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Some Aspects of Karnataka State Finances: A Critical Analysis

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Abstract

In Indian fiscal federalism states play important role by shouldering responsibility of social and economic development activities. With the progress in economic development, fiscal burden of states is increasing over the years. On the other hand, fiscal sector reforms like introduction of GST have affected the revenues of states. As a result, most of the state governments are finding it difficult to manage finances effectively. This paper tries to analyse the financial position of Karnataka state by taking into consideration revenue and expenditure aspects. It is concluded that due to proactive policies and efficient fiscal management Karnataka state was able sustain prudent fiscal management

Key words: Fiscal federalism, revenues, public expenditure, fiscal management.

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1.Introduction

India is a model country for fiscal federalism. Constitution of India well demarcates the boundaries of fiscal federalism. The constitution provides for division of functional domains and resource raising powers between centre and states as per central list, state list and concurrent list. The states in the federal system are entrusted with major responsibilities of development expenditure such as agricultural development, infrastructure, poverty alleviation, water supply and irrigation, public order, public health, and sanitation as well as in the sphere of administrative expenditure such as general administration, law, and order etc. States also have important responsibilities in the areas of concurrent jurisdiction such as education, electricity, economic and social planning and family planning. In nutshell constitution framers expected a major role for state governments in the sphere of social and economic development. As result today state governments in India are engaged in the provision of various social and economic services and transfer of resources to the third tier of government – rural and urban local bodies such as municipalities, panchayats. Further, with the introduction of New Economic Policy in 1991 the role of state governments has gradually increased. One estimate puts that at present state governments spend around 60 per cent of the combined expenditure by centre and states on development activities. The States' ability to undertake and perform the developmental functions adequately, effectively, and efficiently is dependent on their fiscal position, which is a function of their efforts in generating resources via tax, non-tax receipts, borrowings and resource transfer from the Central Government. By very nature of revenue and expenditure powers and obligations, states are faced with shortage of resources and consequently their fiscal performance is deteriorating day by day in recent years. However, there are certain bright spots in the fiscal map of India in which some of the state governments like Karnataka government which have put themselves in the fiscal consolidation map and have come out of fiscal mess.

2. Review of literature

Several studies on State finances in India have been conducted since long time and these studies have observed that over a long period of time, revenue receipts of the states have generally been lower than their expenditures, leading to high levels of revenue and fiscal deficits (Karnik, 2005; Vadra, 2010 and Dasgupta, 2012). Kishore and Prasad (2007) observed that growing interest burden, increasing pension liabilities, unrestrained administrative expenditure, losses incurred by State Public Sector Undertakings (PSUs), inadequate tax buoyancy, and inappropriate user charges led to divergence in growth of receipts and expenditure and hence, created fiscal deficits. Various competent authorities—such as the Finance Commission (FC), Reserve Bank of India (RBI), and Comptroller and Auditor General of India (CAG)—in their recent reports have repeatedly warned against the unsound financial practices of states (Rajaraman et.al. 2005). Rao (2002) observed that transition from plan to market based development since1991 has envisaged greater role for state governments in providing physical and social infrastructure and creating accommodating investment climate. Liu and Webb (2011) observed, "When SNGs follow unsustainable fiscal policy, it can jeopardize the services they manage the safety of the financial system, the country's international creditworthiness, and overall macroeconomic stability. Too often the central government then gets dragged in to provide bailouts, which can disrupt its own fiscal sustainability and reward the populist fiscal tactics of the recipient SNGs." Against this background, the Twelfth Finance Commission (TwFC)recommended a three-pronged strategy to alleviate States' fiscal distress—subjecting States to greater market discipline, rewarding States for fiscal consolidation targets achieved by providing debt and interest rate relief, and making statutory commitments to fiscal correction by passing of fiscal responsibility legislation. Fiscal performance of national and state governments is an important measure to assess the macro-economic stability. There are plethora of studies analysing finances of centre as well as combined finances of all states but there are very few studies analysing finances of individual state. Hence state level studies are imperative to put centre state finances in perspective, to understand constraints faced by states and to have a comprehensive analysis of stability and sustainability. In view of the above, present study was undertaken to understand the fiscal position of Karnataka state.

3.Objectives of the study

The study was undertaken to attain following objectives

1. To analyse the composition and trends in the growth of revenue of Karnataka government.
2. To analyse the composition and trends in the growth of public expenditure of Government of Karnataka
3. To analyse the financial situation of the Karnataka Government.
4. To list out the causes for the rapid growth of public expenditure.
5. To suggest suitable policy prescriptions for the improvement of financial situation of the state government

4.Methodology and Data Source

Current study is analytical in nature; therefore, it strives to analyse the fiscal situation of the state government by taking into consideration the revenue, expenditure and fiscal deficit aspects of Government of Karnataka. Ten-year period starting from 2011-12 to 2020-21 has been taken into consideration for analysis. Data required for the study was sourced from publications of Finance Department of GOK, Annual Economic Surveys. Simple statistical tools such as percentage, growth rate etc. were used to analyse the data and draw conclusions.

5. Some Aspects of Karnataka State Finances

A) Trends in Revenue and Capital Receipts in Karnataka

By definition, total revenue receipts of state government include four major components: own tax revenue, non- tax revenue, devolution from the Central Government and Grants-in- Aid & contributions. The analysis of revenue receipts of Karnataka government (Table-1) shows that large chunk of revenue receipts of the state comes from state's own tax revenue which constitute 66 % of state's revenue receipts in a year. The tax devolution from Government of India constitutes second important source (almost 17%) of revenue receipts. The lowest contributor to the revenue receipts is coming from the non-tax revenue (5%). The rest of the revenue receipts is in the form of Grants - in - aid from Central Government. The State's own tax revenues (SOTR), which is identified as a crucial parameter to understand the fiscal strength of the state, is healthy as far as Karnataka state is concerned.

