



**GOVERNMENT OF SIKKIM  
FINANCE DEPARTMENT  
GANGTOK**

**Evaluation Report of Compliance to  
Provisions of the Sikkim FRBM Act:  
Fiscal Year 2019-20**



**National Institute of Public Finance and Policy  
New Delhi**

**Presented before the Sikkim Legislative Assembly as required under Sub  
section (7) of section 7 of the Sikkim Fiscal Responsibility and Budget  
Management Act 2010**

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# **1.Introduction**

## **Objectives and Approach of the Report**

The assessment of compliance to the provisions of fiscal responsibility legislation by the state government by an independent body has become part of established accountability structure in the State and is expected to improve transparency in the fiscal management. As the report is placed in the State Legislature as per the requirements of the Fiscal Responsibility and Budget Management Act (FRBM Act) and requires legislative approval, it adds to the legislative scrutiny of public finances. The report is expected to help in the process of wider dissemination of information and consultation process. While Covid-19 pandemic affected revenue generation, increased expenditure and changed the spending pattern, partially in 2019 and to a large extent in 2020-21, the assessment of fiscal management and compliance to the FRBM Act in 2019-20 will point toward the capacity of the government to come back to the consolidation process.

The independent review while assessing compliance record of the government in 2019-20, in terms of statutory fiscal targets and fiscal management principles enshrined in the FRBM Act, analyzed the state finances in recent years. Independent scrutiny of fiscal management in general and fiscal rules in particular, is a means of practicing transparency in governance<sup>1</sup>. This feature assumes significance in public financial management (PFM) and enhances trust on government policies. Sound PFM systems prescribe submitting key fiscal data and information, planned programs and policy objectives, expected outcomes to the legislature for better legislative control and disseminate to the public at large to enhance transparency and accountability. The independent scrutiny becomes instrumental in this process, by helping legislatures and the public in accessing the quality of fiscal policies, plans and performance.

The FC-XIII recommended to institutionalize independent review of FRBM Act at the level of Union and state governments to bring in efficiency to public spending and improve credibility. The Commission opined that the process of independent review mechanism should evolve into a fiscal council with legislative backing over time<sup>2</sup>. FC-XIV and other expert bodies also

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<sup>1</sup> IMF Code of Good Practices on Fiscal Transparency.

<sup>2</sup> Report of the Thirteenth Finance commission, paras 9.65 and 9.66, pp.137

avored creating fiscal council at the Union level<sup>3</sup>. The Union Government, however, has entrusted the responsibility of independent evaluation of FRBM Act to the Comptroller and Auditor General of India (CAG). Establishing fiscal council for all the states could be a complex effort, for which periodical independent review looks more feasible to enhance accountability and transparency.

Sikkim enacted FRBM Act in 2010-11 with the objective of designing and implementing a rule based fiscal management system to ensure fiscal stability and sustainability while ensuring efficient provision of public services. Introduction of FRBM Act facilitated formulation of Medium-Term Fiscal Plan (MTFP) to provide a medium-term perspective of macro-fiscal situation and improve transparency. The state FRBM Act lays down quantitative targets with regard to deficit measures and debt level. Over the years there have been several changes in these targets following recommendations of successive Central Finance Commissions. The fiscal management principles enshrined in the Act call upon the State government to design and implement prudent fiscal policies to ensure transparency in fiscal management, improve predictability in funding arrangements, provide a medium-term perspective of revenue effort and expenditure management, and improve efficiency in management of assets and liabilities.

The Sikkim Fiscal Responsibility and Budget Management Act (FRBM), 2010 under Section 7(7) prescribes that “the Government may assign to an independent external agency the task of carrying out the periodical review for the compliance of the provisions of this Act in the manner as may be prescribed”. This is among the measures prescribed to enforce compliance to the Act. The specific objective of the review is to examine the concurrence of the state government to the fiscal targets in terms of deficit and debt stock relative to the State GSDP. These are the benchmarks for a rule based fiscal management system to attain fiscal stability and sustainability. The review also looks at the other budget management requirements enshrined in the Act like improving transparency and following the desirable fiscal management principles.

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<sup>3</sup> The 13th and 14th Finance Commissions advocated for establishing independent fiscal agencies to review the government’s adherence to fiscal rules, and to provide independent assessments of budget proposals. The N.K. Singh committee, (2017) on the review of fiscal rules suggested the creation of an independent fiscal council that would provide forecasts and advise the government on whether conditions exist for deviation from the mandated fiscal rules. In 2018, the D.K. Srivastava committee on Fiscal Statistics suggested the establishment of a fiscal council that could co-ordinate with all levels of government to provide harmonized fiscal statistics and provide an annual assessment of overall public sector borrowing requirements.

## 1.1 Objectives of the Review Report

Government of Sikkim entrusted the responsibility of reviewing the compliance of the Act for the fiscal year 2019-20 to National Institute of Public Finance and Policy (NIPFP), New Delhi. The evaluation report analyzes the state finances in recent years and summarizes the key conclusions and lessons of fiscal management for the fiscal year 2019-20. In addition to highlighting state's compliance to fiscal responsibility act targets, the report contains broad trend of fiscal management. The evaluation aims to address following issues pertaining to state finances in general and fiscal responsibility legislation in particular;

- a) Compliance of the State Government to the provisions of FRBM Act in the fiscal year 2019-20. These include fiscal targets relating to deficit, debt, and other fiscal variables as specified in the Act.
- b) Assessment of macroeconomic outlook that includes broad composition of gross state domestic product, contribution of various sectors to the state income, and growth perspective. The FRBM Act calls upon the state to prepare a macroeconomic outlook along with its medium - term fiscal plan (MTEFP).
- c) Assessment of state finances in terms of revenue effort, central transfers, spending pattern, and debt management. Assessment of fiscal management in these years provides a context and background to comprehend the response of the State government to the requirements of fiscal responsibility act given the availability of resources and commitments.
- d) Evaluation of credibility of state budget in terms of its budget projections and outturns, both on revenue and spending side.
- e) While assessing the compliance of the state to the provision of the FRBM Act, the report reviews the state's adherence to fiscal management principles and transparency requirements enunciated in the Act.

Limiting the fiscal deficit to targeted level to ensure sustainable level of debt has remained at core of the Act. Maintaining debt stock at a sustainable level, using borrowed funds for productive use, pursuing tax policies with due regard to economic efficiency, pursuing expenditure policies to provide impetus to economic growth, and formulating a realistic budget to minimize deviations during the course of the year are the major features of the fiscal

management principles. The budget management in terms of budget projection has to be unbiased to avoid discrepancies in flow of funds to programs.

