

# Fiscal Discipline: A Case Study of Odisha's Compliance with FRBM Act 2003

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**Abstract:** This research delves into the fiscal discipline landscape, focusing on the compliance of the Indian state of Odisha with the Fiscal Responsibility and Budget Management (FRBM) Act of 2003. As the FRBM Act serves as a crucial framework for fiscal management, this case study explores the extent to which Odisha adheres to the stipulated fiscal targets, debt control measures, and overall fiscal prudence outlined in the Act. The study employs a comprehensive qualitative analysis of budgetary data, debt indicators, and fiscal performance metrics. By scrutinizing Odisha's adherence to the FRBM Act, this research aims to provide valuable insights into the effectiveness of fiscal policies and the state's commitment to sustainable and disciplined financial management.

**Keywords:** Revenue Deficit, Fiscal Deficit, FRBM Act, Fiscal Discipline.

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## 1. INTRODUCTION

India as a welfare state where government revenues and expenditures are harnessed to promote social welfare, fiscal management plays an important role in the macroeconomic stability and development of nation. This is very essential to ensure that public resources are allocated efficiently and public debt is sustainable. Effective fiscal management is imperative for several reasons for example it provides tools to government to address business cycle and stimulate growth during downturns and manage inflation during upswings.

In 2000 the fiscal situation of Government of India had worsened and the Gross Fiscal Deficit reached up to 6% of GDP. Government set up committee chaired by Dr. E.A. S. Sharma to offer way forward. Based on the recommendations of committee Government enacted the FRBM Act 2003 which came into force in 2004. It provides institutional framework for fiscal consolidation. It is now mandatory for the Central Government as well as State Government to take measures to reduce fiscal deficit, to eliminate revenue deficit and to generate revenue surplus in the subsequent years. The Act binds not only the present Government but also the future Government to adhere to the path of fiscal consolidation.

As per recent report and review of Comptroller and Auditor General of India Odisha is top performer state followed by Maharashtra and Gujrat as far as the performance of FRBM Act 2003 is concerned. However, it is to be noted that Odisha was considered one of the most fiscally stressed state in late 1990 and early 2000. The report of 12th finance commission stated the debt and fiscal stress of Odisha. The debt to GDP ratio of Odisha in 2002-03 was 50.73% compare to all states. The liquidity position of state was in bad situation. The state had no money to even repair roads and treasuries were closed for most of the days. The super cyclone of 1999 made things worse. When Navin Patnaik took oath as Chief Minister the state was in bad shape. He promised for financial stability in Odisha. From debt ridden state to now top performer it is not an event. Thus, the aim of our study is to assess the fiscal reforms of Odisha state with the help of annual financial statements from 1992-93 to 2021-22.

### FRBM Act 2003

FRBM rule specifies reduction of fiscal deficit to 3% of the GDP by 2008-09 with annual reduction target of 0.3% of GDP per year by Central government. Similarly, revenue deficit has to be reduced by 0.5% of the GDP per year with complete elimination to be achieved by 2008-09. It is the responsibility of the government to adhere to these targets. Finance Minister has to explain the reasons and suggest corrective actions to be taken, in case of breach.

Government can move away from the path of fiscal consolidation only in case of natural calamity, national security and other exceptional grounds which Central Government may specify. It is called escape clause.

Further, the Act prohibits borrowing by the government from Reserve Bank of India, thereby, making monetary policy independent of fiscal policy. The Act bans the purchase of primary issues of the Central Government securities by the RBI after 2006, preventing monetization of government deficit. Act also requires govt to lay before parliament three policy statements in each financial year Medium Term Fiscal Policy Statement, Fiscal Policy Strategy Statement and Macroeconomic Framework Policy Statement.

#### **FRBM (Amendment) Act 2012**

It was decided that in addition to the existing three documents, Central Government shall lay another document the Medium Term Expenditure Framework Statement before both Houses of Parliament in the Session. The amendment act introduced the concept of Effective Revenue Deficit. Central Government may entrust the Comptroller and Auditor General of India to review periodically as required, the compliance of the provisions of FRBM Act and such reviews shall be laid on the table of both Houses of Parliament.

#### **FRBM (Amendment) Act 2015**

The effective revenue deficit which had to be eliminated by March 2015 will now need to be eliminated by March 2018. The 3% target of fiscal deficit to be achieved by 2016-17 has now been shifted by one more year to the end of 2017-18.

#### **N. K. Singh Committee 2016**

In the Union Budget 2016-17 it was proposed to constitute a committee to review the implementation of the FRBM Act and give its recommendations on the way forward. Hence Government constituted the Committee in May 2016 under the Chairmanship of Shri N.K. Singh, former Revenue and Expenditure Secretary. The committee recommended that instead of fixed numbers as fiscal deficit targets, it may be better to have a fiscal deficit range as the target similar to inflation range.