Table-1: Trends in Revenue and Capital Receipts in Karnataka (2011-12 to 2020-21)

(Rs. in Crores)

Year	State's Own Tax Revenues	% of Total Revenue Receipts	Share in Central Taxes	% of Total Revenue Receipts	Total Tax Receipts	Total Non-Tax Receipts	% of Total Revenue Receipts	Total Revenue Receipts	Total Capital Receipts*	AggregateReceipts
2011-12	46476.01	66.57	11074.99	15.86	57551.00	4086.86	5.85	69806.27	15317.53	85123.80
2012-13	53753.56	68.75	12647.14	16.17	66400.70	3966.11	5.07	78176.22	16878.51	95054.73
2013-14	62603.54	69.91	13808.27	15.42	76411.81	4031.89	4.50	89542.52	19533.42	109075.94
2014-15	70180.30	67.38	14654.14	14.07	84834.44	4688.24	4.50	104142.13	21994.02	126136.15
2015-16	75566.45	63.59	23967.07	20.17	99533.52	5355.04	4.50	118817.31	22337.72	141155.03
2016-17	82956.21	62.27	28759.86	21.58	111716.07	5794.53	4.34	133213.79	32405.92	165619.71
2017-18	93376.34	63.52	31751.98	21.60	125128.32	6476.53	4.40	146999.63	35384.55	182384.18

2018-19	107667.09	65.26	35811.28	21.70	143478.52	6773.00	4.10	164978.52	42399.55	207461.74
2019-20	116879.29	66.61	30899.42	17.61	147778.68	7681.47	4.37	175442.79	42952.25	218395.04
2020-21	110862.79	70.74	21673.11	13.82	132535.90	7893.84	5.03	156716.41	71252.66	227969.07

Source: Annual Financial Statements-2011-12 to 2020-21, Finance Department GoK & author's calculation

B) Trends in Public Expenditure

Trends in public expenditure of Karnataka state is presented in the table-2. Expenditure of the Karnataka state government are broadly classified into two categories i.e., Developmental expenditure and non-developmental expenditure. Developmental expenditure constitutes the expenditure incurred on the development of economic and social sector activities such as agriculture, industry, tertiary sector activities, education, health etc. The analysis of the data reveals that developmental expenditure of government of Karnataka over the decade constitute the major chunk of expenditure. Data shows that the share of development expenditure in aggregate expenditure is almost 72 %. On the other hand, expenditure on non-developmental activities such as general services, pension, fiscal services, interest payment etc. constitute 27 % of the aggregate expenditure. Further, the analysis of the data reveals that this pattern of public expenditure of the state government has remained same thought the decade. Thus, despite of the efforts of the state government to enhance the share of developmental expenditure in recent years non-developmental expenditure is dragging the feet.

Table-2: Trends in Public Expenditure in Karnataka

(Rs. in Crores)

Year	Developmental Expenditure	Developmental Expenditure as % of Total Expenditure	Non-Developmental Expenditure	Non-Developmental Expenditure as % of Total Expenditure	Aggregate Expenditure
2011-12	60929.69	72.14	23533.97	27.86	84463.66
2012-13	68067.53	71.66	26922.26	28.34	94989.79
2013-14	76328.45	69.99	32729.25	30.01	109057.70
2014-15	88904.73	70.44	37312.82	29.56	126217.55
2015-16	100440.69	71.12	40794.06	28.88	141234.75
2016-17	123989.38	74.94	41455.39	25.06	165444.77
2017-18	136285.13	73.09	50177.82	26.91	186462.95
2018-19	154527.55	74.61	52584.47	25.39	207112.02

2019-20	157822.41	72.49	59903.41	27.51	217725.82
2020-21	162219.00	71.13	65825.87	28.87	228044.87

Source: Annual Financial Statements-2011-12 to 2020-21, Finance Department GoK & author's calculation

C)Expenditure Indicators in Karnataka

To throw more light on the expenditure of the state government, expenditure indicators in Karnataka for the year 2020-21 is presented in the following table.

Table -3: Expenditure Indicators in Karnataka (% of GSDP)

Particulars	2020-21
Revenue Receipts	8.69
Revenue Expenditure (RE)	9.76
Development Expenditure	8.99
Social Services	4.06
Economic Services	4.78
General Services	3.12
Interest Payments	1.22
Wage Bill	1.77
Pensions	1.05
Capital Outlay (Outside the revenue Account)	3.28
Total Expenditure (RE+CE)	12.28
Outstanding Debt	21.35
Total Consolidated Fund	13.04

Source: Annual Financial Statement 2020-21, Finance Department, GoK,

D) Conclusion

From the above analysis of fiscal situation in the state of Karnataka it can be concluded that the finances of the state government have come under pressure like all India trends. However, with some prudent fiscal management, the state could ensure that the fiscal situation does not derail as happened in the case of many states. This is evident from the fact that fiscal deficit of state government has not crossed 3.5 percent of GSDP. However, ensuring the quality of public expenditure, improving its efficiency and rationalization of subsidies, decline in the share of state in the central government devolution plan and with GST in place, the pressure on state's own tax revenue has increased manifolds. Further, with decline in the grants-in-aid, the state is in dire need to look for alternative sources of revenues. One way that the state could do is to improve the tax administration through use of IT services to improve the buoyancy.

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