Unit V Semester VI

Public Budget

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Q1. Meaning and definitions 7
of Public Budget

Public Budget and Classification

INTRODUCTION

The word 'Budget' is said to have its origin from the French word 'Bougett" which refers ' a small leather bag'. Today, bag itself is not vital but people are anxious to see what the bag contains. Therefore, the bag contains economic bill presented by the Finance Minister in the Parliament House annually. Every democratic government makes vigorous efforts for this end, maximising the welfare of the community in the modern times. In order to achieve, the government takes in hand various socio-economic activities. This requires proper manipulation of the budgetary policy of the government. A budget, therefore, is not only a financial statement of actual and anticipated revenues and outlays of the government but is also a document of detailed programmes and policies of action which they desire to pursue in the coming years for raising the level of economic activity.

WHAT IS PUBLIC BUDGET

Many scholars have defined budget in different ways. According to *Prof. Rene Stourn*, "It is a document containing a preliminary approved plan of public revenue and expenditure." In the words of *Beauliu*, "It is a statement of the estimated receipts and expenses during fixed period; it is a comparative table giving the amounts of the receipt to be realised and the expenses to be incurred; it is furthermore an authorisation or command given by the proper authorities to incur the expenses and collect the revenues."

"(A) Finance Plan (B) A procedure formulating authorizing, executing and controlling this plan and (C) some government authority elements of a budget."

According to *Prof. Bastable*. "The budget has come to mean the financial arrangements of a given period, with the usual implication that they have been submitted to the legislature for approval." *W.E. Willoughby* also states, "A budget is at once a report on estimates and proposals, that it is the instrument by which all the processes of financial administration are correlated and coordinated."

According to *I.C.W.A. London*. "A budget is a financial and/or quantitative statement prepared prior to a defined period of time, of the policy to be pursued during that period for the purpose of attaining a given objective." In the words of *Crown and Howard*, "A budget is a pre-determined statement of management policy during a given period which provides a standard for comparison with the results actually achieved."

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These definitions show that public budget contains the following features.

(i) It is a statement of expected revenue proposed expenditure of the public authorities concerned.

(ii) It possesses periodicity which is generally in one current year.

(iii) It has a sanction of public authority.

(iv) Budget proposals should be clear.

(v) It sets procedure in which the collection of revenue and administration of expenditures is to be executed.

(iv) The anticipations of revenue and expenditures should make positive contribution to economic goal.

Q2 PURPOSE OF THE BUDGET / Objectives of P. Budget Unit V

Public budget is considered sin-quo-non of the modern Govt. as it provides the detailed information of revenue and expenditure in a particular period. However, its purpose is under mentioned :

1. Necessity of Planning. To achieve any purpose, a planning is necessary. The government needs to achieve many goals all of which cannot be attained at a time. A proper plan of action is, therefore, necessary. A budget is such a plan which explicitly mentions the programmes that are to be taken up in the course of the fiscal year.

2. Necessity of Time. Different programmes may need different duration for completion. What part of the action can be completed within the fiscal year needs to be specified so that the implementing agency clearly can know as to which portion of the programme should be completed within specific year. The budget spells out such year-wise responsibility.

3. Necessity of Funds. Implementation of a programme requires availability of necessary funds. The extent of availability depends upon the budgetary sources of revenue. Hence, that programme-structure has to be built which can be supported by the provision made in the budget. This is the most important purpose of the government budget. The budget draws up schemes of revenue mobilisation on the one hand and programmes of public expenditure on the other.

4. Efficiency of Collecting Funds : To achieve efficiency in revenue collection, the expenditure on account of the collectorate is specified on the basis of past trend and present level of cost of collection in the budget. The ratio of cost of collection to the amount of revenue collected speaks of the level of efficiency of the collecting agencies.

5. Efficiency in Expenditure : To achieve efficiency in public expenditure, physical targets of attainment are specified in the budget. In fixing the physical targets, careful consideration is given to the factors of efficiency in course of implementation of the programmes so that nearer the actual achievement at the close of fiscal year, the higher is the efficiency level of expenditure agencies.

6. Basis of Past Experience. Formulation of future programmes on the basis of past experience is an important purpose of the government budget. The lessons derived from past mistakes are utilised in formulating the future course of action. According to *Hicks*, this purpose is achieved by the arrangement of the Budget Speech, which is traditionally divided into three parts – first a presentation of the revenue and expenditure accounts of the year just ended ; secondly, a forecast of the extent to which the estimates for the year just beginning would be covered at existing rates of tax; and finally, a recommendation of adjustments in taxes, calculated to bring about the desired balance at the end of the year.

