financial Statement' constitutes the main budget document. Further, the budget must distinguish expenditure on the revenue account from other expenditures. Therefore, the budget comprises of the (a) Revenue Budget and the (b) Capital Budget (Refer Chart 1).

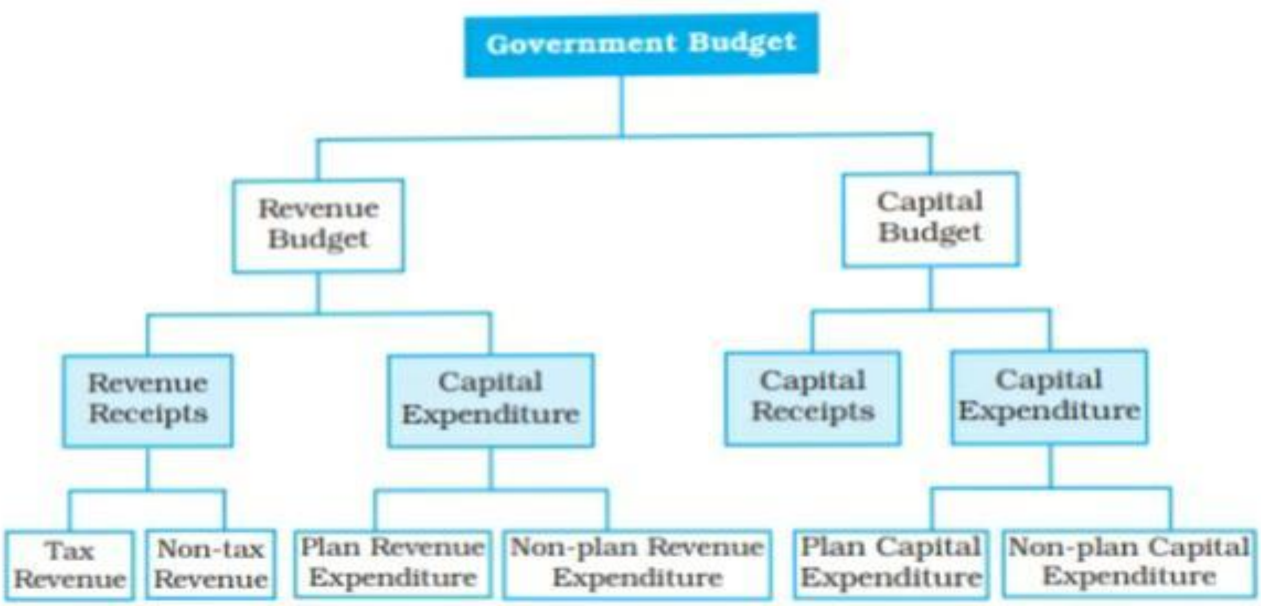

Chart 1: The Components of the Government Budget

The Revenue Account

The Revenue Budget shows the current receipts of the government and the expenditure that can be met from these receipts.

Revenue Receipts: Revenue receipts are divided into tax and non-tax revenues. Tax revenues consist of the proceeds of taxes and other duties levied by the central government. Tax revenues, an important component of revenue receipts, comprise of direct taxes – which fall directly on individuals (personal income tax) and firms (corporation tax), and indirect taxes like excise taxes (duties levied on goods produced within the country), customs duties (taxes imposed on goods imported into and exported out of India) and service tax. Excise taxes are the single largest revenue earner contributing 35.7 per cent of total tax revenue in 2003-04. Other direct taxes like wealth tax, gift tax and estate duty (now abolished) have never been of much significance in terms of revenue yield and have thus been referred to as 'paper taxes'. Two new taxes – the fringe benefits tax (on those benefits enjoyed collectively by the employees) and on cash withdrawals from banks over a certain threshold in a day – were introduced in the budget for 2005-06. The share of direct taxes in gross tax revenue has increased from 19.1 per cent in 1990-91 to 41.3 per cent in 2003-04. There has been a reduction in the share of indirect tax revenue, falling from 78.4 per cent in 1990-91 to 57.9 per cent in 2003-04.

The redistribution objective is sought to be achieved through progressive income taxation, in which higher the income, higher is the tax rate. Firms are taxed on a proportional basis, where the tax rate is a particular proportion of profits. With respect to excise taxes, necessities of life are exempted or taxed at low rates, comforts and semi-luxuries are moderately taxed, and luxuries, tobacco and petroleum products are taxed heavily.

Non-tax revenue of the central government mainly consists of interest receipts (on account of loans by the central government which constitutes the single largest item of non-tax revenue), dividends and profits on investments made by the government, fees and other receipts for services rendered by the government. Cash grants-in-aid from foreign countries and international organisations are also included.

The estimates of revenue receipts take into account the effects of tax proposals made in the Finance Bill1.