The report is based on published fiscal data from state budgets, finance accounts, appropriation accounts, and CAG reports of relevant years. The report also used other socio-economic data published by the State government. The department of finance provided data and information on state finances for this study and gave an overall perspective on the state fiscal management including revenue receipts trends, debt management, resource allocations to different sectors, and achievement of FRBM fiscal targets. The study also benefited from the inputs provided by the spending departments.

The rest of the report is organized as follows. Section 2 provides an overall assessment of macroeconomic outlook and sector composition of GSDP. Section 3 contains analysis on state finances in recent years. Compliance of the State Government to the fiscal targets and fiscal management principles under the Sikkim FRBM Act are included in section 4. Issues related to revenue mobilization and expenditure pattern for the year 2019-20 as compared to the budget provisions are analyzed in this section. Concluding observations are contained in Section 5.

## 2. Overview of the State Economy

Slowdown in the national economy due to Covid-19 pandemic in 2020-21 had its impact on fiscal management at the sub-national level. The growth rate of gross domestic product (GDP) had already decelerated before the pandemic struck. The growth had declined from 6.5 percent in 2018-19 to 4 percent in 2019-20. As the growth of GDP has started picking up after since 2021-22, it is expected that higher national growth will help in developing sound fiscal strategy and ensure predictability of flow of funds to states. Predictability in fund flows to a state like Sikkim in the long run facilitates building sound fiscal forecasting to support development process. Growth of the economy serves as an accepted base for revenue generation effort. Robust macro-fiscal projection is crucial to get an unbiased picture of resource envelope for the budget management process while taking allocation decisions. Assessing macroeconomic outlook of Sikkim during 2019-20 assumes significance to show the strength of the state economy to augment fiscal management process.

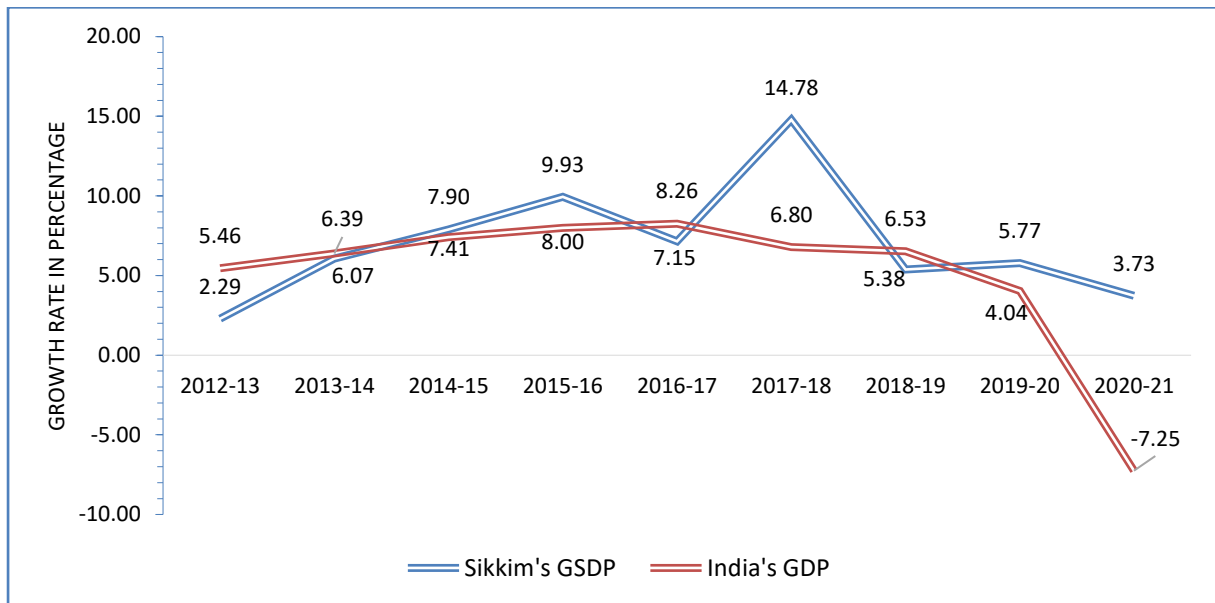
Assessing macroeconomic outlook has been stipulated in the state FRBM Act. This comes in the form of a statement containing analysis of growth perspective and sectoral composition of GSDP. Contribution of various sectors to the state economy assumes significance in budget management process due their impact on revenue generation efforts. The fiscal variables like deficit and debt numbers are presented as percentage to GSDP to track their movements in the context of fiscal consolidation process. The Ministry of Finance, Government of India determines the borrowing limit of the state government as a proportion to state GSDP.

### 2.1 Gross State Domestic Product of Sikkim

The GSDP at constant prices in Sikkim continued to grow steadily from 2.29 percent in 2012-13 to 9.93 percent in 2016-17. After a sharp decline in 2016-17 (7.15 percent), the GSDP growth rate reached a peak of 14.78 percent in 2017-18 (Figure 2.1). Once again, the GSDP suffered a setback in 2018-19, as its growth declined to 5.38 percent. While in 2019-20, the GSDP growth rate improved marginally to 5.77, large decline came in 2020-21 to 3.73 percent. The impact of Covid-19 disruption was clearly visible.

**Fig 2.1**

**Sikkim's Economic Growth: GDP-GSDP Growth rates (at constant prices)**



Per capita income of the State is an important indicator of economic progress. Despite the problems of outliers influencing per capita income, it remains as an important measurement while a large number of people like a population of State is concerned. Per capita income of Sikkim (Per capita NSDP) has improved from Rs. 245987 in 2015-16 to Rs. 403376 in 2019-20 at current prices. The per capita income of the State shows an annual average growth rate of 13.37 percent during this period. Sikkim occupies second position, remaining only behind Goa among all states in India Based on average per capita income during the period from 2015-16 to 2019-20.

The growth of the GSDP and very high per capita income of Sikkim needs to be examined in terms of its impact on internal revenue generation efforts. The decomposition of GSDP shows that manufacturing and construction sectors are major components of the state economy. The impressive growth of power sector driven by generation of hydroelectricity in newly commissioned power projects and pharmaceutical industries have contributed to growth process. However, their impact on state finances, particularly on revenue generation has not been very productive. The generation of hydroelectricity, though adds to the GSDP numbers, remain outside the state tax system. Similarly, the pharmaceutical industries did not generate revenue earlier under VAT due to consignment transfer, and do not hold promise under GST regime either.