7. Current Programmes : The purpose of modern budgets is to project current programmes and policies in relation to future benefits and costs on the one hand and to evaluate the actual performance of the budgetary programmes on the other. This is why modern budgets are presented in the form of programme and performance budgets.

8. Act as Anticyclical Weapon : In developed countries the main purpose of the budget in developed countries is to act as an anticylical fiscal weapon. This is done through manipulation of the budget balance. When the economy suffers from unemployment and depression, deficit budget is framed, i.e., public expenditure is incurred in larger quantity than the public revenues received. The gap is over either by borrowing or by printing new money. In either case, the public expenditure pumped into the economy activates production, consumption and savings and, hence, effective demand and employment increases. When the economy suffers from inflation, the situation is corrected by drawing up surplus budget. In such a case, government revenues are raised in larger amounts than public expenditure and, thus, the excess purchasing power is wiped out of the economy. Economic stabilisation is thus regained.

9. Public Accountability : The government budget serves the purpose of public accountability of funds to a considerable extent. The first control is imposed at the budget framing level itself when the government asks different departments to submit their own budgets. Because the departments know that their programmes of expenditure will be scrutinised at the government level, they become careful to observe economy in the budget. The next stage of control is imposed by the legislature which is the ultimate authority to decide the size and extent of the budget. At the end of the financial year, again, the government and its various departments are responsible to the legislature for their action and budgetary performances. Hence, budget serves as a powerful weapon of financial control in respect of both collection of revenue and disbursement of them.

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4. PRESENTATION OF BUDGET

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The public budget may either be presented as a whole or in parts. The countries having a unitary system of government generally presents one single unified budgetary document. In federal countries, on the other hand, it is presented in parts. These countries have different layers of government administration- central, state and local and the budgets are prepared, passed and implemented separately by the each individual layer of the government. Although, these budgets are passed separately, yet they may involve certain inter-government transactions like the loans and grants of the sharing of the revenues between the state and the central government budget. Sometimes, these budgets are split up into parts. For instance, in India also, railway budget is presented separately from the central budget but railway budget is the integral part of the central finances.

In India, according to Article 112 of the constitution, an annual financial statement will be placed before Parliament (Lok Sabha and Rajya Sabha) and Article 202 of the constitution provides that a similar financial statement for each state will be placed before the legislature of respective state. Moreover, the government ac-

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counts (centre and states) are kept under three heads : 1. Consolidated Fund 2. Contingency Fund 3. Public Account

1. Consolidated Fund. It consists the revenue receipt from taxes, loan and other receipts. No amount can be spent without the prior sanction of the Parliament and state legislature in either case of Parliament or state governments.

2. Contingency Fund. It includes the funds of the government to meet the emergency expenses and which cannot be delayed, comes under the contingency fund. The prior sanction of the Parliament or state legislature is not required under this fund. The sanction of the Parliament or state legislature is sought for the revival of the same amount in the contingency fund and the contingency fund is to be replenished. Presently, the corpus of the contingency fund of the Government of India is authorised by the Parliament to be of amounting Rs. 50 crores.

3. Public Account. This fund is collected through other agencies such as small savings, provident fund etc. This fund does not belong to the government and comes under the public account. To make the payment out of this fund, no sanction of the Parliament or state legislature is required.

the whole, is the financial document showing the original estimates of the revenues and outlays for the current year; the revised estimates of revenues and outlays of the current year and the anticipated estimates of revenues and outlays in the ensuing year.

Characteristics of the Budget

From the above definition of the budget, it is now proposed to assess whether a budget is good or not. A good budget is one which is able to satisfy certain conditions and is formulated according to certain well drawn principles. These conditions or requirements are as follows :

1. The budget should be accompanied by an account of the performance of the fiscal policies and programmes of the government during the previous year. This provides a necessary basis for deciding as to what was to be done, what has been accomplished and what more should be aimed at and in what direction.

2. The budget proposals should also accompany an account concerning the position of treasury and the current economic situation of the country. Such an analytical account enables the legislature and the general public to appreciate the budget proposals in a more objective manner.

3. The proposals themselves should be as clear as possible. They should be clearly comprehensive so that correct judgement can be formed as to the way in which the budget is expected to function in the coming year. Accordingly, detailed budget proposals must accompany the proposals under major heads of receipts and expenditure. This would help the legislature and the public to fully comprehend the possible impact of these proposals as the economic activity in general and specific sections of the society in general.

4. The estimates of revenues and expenditures in the budget for the ensuing year should be made in a pragmatic way. These should not have an abnormal variation from the actuals of the current year.