#### **FRBM (Amendment) Act 2021**

Central government shall take measures to limit the fiscal deficit up to 3% of GDP by March 2021. General government debt does not exceed 60% of GDP by 2024-25. The central government debt shall not exceed to 40% of GDP by 2024-25. The state government debt shall not exceed to 20% of GSDP by 2024-25. Any deviation made under escape clause shall not exceed 0.5% of GDP in that year. Further RBI may subscribe to primary issues only on the grounds mentioned in escape clause and no deviation shall be permissible without approval of parliament. Revenue deficit has to be eliminated by 2024-25.

#### **Odisha**

Odisha earlier known as Orissa, an eastern Indian state known for its tribal cultures and its many ancient Hindu temples. It is the eighth largest state by area and the eleventh largest by population with over 41 million inhabitants. The state also has the third largest population of Scheduled Tribes in India. Odisha has abundant natural resources and a large coastline. It has emerged as the most preferred destination for overseas investors with investment proposals. It contains a fifth of India's coal, a quarter of its iron ore, a third of its bauxite reserves and most of the chromite. Rourkela Steel Plant was the first integrated steel plant in the public sector in India built with collaboration of Germany.

#### **State Finances**

GSDP (6.45 Lakh crore) (2021-22)

Growth rate at constant prices at 11.5%. (2021-22)

#### **Sectors Contribution in GSDP**

Primary	29%
Secondary	31%
Service	40%

#### **Unemployment Rate**

As per latest data Odisha is the state with lowest unemployment rate at 0.9%.

### Annual Financial Statement of 2023-24

Finance Minister Mr. Niranjan Pujari presented the annual financial statement for the financial year 2023-24 on February 24, 2023.

Gross State Domestic Product of Odisha for 2023-24 at current prices is projected to be Rs 8.65 lakh crore. Expenditure except debt repayment in 2023-24 is estimated to be Rs 2,11,214 crore, an increase of 14% over the revised estimate of 2022-23. In addition, debt of Rs 18,786 crore will be repaid by the state.

Receipts except loans for 2023-24 are estimated to be Rs 1,85,370 crore, an increase of 13% as compared to the revised estimate of 2022-23. Revenue surplus in 2023-24 is estimated to be 3.1% of GSDP. In 2023-24, the fiscal deficit is estimated to be 3% of GSDP. For 2023-24, the central government has permitted fiscal deficit of up to 3.5% of GSDP to states of which 0.5% of GSDP will be available only upon carrying out certain power sector reforms.

## 2. LITERATURE REVIEW

This chapter of study focuses on literature review. It starts with the theoretical review and then empirical review relevant to the study. The theoretical review is in part one and empirical literature is in part two. It should be noted that other theories related to the study were also reviewed to enhance the scope of the study.

### Theoretical Review

Scholars often discuss various theoretical frameworks related to fiscal discipline. This includes the application of economic theories to understand the impact of fiscal policies on macroeconomic stability. Numerous studies provide empirical evidence on the relationship between fiscal discipline and economic outcomes.

*Dhyani Mehta (2018)* extensive literature on the theoretical and empirical debate between Wagner's law and the Keynesian law attempts to validate the causal relation between public expenditure and GDP.

*Sahani (1984)* examined the link between public expenditure and national income.

*Dholkia (2014)* centre must find the path for fiscal consolidation so that macroeconomic stability will be back in nation.

*Pattnaik (2016)* conferred with the view that quality of fiscal adjustments has been poor at both centre and state. However, state governments were found to be more responsible in eliminating revenue deficit compared to Central Government.

*Reddy (2008)* observed that despite the positive effect of FRBM, it led to expansion of off budget liabilities which could be detrimental to debt and monetary management.

### Empirical Review

*IMF (2016)* public debt is considered sustainable if the government is able to meet all its current and future payment obligations without exceptional financial assistance.

*Balbir Kaur and Anand Mukharjee (2018)* the debt position of the state governments in India, which deteriorated sharply between 1997–1998 and 2003–2004, has witnessed improvement since 2004–2005. Debt sustainability analysis based on empirical estimation indicates that the debt position at the state level is sustainable in the long run.

*Devi Prasad (2017)* there is an immediate requirement for greater transparency in budget preparation, making the medium term framework more binding and greater capacity building on the part of government to promote budgetary and debt management institutions.

*Pujari and R.R. Biradar (2022)* the study recommends that efficient debt management strategy is important for the sustainability of debt and overall financial stability.

## 3. STUDY GAP

The identification of a study gap is crucial for every research as it helps establish the unique contribution of the study. Prior studies on this topic have been more superficial in their nature and lack focused approach. There have been important policy shifts since 1992 that are not well documented and those documented are not well updated. It is to be noted that public finance is a dynamic discipline as it transformed over the time and thus there is need of thread based analysis of annual financial statements of Odisha to enhance scope of study for future use.

#### 4. OBJECTIVES

Primary objective of this study is to assess the fiscal reforms of Odisha state from the perspective of FRBM Act 2003. However, there are some secondary objectives to co check the compliance with the provisions of FRBM Act 2003, to identify loopholes and recommend measures to fiscal correction and to assess the impact of FRBM Act 2003 on the fiscal discipline of state.