**Table 2.1**  
**Per Capita Income (Per capita NSDP) of all States (at current prices) (Rs.)**

Sl. No.	States	2015-16	2016-17	2017-18	2018-19	2019-20	Average
1	Andhra Pradesh	108002	120676	138299	154031	169320	138066
2	Bihar	30404	34045	36850	40715	45071	37417
3	Chhattisgarh	72991	83285	89690	98254	105089	89862
4	Goa	334576	378953	411740	423716	435959	396989
5	Gujarat	139254	156295	176961	197457	213936	176781
6	Haryana	164963	184982	208437	223015	240507	204381
7	Jharkhand	52754	60018	67484	75421	77739	66683
8	Karnataka	148108	169898	185840	204804	222002	186130
9	Kerala	148133	166246	183252	205437	213041	183222
10	Madhya Pradesh	62080	74324	81966	92486	103103	82792
11	Maharashtra	146815	163726	172663	186074	196100	173076
12	Odisha	65993	79181	89392	100838	110081	89097
13	Punjab	118858	128780	139835	149974	155590	138607
14	Rajasthan	83426	91924	98698	106624	115356	99206
15	Tamil Nadu	142028	156595	175276	194373	213396	176334
16	Telangana	140840	159395	179358	209848	230955	184079
17	Uttar Pradesh	47118	52671	57944	62380	66136	57250
18	West Bengal	75992	82291	91401	103944	113163	93358
1	Arunachal Pradesh	116985	124129	138836	155076	168679	140741
2	Assam	60817	66330	75151	81034	96240	75914
3	Himachal Pradesh	135512	150290	165497	174804	185728	162366
4	Manipur	55447	59345	71507	73795	82437	68506
5	Meghalaya	68836	73753	77504	82653	87170	77983
6	Mizoram	114055	127107	155222	164708	188012	149821
7	Nagaland	82466	91347	102003	109198	120871	101177
<b>8</b>	<b>Sikkim</b>	<b>245987</b>	<b>280729</b>	<b>349163</b>	<b>375773</b>	<b>403376</b>	<b>331006</b>
9	Tripura	84267	91596	100444	113016	125675	102999
10	Uttarakhand	147936	161752	180858	186169	188179	172979

Source: Central Statistical Office, GoI

The GSDP growth at constant prices, which was showing increasing trend until 2017-18, has declined since then. The growth of GSDP increased from 9.93 percent in 2014-15, to 14.78 percent and then declined to 5.77 percent in 2019-20 (Table 2.2). Average annual growth rate during this period works out to be 8.49 percent. The growth rate becomes a crucial factor in the context of budget making as GSDP is used as denominator in all target fiscal ratios, and it is also the determining factor for borrowing limit of the state. The growth rates assumed by Central Finance Commissions becomes reference points while making budget estimates. FC-XIV projected the GSDP growth at current prices for Sikkim for the award period 2015-16 to 2019-20 at 24.32 percent. However, the average annual growth rate of GSDP during this period

was only 15.03 percent at current prices. The growth rates of components of GSDP indicate that manufacturing sector declined in 2019-20 and services sector increased at a higher growth rate of 20.92 percent.

**Table 2.2**  
**Growth Rate of Key Aggregates of State Domestic Product (Constant Prices)**

Item	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
Agriculture, forestry and fishing	3.88	8.90	16.26	11.41	4.00	3.68
<b>Primary</b>	<b>4.02</b>	<b>8.80</b>	<b>16.06</b>	<b>11.17</b>	<b>3.92</b>	<b>3.62</b>
<b>Secondary</b>	<b>11.04</b>	<b>8.22</b>	<b>14.95</b>	<b>6.56</b>	<b>-0.11</b>	<b>-0.40</b>
<b>Tertiary</b>	<b>6.52</b>	<b>1.23</b>	<b>4.16</b>	<b>11.54</b>	<b>20.92</b>	<b>11.71</b>
<b>TOTAL GSVA</b>	<b>9.09</b>	<b>6.16</b>	<b>11.94</b>	<b>8.26</b>	<b>6.01</b>	<b>3.73</b>
GSDP	9.93	7.15	14.78	5.38	5.77	3.73
Per Capita GSDP (Rs.)	8.73	5.99	13.55	4.43	4.66	2.80

Source: Central Statistical Office, GoI

## 2.2 Contribution of Various Sectors to the GSDP

Composition of GSDP at constant prices given in Table 2.3 shows that industry sector, which contains manufacturing, construction, and electricity, is the largest contributor to the economy. On an average industry sector account for about 63 percent of state GSDP during 2014-15 to 2019-20. Manufacturing is the largest component in this sector, which accounts for about 45 percent of the GSDP during this period. While the relative share of industry sector increased from 61.2 percent in 2014-15 to 64.2 percent in 2018-19, mostly driven by manufacturing activities, it declined in 2019-20 to 60.5 percent.

The service sector including trade, hotel, transport, real estate, and financial services is an important component of the economy. Relative share of services sector remained subdued until 2018-19, after which improvement is seen in 2019-20. Relative share of agricultural sector including other associated activities remained more or less stagnant during 2014-15 to 2019-20. A marginal improvement in its relative share is seen during this period. The services sector, which consists of financial service, hotel industry, transport services, services relating to real estate, and public administration, has been a growing sector in the national economy. Improving service sectors augurs well for revenue generation and particularly for states in increasing the GST collection.

**Table 2.3**  
**Composition of GSVA (Constant Prices)**

Economic Activity	Percentage Share (%)					
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Agriculture, Forestry and Fishing	7.9	7.5	7.7	8.0	8.2	8.1
Mining and Quarrying	0.1	0.1	0.1	0.1	0.1	0.1
<b>Primary</b>	<b>8.0</b>	<b>7.6</b>	<b>7.8</b>	<b>8.1</b>	<b>8.3</b>	<b>8.1</b>
Manufacturing	41.6	43.5	46.3	48.0	46.4	42.6
Electricity, Gas, Water Supply & Others	14.4	13.5	12.7	13.0	13.7	13.6
Construction	5.3	5.3	4.5	4.3	4.1	4.2
<b>Secondary</b>	<b>61.2</b>	<b>62.3</b>	<b>63.5</b>	<b>65.2</b>	<b>64.2</b>	<b>60.5</b>
Trade, Repair, Hotels and Restaurants	4.8	4.5	4.5	4.7	5.0	5.3
Transport, Storage, Communication	3.2	3.1	3.3	3.1	2.9	3.0
Financial Services	1.6	2.7	1.7	1.5	1.5	1.5
Real estate	5.0	4.6	4.5	4.1	3.9	3.8
Public Administration	7.1	6.6		5.6	6.8	8.7
Other Services	9.3	8.6	8.5	7.8	7.5	9.1
<b>Tertiary</b>	<b>30.8</b>	<b>30.1</b>	<b>28.7</b>	<b>26.7</b>	<b>27.5</b>	<b>31.4</b>