5. The anticipations of revenues and expenditures must make a positive contribution to the realisation of economic goals.

6. The budget should be for a fixed period of one year.

From the above mentioned characteristics of the budget, we can define budget as "a comprehensive plan or programme, ready for execution, containing estimates of expenditures and revenues, for a definite period, usually a year, prepared and presented by the Executive to the Legislature for a vote."[5]

Purposes of the Budget

Government budget serves several purposes.[6]

(*i*) It sets a framework for policy formation. Decisions are needed about actions to be taken to reach objectives. Objectives may be competing. Choices are made to see the extent to which various objectives can be advanced simultaneously.

(*ii*) Budgeting is a means of policy implementation. The budget is a guide for management and budgetary procedures are instruments of administrative control.

(*iii*) The budget is a means of legal control. At each stage of the process of the budget formulation and execution, the question can be raised whether actions have been taken or omitted in confirmity with legal requirements. The emphasis in legal control is on prevention of abuse of power and diversion or improper use of public funds.

(*iv*) The budget document may be a source of public information on past activities, current decisions and future prospectus.

Canons of Public Budgeting

It is difficult to formulate a universally acceptable set of public budgeting principles because of the differences in the nature of world economies, their socio-economic objectives, and political set-ups. Nevertheless, some general guidelines can be provided to the government authorities incharge of public funds.

The list of these guidelines is given below :

1. Although a budget can be prepared for any length of time, it is a common convention to frame it on annual basis.

5. G.S. Lall, *Financial Administration in India*, 1969, P.84.
6. Richard Goode, *Government Finance in Developing Countries*, pp.9-10.

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2. Budget-making involves extensive estimates of revenue and expenditure for the ensuing financial year. The 'actuals' or 'accounts' represent the figures available after the expiry of the financial year under review. There is every possibility of variations between estimates and actuals. However, the nature and the degree of these variations is of immense importance because it has far reaching implications in terms of resource mobilisation, economic planning, financial stability and tax burden. The degree of divergence reflects upon the skill and competence of the budgets makers. Excessive deviation shows the poor financial predictability of the experts. These variations in the budget of the government has two aspects : (*a*) over-estimation and (*b*) under-estimation. Over-estimation of revenue results in shortages of funds leading to curtailment or even exclusion of certain development projects. During the inflationary period in the economy it may further worsen the economy. In case the public expenditure is inelastic as compared to the estimates of revenue, it will necessitate deficit financing. Also, over-estimation may slacken government efforts for additional resource mobilisation.

On the contrary, under-estimation of revenues may lead to unwanted tax doses. It will create resentment among the tax payers. Moreover, it may complicate the tax structrue and increase in cost of administration. Unexpected resources available to the public authorities are generally utilised in unproductive projects formulated at a short notice. Underestimation may also induce the government to resort to public borrowing resulting into unnecessary increase of liabilities of the public exchequer.

In countries like India where the process of economic planning is linked with annual budgets, the need for close relation between the budgetary authorities and planners is of great significance. Surplus on Revenue Account is the first major source of funds available for capital expenditure. The integration of budget with plan will become difficult in the face of inaccurate revenue estimates. The importance of accurate revenue estimates become all the more relevant if the country emphasises on self-reliance, *i.e.*, dependence on internal resources.

3. Government transactions, both on revenue and expenditure sides should be shown on gross basis rather than net basis. It will be an unsound budgetary practice if the receipts are deducted from charges and the expenditure is shown on net basis in the budget estimates. Under this defective practice the government will approach legislature for the authorisation of only that part of expenditure which cannot be met from receipts. This would render legislature's control over government expenditure meaningless. Therefore, budget estimates should be presented on gross basis.

4. It is always desirable to have one budget for a government. If different ministries/departments have their separate budgets, it would be difficult to evaluate the true financial position of the government. Furthermore, the government should try, as far as possible, to prepare a balanced budget. The budgetary surpluses raise doubts among the public regarding the desirability of imposition of taxes. On the other hand, a deficit budget erodes government's confidence and the will to execute budgetary plans. The government will be under pressure all the time to look for additional funds.

5. A good budgetary practice is one which makes provision for the expiry of all appropriations at the close of financial year. This necessitates to prepare and balance the accounts and also to ascertain surpluses or deficits for each year.

6. The estimates and accounts of budgetary transactions should be prepared on cash basis. This system facilitates the transactions of the year to be closed soon after their termination so that the actual trends in government finances may be available to the legislature and government departments for scrutiny and forecasting. The form in which the budgetary estimates are presented should confirm to that of accounts. The task of government officials and legislators becomes difficult, if the scheme of classification of estimates is different from that of accounts.