#### 5. DATA COLLECTION

Data for the study has been collected from secondary sources such as from Finance Department of Odisha state and Economic Surveys year wise from 1992-93 to 2021-22. This approach involves to extract relevant information and reports. The comprehensive data set of finance department offers a valuable foundation to draw conclusions for this qualitative research and data offered by economic surveys and helps to understand the topic better and making results more reliable.

#### 6. ANALYSIS OF RESULTS

As far as analysis of results are concerned, I have taken parameters as mentioned below.

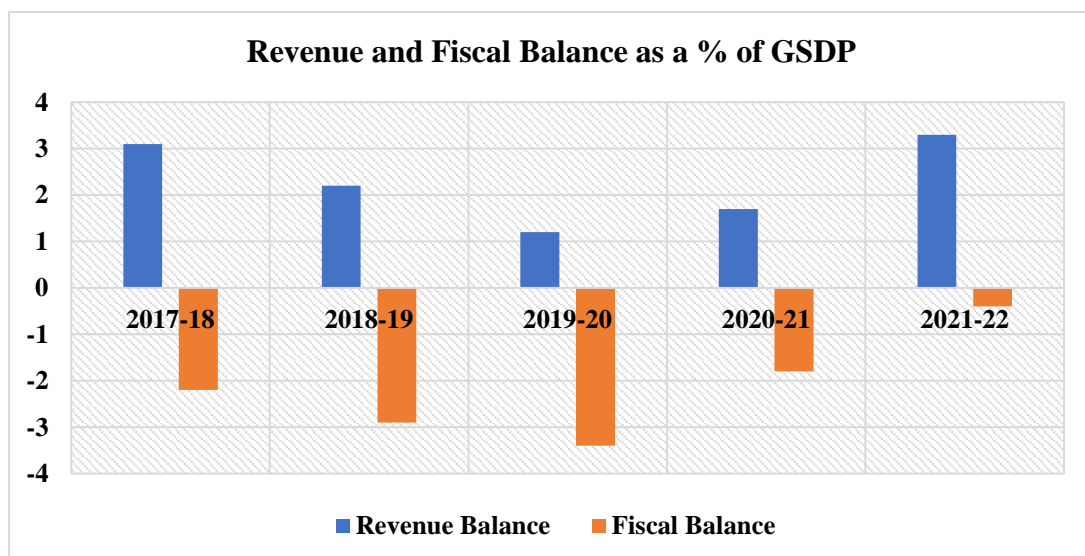
##### Revenue Deficit / Surplus (₹ Crore)

Since 1992-93 Odisha has revenue surplus till 2004-05. In 1992-93 the revenue surplus was 13572 Crore. In 2004-05 the revenue surplus was 522.30 Crore. In 2005 Odisha Government introduced FRBM Act. Since 2005-06 to 2008-09 it faced revenue deficit. In 2005-06 the revenue deficit was 481.20 Crore. In 2007-08 it touched to 4243.93 Crore because of economic downturn and increase in public expenditure. However, in 2009-10 it achieved revenue surplus up to 2369.09 Crore. Since 2009-10 we can see the upward trend in terms of revenue surplus except some years.

##### Fiscal Deficit / Surplus (₹ Crore)

From the analysis we can say that fiscal situation of state has been improved since 1992. In 2004 -05 the fiscal deficit of Odisha was 1366 Crore. In 2005-06 Government took some measures like increase in tax collection efficiency by use of IT tools and introduction of VAT due to this fiscal deficit touched to 276 Crore lower than 2004-05. For the first time the State has been able to generate fiscal surplus of Rs.823.18 crore in 2006-07. Since then, till 2007-08 it achieved fiscal surplus. From 2009-10 Government invested more on capital expenditure in critical sectors so fiscal deficit touched to 2265 Crore. So, the fluctuations in fiscal deficit from surplus to deficit is a positive because Government is efficient in terms of fiscal discipline. In 2021-22 the fiscal surplus of Odisha was 20627 Crore which is about to 3.1% of GSDP of state.

From the below chart we can conclude that from the debt ridden state to revenue surplus is not an event but fiscal measures taken by state to improve the fiscal situation of Odisha state.



Source: Economic Survey of Odisha (2021-22)

Fig 1

## 7. CONCLUSION

From the study we can conclude that Odisha is consistently growing faster than national average even in testing times like Covid19. It has been possible due to policy of government to invest in critical sectors which will not only foster growth but also create an enabling environment for private investment. On an average the state growth has been one percent more than national average since last 10 years. Growth in population is lower than the national average these two factors are contributing to increase in per capita income. Over the years dependence of state on central transfers is gradually decreasing because of robust growth in its own revenue. Mining revenue is one of the Odisha's major sources of revenue. It contributes about 10% of the resource pool of state. This is not because of hinger extraction but because of higher premium. The state has been doing outcome budgeting for more than 10 years. Currently 27 major spending departments are preparing the outcome budget every year. Programme Performance and Outcome Monitoring Unit is providing required technical support to the departments for outcome budgeting and outcome monitoring.

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