Source: Central Statistical Office, GoI

### **3. Review of State Finances of Sikkim**

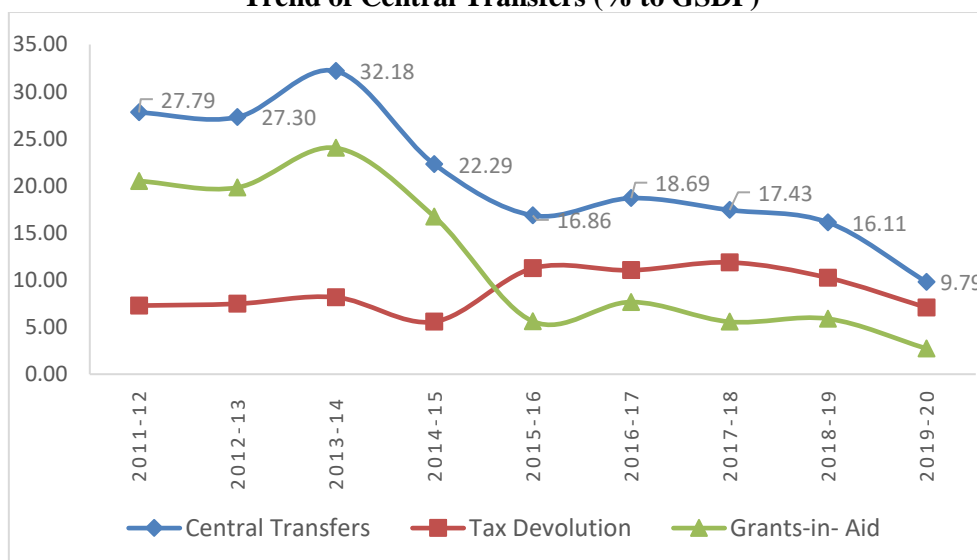
State finances in Sikkim depends considerably on transfers from Union Government. The data for recent years show that this dependency has been declining and this is more pronounced in the fiscal year 2019-20. While, Constitutional provision relating to division of financial sources and functions between central and state governments traditionally necessitated transfers to the states, the changing dynamics of transfer system has emerged as the most influencing factor in recent years. As the own revenue base for the state has not changed noticeably, less than expected transfers from the central government has created challenges for fiscal management. The distortions created by Covid-19 pandemic became more pronounced both in flow of central transfers and own revenues, which necessitates a relook at public financial management at the state level to avoid fiscal stress and come back to fiscal consolidation path.

The fiscal year 2019-20 was the last year of the award period of FC-XIV. After the recommendations of the FC-XIV, the fiscal transfer system in India went through significant changes in the fiscal year 2015-16. The changes in plan transfers by the central government also contributed to this. The composition of central transfers has changed noticeably. Sikkim faced challenges in fiscal management following the recommendations made by the Commission as overall impact of changes in transfer system was not favorable to the state.

- The FC-XIV recommended increasing the tax devolution to a high of 42 percent of all the central taxes and refrained from giving specific-purpose grants. The Commission recommended disaster relief grants and grants for local bodies. Some states received revenue deficit grant based on assessment of their post-devolution revenue deficits.
- Central government restructured plan grants to states in 2015-16 expecting reduction in net revenues available to it. It subsumed Normal Central Assistance (NCA), Special Plan Assistance, and Special Central Assistance in the FC-XIV award and delinked eight schemes like National e-Governance Plan, the Backward Regions Grant Fund (BRGF), the Rashtriya Krishi Vikas Yojana (RKVY) etc. from central funding.
- Thus, the increment in tax devolution signifies a change in composition of central transfers, as the plan grants to the State budget have been removed leaving mostly the CSS funds. The Central Government also restructured the CSS based on the recommendations of the subgroup of chief ministers in 2016-17.

- During the award period of FC-XIV, while states continued to adhere to FRBM Act targets, the state finances were affected by moderation in national growth and its adverse impact on flow of central funds. Debt burden has increased continually since 2015-16, led by restructuring of power sector through schemes like UDAY. The RBI Study on State Finances (RBI 2019, State Finances: A study of budgets) has indicated that there has been a continual decline in state expenditure, mainly capital, which has wider repercussion on development process.
- For Sikkim higher tax devolution could not compensate loss of plan grants, which created difficulties for ongoing projects. The increment in tax devolution was aimed at providing larger untied fund to the states and thus flexibility to take policy choices. In the case of Sikkim, the central grants funded large number of projects. While the policy choices to fund the existing plan schemes from the untied tax devolution was open, the nature of centrally funded schemes was such that uncertainties started creeping into the project executions. The FC-XIV transfer was also designed based on a very unrealistic own tax projection for Sikkim.
- Central transfers as percentage to GSDP given in Figure 3.1 shows that while there was some improvement in tax devolution, grants declined as percentage to GSDP. Overall transfers suffered declined since 2015-16. In 2019-20, the decline has been steep as both tax devolution and grants as percentage to GSDP declined considerably as percentage to GSDP.