Q7 Significance of Public Budgeting / Importance

Budgetary operations of the government significantly influence the functioning of an economy. In a country where the ideals of welfare state and economic planning have emerged, the magnitude of public spending has increased tremendously. This has resulted in the emergence of government as an important sector of the economy. This sector has its own money inflows and outflows. A huge sum of money is collected by the government through taxation, borrowings and sale

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(*vi*) Deficit budget may adversely affect the exchange value of currency and shake the confidence of foreign investors.

4. TYPES OF BUDGET / Kinds

In the modern world, the government budget is a mere statement of revenues and expenditures of the government. On the other hand, it is now increasingly recognised as a powerful instrument of economic policy. The various types of budget are discussed below :

1. **Revenue and Capital Budget :** The budget is divided into two accounts, *i.e.*, revenue (or current) account and capital budget, in many countries. The revenue (current) budget is related with current financial transactions of the government which are of recurring nature. Capital budget is related to such transactions as are related to the acquisition and disposition of capital assets.

The distinction between revenue and capital budget is justified on the following grounds :

(*i*) For the efficient administration and effective control on public expenditure, it helps to make a clear-cut demarcation the routine administrative work of the government and its functions in respect of creation and management of capital assets.

(*ii*) It helps in analysing the effects of government revenue and outlays on economic activity.

(*iii*) Its transactions in the revenue and capital accounts can help to trace the effects of government transactions on current consumption, capital formation and price movement.

2. **Executive and Legislative Budget :** The executive budget is prepared by the executive of the government. It does not mean that legislature has nothing to do with the executive budget. This budget has to be passed and adopted by the legislature, but the main initiative lies with the government. On the contrary, the legislative budget is one that is prepared and adopted by legislature either directly or through the committees appointed by it. Executive budget is generally considered better than the legislative budget due to certain favourable arguments :

(*i*) Executive is more capable and efficient in making estimate of revenue receipts and disbursements.

(*ii*) Executive is directly responsible for any financial irregularities because budget is prepared by itself.

(*iii*) The ultimate task of executing the budget lies with the executive. Therefore, it is more fair to assign this job of preparing the budget itself.

(*iv*) It is more realistic in approach.

3. **Administrative and Cash Budgets :** The **administrative** budget (also known as the conventional budget) represents a set of accounts established within the frame work of such programmes as are financed in the conventional manner, *i.e.*, through the levy of taxes. Such flows of funds as do not belong to the government remains excluded.

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The administrative budget is often criticised on the following grounds :

(*i*) It presents an incomplete picture of financial activity of the government because there is always some divergence between the receipts and payments falling due in specific periods and their accrual values.

(*ii*) The administrative budget tends to ignore the effect of the funds not belonging to the government, on the level of economic activity.

(*iii*) The exclusion or inclusion of certain items in such a budget can make the year-to-year comparison difficult.

The **cash budget** includes all the cash receipts from and payments to the government. The funds owned or not-owned by the government are included in this budget. The U.S. cash budget receipts consist of conventional budget receipts *plus* trust fund receipts *less* intra-governmental transactions. The payments consist of conventional budget expenditures *plus* trust fund expenditures *plus* government-sponsored enterprise expenditure (net) *less* intra-governmental transactions.

The cash budget is more detailed than the administrative budget.

4. Multiple and Unified Budget : Before 1968, the American federal government budget was divided into different parts. Such a budgetary system is known as multiple budget. The U.S. federal government budget consisted of the administrative budget, the consolidated cash budget and the national income account budget.

5. Federal, State and Local Bodies Budget : The federal and state government budgets are prepared by the executive. These are got passed by the executive and the responsibility of its implementation also rests upon it. In case of relatively large municipal bodies, the independent budget is followed. In some cases, these is departure of local budgets from executive budget. The budget process in general tends to be less complex at the state and the local levels of the governments than at the federal level.

6. Ordinary and Emergency Budget : The ordinary budget deals with the functions which are relatively permanent while the emergency budget is concerned with the abnormal or exceptional circumstances like war, depression etc.

7. Surplus, Deficit and Balanced Budget : A budget is said to be surplus when the public revenues exceed the public expenditures. A budget is said to be deficit when public revenues fall short of public expenditures. When there is an equilibrium between the government revenues and expenditures, the budget is said to be balanced. These budgets have significant effects upon the level of economic activity in the country.

8. Plan and Non-Plan Budget : The part of the budgetary receipts which goes to finance the planned developmental expenditures constitute the plan budget, while the remaining part of the budgetary resources and expenditures is referred to as the non-plan budget.