**Figure 3.1**  
**Trend of Central Transfers (% to GSDP)**

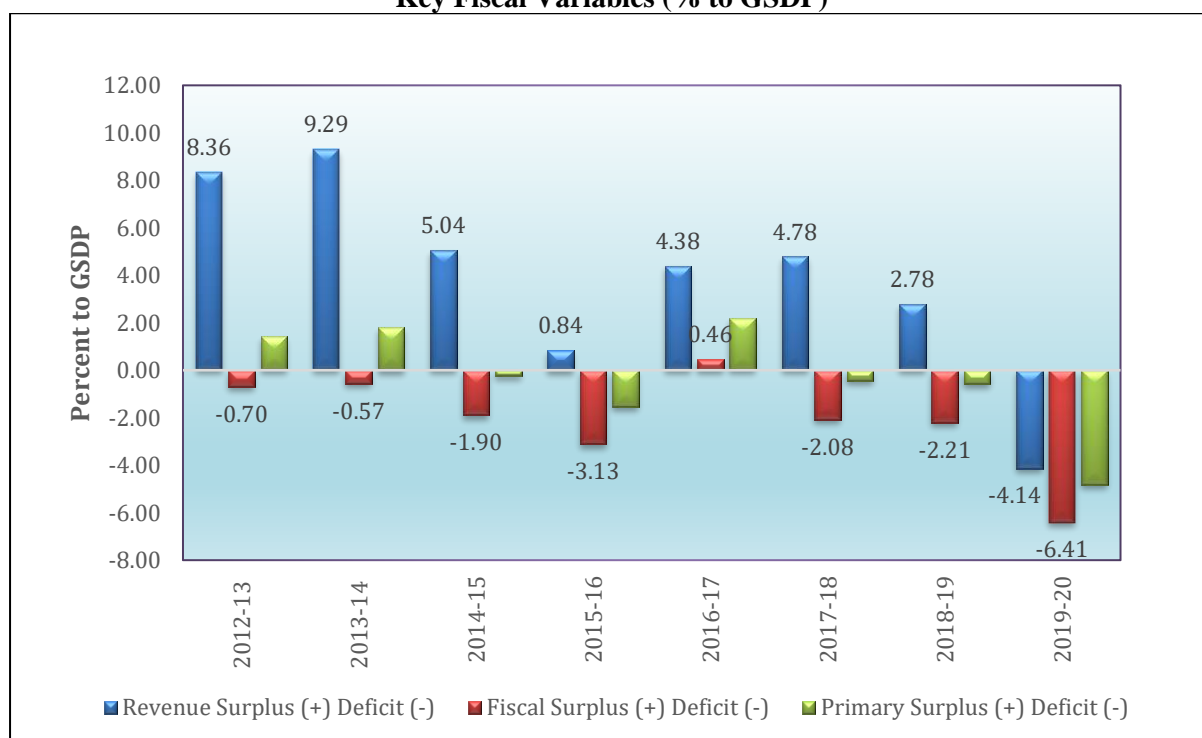


### 3.1 Overview of State Finances: Challenges in 2019-20

Sikkim’s consistent record of achieving revenue surplus and containing fiscal deficit within the limits of the FRBM Act was broken in 2019-20 (Figure 3.2). The deterioration was sharp as compared to the previous year. In earlier years, the State managed to generate revenue surplus due to dominance of central transfers in the aggregate revenue. After adoption of FRBM Act, containment of fiscal deficit was a positive development in fiscal management. Emerging fiscal pressure was visible in 2018-19 as the revenue surplus declined.

The 2019-20 data shows that state finances deteriorated massively with respect to FRBM Act targets. Revenue deficit increased to 4.14 percent of GSDP as compared to surplus in earlier years and fiscal deficit of 6.41 percent was much higher than the FRBM targets. Revenue deficit constitutes about 64.57 percent of fiscal deficit and rest 35.43 percent was due to capital outlay. Given the impact of Covid-19 pandemic on state finances, this fiscal stress is a worrying factor.

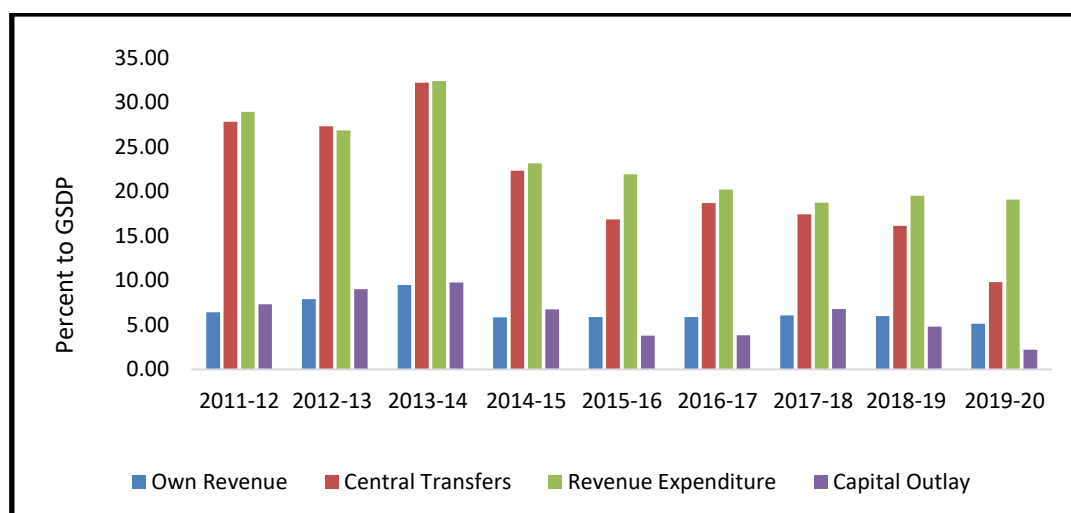
**Figure 3.2**  
**Key Fiscal Variables (% to GSDP)**



In 2019-20, the State was entitled to increase fiscal deficit by 0.5 percent beyond the FRBM Act targets of 3 percent due to its previous record of fiscal management as recommended by FC-XIV. Fiscal imbalance, however, exceeded enhanced limit due to resource problems and committed spending pressure. This indicates limitations on budget management process at state level due to less than expected resource availability.

Broad fiscal trends as percent to GSDP for 2019-20 show that revenue receipts have suffered large decline driven by central transfers (Figure 3.2). Own revenue of the State also shows decline in this fiscal year. The revenue expenditure as percent to GSDP has been curtailed rather marginally. It was the capital expenditure, which has been reduced drastically. Capital spending continues to be a residual given the committed nature of the revenue expenditure.

**Figure 3.3**  
**Broad Fiscal trends in Sikkim**



The state faced severe contraction in fiscal space due to decline in revenue receipts as percentage to GSDP as is evident from fiscal outcomes for the year 2019-20. Revenue surplus arises due to high dependence on central transfers, all of which are usually booked under revenue receipts. Many of the central grants are tied grants, proceeds from which are utilized for capital expenditure as per the design of the scheme. Receipt of central grants at the end of the financial year, many a time could not be put to use and adds to the revenue surplus same year. Decline in central transfers removed the availability of fiscal space and adversely affected the capital outlay. The decline in capital outlay as percentage to GSDP in 2019-20 becomes a

worrying factor for future years as debt has gone up. What is more important for the state is to improve efficiency to be able to utilize the unspent balances.

### 3.2 The Revenue Receipts

Sikkim witnessed large fall in revenue receipts relative to the GSDP in 2019-20 as compared to the previous year. The decline in aggregate revenue receipts was massive at 7.37 percentage points (Table 3.1). While own tax revenue and non-tax revenue accounted for 0.55 and 0.32 percentage points decline, it was the central transfers, which declined by 6.50 percentage points. The decline in central transfers was caused by both decline in tax devolution and grants. The deterioration in revenue receipts in 2019-20 exceeded the level of decline that was witnessed in state revenues after the recommendations of the FC-XIV in 2015-16. There was a turnaround in revenue receipts in 2016-17 as percentage of GSDP, which started falling after that. In nominal terms, the state received Rs. 4841.27 crores in 2029-10 as compared to Rs. 5970.40 crores in 2028-19. The sharp reduction in revenue receipts due to decline in central transfers adversely affected fiscal management in 2019-20.

**Table 3.1**  
**Revenue Receipts in Sikkim**

Heads	Percent to GSDP								
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
<b>Total Revenue</b>	<b>34.19</b>	<b>35.19</b>	<b>41.66</b>	<b>28.16</b>	<b>22.75</b>	<b>24.57</b>	<b>23.48</b>	<b>22.29</b>	<b>14.91</b>
<b>Own Revenues</b>	<b>6.40</b>	<b>7.89</b>	<b>9.49</b>	<b>5.86</b>	<b>5.89</b>	<b>5.89</b>	<b>6.05</b>	<b>5.99</b>	<b>5.13</b>
<b>Own Tax Revenues</b>	<b>3.50</b>	<b>4.66</b>	<b>5.62</b>	<b>3.63</b>	<b>3.41</b>	<b>3.48</b>	<b>3.10</b>	<b>3.54</b>	<b>2.99</b>
Sales Tax	1.48	2.43	3.06	1.94	1.96	1.94	1.12	0.70	0.61
SGST	0.00	0.00	0.00	0.00	0.00	0.00	0.77	1.51	1.40
State Excise Duties	1.15	1.19	1.29	0.90	0.85	0.83	0.68	0.68	0.64
Motor Vehicle Tax	0.20	0.18	0.20	0.13	0.13	0.13	0.13	0.12	0.13
Stamp Duty and Reg. Fees	0.10	0.06	0.07	0.05	0.05	0.07	0.06	0.06	0.04
Other Taxes	0.58	0.81	0.99	0.61	0.41	0.50	0.33	0.46	0.17
<b>Own Non-Tax Revenues</b>	<b>2.91</b>	<b>3.23</b>	<b>3.87</b>	<b>2.23</b>	<b>2.48</b>	<b>2.41</b>	<b>2.95</b>	<b>2.46</b>	<b>2.14</b>
<b>Central Transfers</b>	<b>27.79</b>	<b>27.30</b>	<b>32.18</b>	<b>22.29</b>	<b>16.86</b>	<b>18.69</b>	<b>17.43</b>	<b>16.29</b>	<b>9.79</b>
Tax Devolution	7.28	7.47	8.16	5.57	11.24	11.03	11.86	10.41	7.07
Grants	20.51	19.82	24.02	16.72	5.62	7.66	5.56	5.88	2.72

Source (Basic Data): Finance Accounts, State Budget 2021-22 and CSO

Own revenue receipts suffered a marginal decline from 5.99 percent in 2018-19 relative to GSDP to 5.13 percent in 2019-20. Central transfers taking both tax devolution and grants declined from 16.29 percent to 9.79 percent during the same time. While shortfall in own revenues as compared to the budget estimates of the state accounts for only 10 percent of total



shortfall in revenue receipts, central transfers accounts for 90 percent. As alluded earlier, central transfers, which constituted about three-fourth of the aggregate revenue receipts, reduced to about 52 percent of the total revenue.

### ***Trend of Individual State Taxes***

The trend of own tax revenue during the period 2011-12 to 2019-20 relative to GSDP is contained in Table 3.1 shows that aggregate of state taxes declined marginally in the fiscal year 2019-20. Sales tax including GST from 2017-18 account for major share of own tax receipts. Its share in own tax revenue has increased from 57.46 percent in 2015-16 to 67.24 percent in 2019-20. However, as percentage to GSDP sales and SGST declined from by 0.21 percentage points in 2019-20. The fiscal year 2019-20 was the third year of implementation of goods and services tax (GST). Because of the teething problems in the implementation process and decline in national growth rate, GST fared badly in the first year of its implementation. While an improvement in 2018-19 indicated positive movement, the 2019-20 data shows that GST has not emerged as a buoyant source. Other state taxes show decline as percentage to GSDP in 2019-20

The buoyancy coefficients, reflecting the response of tax growth relative to the growth of state economy, for two periods are given in Table 3.2. The longer period buoyancy coefficients, from 2004-05 to 2019-20 shows that taxes have not grown commensurate with the growing economy over the years for which the buoyancy coefficients remain low. The results of regression method adopted to estimate tax buoyancy for a longer period is considered as more robust. The sectors, electricity, and manufacturing, growing rapidly and contributing to growth process since 2008-09 have not contributed to tax revenues. Although the value of the electricity generated by the newly commissioned hydroelectric units contributes to the growth numbers, it does not enlarge the tax base. Similarly, the improved production by the pharmaceuticals in the manufacturing sector, though adds to the growth, most of it goes out of the State in the form of consignments attracting no GST.

Tax buoyancy estimated for more recent years from 2011-12 to 2019-20, shows an improvement as aggregate buoyancy coefficient has nearly reached 1. This implies, the tax growth rate has started catching up with GSDP growth rate. The buoyancy coefficient of sales tax and SGST taken together shows an impressive figure of 1.333. This has positively

influenced the aggregate tax buoyancy. It reflects the expansion in economic activity due to higher contribution of industry and services sectors.

**Table 3.2**  
**Buoyancy of State Taxes**

	<b>2004-05 to 2019-20</b>	<b>2011-12 to 2019-20</b>
Own Tax Revenues	0.653	0.995
Sales Tax + SGST	0.797	1.333
State Excise Duties	0.657	0.662
Motor Vehicle Tax	0.758	0.891
Stamp Duty and Registration Fees	0.635	0.898
Other Taxes	1.049	0.167

Source (Basic Data): Finance Accounts and State Budget 2021-22

### ***The Transfers from Centre***

It has already been discussed as to how decline in central transfers affected the financial management in 2019-20 in earlier paragraphs. While a point has been made that the dependency of Sikkim on central transfers has gone down from an average of about 75 percent in earlier years to 52 percent in 2019-20. However, this relative change in shares between own revenues and central transfers has not happened due to rise in own revenue receipts. Own revenue receipts also failed to be buoyant over the years. This has resulted in overall deterioration of resource envelope and rise in fiscal pressure as the State remained dependent upon central transfers unpredictability in flow of funds, as was the case in 2019-20 brings lots of distortions.

In 2015-16, following the FC-XIV recommendations, the share in central taxes has more than doubled as compared to 2014-15, but grants from Centre has declined significantly. The share of grants from Centre to GSDP in 2015-16 came down to 5.62 percent, compared to 16.72 percent in 2014-15. In nominal terms the grants from Centre was Rs. 2427 crore in 2014-15, which came down to Rs. 934.20 crore in 2015-16. In 2029-20, both the tax devolution and grants declined considerably. Central transfers in nominal terms declined by Rs.1187 crores in 2019-20 as compared to the previous year. The year-on-year growth of central transfer shows that it declined by about 27 percent over the previous year.

### **3.3 The Expenditure Trends**

Deterioration in revenue receipts necessitates prioritizing spending items given the fiscal outcome targets like deficit and debt in FRBM Act. The adjustments are possible, if the size of the resource envelope is foreseen. While own revenue projections at states' level gives reasonably good score for budget realism, central transfers have remained unpredictable. Given the dependence of Sikkim on central transfers, it becomes difficult to make abrupt adjustments to spending, which are committed in nature.

#### ***Revenue Expenditure***

The impact of deterioration in revenue receipts seems to have affected revenue expenditure partially. As percentage to the GSDP, the revenue expenditure has gone down from 19.51 percent in 2018-19 to 19.05 percent in 2019-20. It is usually difficult to slash revenue expenditure given the long-standing commitments both in social sector and infrastructure building. In recent years the state has been implementing ambitious scheme like providing at least one government jobs to each family under 'one family one job'. These commitments make the revenue expenditure downward rigid.

The annual average growth rate of revenue expenditure in Sikkim, during the period 2011-12 to 2019-20, was 13.35 percent. The revenue expenditure grew at the rate of 18.35 percent in 2019-20 over a very high growth of 25.89 percent witnessed in the previous year. Despite some control over growth rate, its relative share increased in 2019-20 as capital outlay was reduced at a higher rate.

Broad composition of government expenditure in terms of revenue and capital expenditure classification reflects distribution of expenditure across sectors and to a certain extent shows the priorities depending on availability of aggregate revenue. Revenue expenditure, taking average of relative share during 2011-12 to 2019-20, constitutes about 80 percent of total expenditure (Table 3.3). As revenue expenditure contains large portion of committed spending, this is most likely to be met from the consolidated fund. Despite the pressure and demand for increasing this type of spending, the Government of Sikkim, have contained the growth of revenue expenditure over the years. While the relative share of revenue expenditure was rising since 2011-12, a declining trend has been witnessed after 2015-16. In fiscal year 2018-19, the relative share of revenue expenditure, however has increased to 80.19 percent as compared to

73.37 percent in the previous year. This share has further increased to 89.56 percent in 2019-20 due to decline in capital expenditure. This trend does not reflect favorably on quality of expenditure.

**Table 3.3**  
**Relative Share of Revenue and Capital Expenditure**

<b>Heads</b>	(Percent)								
	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>
Revenue Expenditure	79.78	74.85	76.84	77.39	85.18	84.02	73.37	80.19	89.56
Capital Expenditure	20.22	25.15	23.16	22.61	14.82	15.98	26.63	19.81	10.44

Source (Basic Data): Finance Accounts and State Budgets

Analyzing revenue expenditure in terms of resource allocation to different sectors assumes significance given its predominance in public expenditure. In revenue expenditure, the State government spent about 63 percent (average during 2011-12 to 2019-20) on social and economic services, out of which 38 percent was spent on social services (Table 3.4). Relative share of general services during the same period was 25 percent and grants to local bodies was 1 percent. The composition of revenue expenditure shows that the share of social and economic services has increased over the years. It is important for the Government of Sikkim to focus on social and economic sectors so that the overall composition of revenue expenditure adds value to the public expenditure.

**Table 3.4**  
**Composition of Revenue Expenditure in Sikkim**

<b>Heads</b>	Percent								
	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>
<i>General Services</i>	30.97	35.13	34.22	36.17	34.13	37.51	36.81	37.51	39.12
<i>Social Services</i>	42.46	37.79	42.19	38.12	33.92	35.24	36.90	39.64	36.44
<i>Economic Services</i>	25.27	26.17	22.42	24.46	30.89	25.78	24.77	21.59	23.08
<i>Assignment to LBs</i>	1.30	0.91	1.17	1.25	1.06	1.47	1.53	1.27	1.57

Downward rigid revenue expenditure can be analyzed in terms of share of a set of spending items that are contractual, committed, and pre-determined in nature cannot be avoided or postponed during the year in it. The expenditures on wages and salary, pension payments, and interest payment taken together refers to what is known as committed expenditure. Higher

share of committed expenditure in total revenue expenditure reduces the discretionary expenditure on providing public services and limits the degree of flexibility available to the government in determining allocation of public expenditures.

The share of committed expenditure in Sikkim has increased considerably in terms of its share of revenue receipts and revenue expenditure. While its share in revenue expenditure increased from 59.08 percent in 2011-12 to 65.77 percent in 2018-19, the share increased sharply to 74.94 percent in 2019-20 (Table 3.5). Similarly, share of committed spending in revenue receipts increased from 49.98 percent in 2011-12 to 57.58 percent in 2018-19, and spiked to 95.75 percent in 2019-20. Spending on salary and wages was the major reason for upward rise of committed expenditure and the spike in 2019-20. Salary and wages account for about 65 percent of total committed expenditure. In 2019-20, the salary and wages increased by Rs.997.78 crores as compared to the previous year.

According to the Government of Sikkim, the steep rise in committed expenditure was driven by salary and wages was due to payment of arrears for 6<sup>th</sup> Pay Revision Commission. The government has paid salary arrear amounting to Rs.605 crore and pension arrears amount to Rs.112 crores in 2019-20. This has increased the committed spending and the government failed to control aggregate revenue expenditure while faced with severe resource crunch.

**Table 3.5**  
**Committed Revenue Expenditure**

	(Percent)								
<b>Committed Expenditure</b>	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>
<b>As Percent of Revenue Receipts</b>									
Interest Payment	6.64	6.05	5.68	5.86	6.93	7.04	6.95	7.25	10.53
Pension	6.05	6.85	6.69	8.15	10.63	9.68	9.69	12.35	18.81
Salaries and wages	37.29	28.28	34.69	30.25	35.88	30.88	28.37	37.98	66.41
<b>Total</b>	<b>49.98</b>	<b>41.18</b>	<b>47.07</b>	<b>44.26</b>	<b>53.43</b>	<b>47.60</b>	<b>45.01</b>	<b>57.58</b>	<b>95.75</b>
<b>As Percent of Revenue expenditure</b>									
Interest Payment	7.85	7.93	7.31	7.14	7.19	8.56	8.72	8.29	8.24
Pension	7.15	8.98	8.62	9.92	11.04	11.79	12.17	14.11	14.72
Salaries and wages	44.08	37.09	44.65	36.83	37.25	37.58	35.62	43.38	51.98
<b>Total</b>	<b>59.08</b>	<b>54.00</b>	<b>60.58</b>	<b>53.89</b>	<b>55.48</b>	<b>57.93</b>	<b>56.51</b>	<b>65.77</b>	<b>74.94</b>

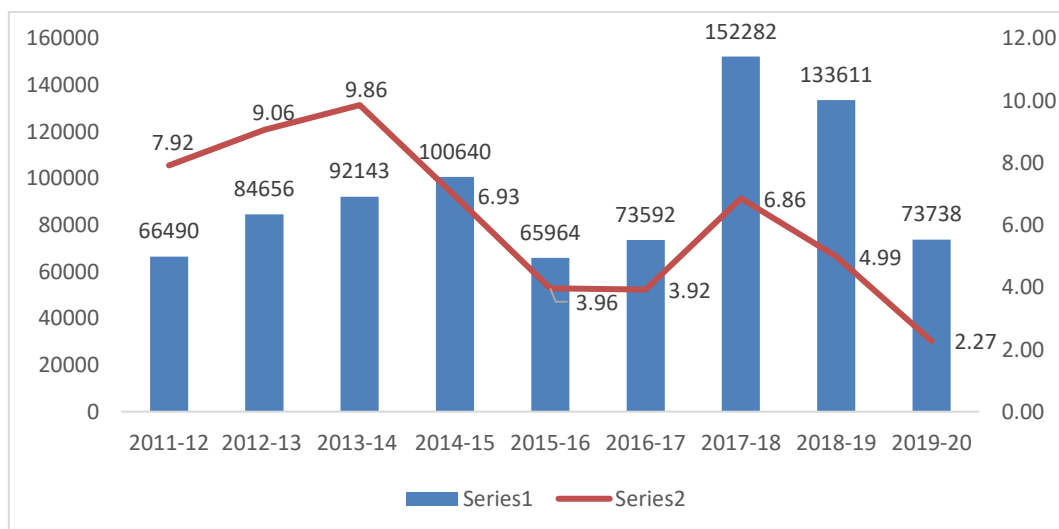
Source (Basic Data): Finance Accounts and State Budget 2021-22

### Capital Expenditure

Capital expenditure bore the brunt of revenue crunch in 2019-20. While capital expenditure is considered crucial for creating social and economic infrastructure, often it becomes residuary in the system depending upon availability of resources and other recurrent expenditure. Although, it remained reasonably high in the state as percentage to GSDP over the years, a declining trend was perceived due to resource problem, particularly after decline in central grants following FC-XIV recommendation. In 2019-20 capital expenditure as percentage to GSDP has plunged to its lowest.

The capital expenditure (taking general, social, and economic services and of loans and advances) declined in nominal terms from Rs. 1336.11 crores in 2018-19 to Rs. 737.38 crores in 2019-20 (Figure 3.4). While capital expenditure has remained volatile in the state. There was an increasing trend from 2011-12 to 2014-15. However, in 2015-16, the capital expenditure declined in nominal terms and as percentage to GSDP, it declined to 3.96 percent in 2015-16 from 6.93 percent in 2014-15. The decline in central grants after the recommendations of the FC-XIV played an important role in the resource allocation relating to capital investment. In 2019-20, the decline was much more as capital expenditure s percentage to GSDP fell to 2.27 percent as compared to 4.99 percent in 2018-19. In nominal terms the decline was to the extent of Rs.598.73 crores. Although the year-on-year growth rate of capital outlay has remained highly unstable, the decline in 2019-20 was 44.81 percent.

**Figure 3.4**  
**Capital outlay in Sikkim**



The size of the capital outlay in the state usually is linked with provisions made in the CSS and other central programs through NEC and NLCPR schemes. The state borrowing, which is usually spent on capital outlay, is limited to the ceilings fixed by the central government aligned with the fiscal deficit target stipulated by the FRBM Act. Thus, the capital outlay will continue to vary depending upon the flow of funds under the central programs and level of resources generated by the state. Decline of capital outlay in 2019-20 is symptomatic of resource trade-off faced by the government in budget management. It is important for the state government to invest efficiently by following the principles of public investment management as capital outlay has a major role to play in stimulating the rate of growth of the state economy. The state government should finance identified public investments with high social returns.

### 3.4 Aggregate Spending Pattern and Priority Areas

Aggregate spending pattern, taking both the capital and revenue expenditure, gives a perspective on spending priorities of the Government and the emerging focus areas. The composition of aggregate expenditure shows that on an average the total expenditure net of debt repayment available to the Government to be utilized on various sectors and administrative services was about 95.70 percent during 2011-12 to 2019-20 (Table 3.6). The relative share of debt repayment and loans and advances was 3.78 and 0.52 percent respectively during the same period. The relative share of debt repayment has been showing an increasing trend from 1.56 percent in 2011-12 to 5.63 percent in 2019-20.

**Table 3.6**  
**Composition of Total Expenditure**

Heads	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Total Expenditure net of Debt	96.89	97.78	97.55	97.45	95.04	94.48	94.02	93.91	94.14
Repayment									
Public Debt	1.55	2.08	2.20	1.96	4.36	5.16	5.70	5.42	5.63
Loans and Advances	1.56	0.15	0.25	0.60	0.60	0.36	0.28	0.67	0.23

The composition of total expenditure (net of debt repayment, loans, and advances) in the state indicates that interest payment, pension, and administrative services are important source of Government spending (Table 3.7). These three spending heads taken together constituted 25.14 percent of total expenditure in 2018-19. Expenditure on education, health, water supply and

sanitation, and welfare and nutrition remained large spending departments in the social sector. However, there has not been a rise in the relative share of these spending in these services except that of water supply, sanitation and urban development. Agriculture, rural development, electricity, and transport have emerged as priority sectors in the economic services as shown in their relative shares in resource allocation.

**Table 3.7**  
**Composition of Total Expenditure (Net of Debt Repayment)**

Heads								Percent	
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	
Interest Payment	6.07	5.81	5.48	5.38	5.82	6.80	6.02	6.24	
Pension	5.53	6.57	6.46	7.48	8.94	9.36	8.40	10.63	
Administrative Services	8.92	9.65	9.82	8.61	9.11	9.46	7.77	8.27	
General Services (Rev. Exp.)	3.42	3.68	3.89	5.80	3.76	4.16	3.22	3.12	
Compensation to Local Bodies	1.00	0.67	0.88	0.94	0.86	1.17	1.05	0.96	
Capital Outlay on Police	0.19	0.20	0.37	0.45	0.11	0.15	0.11	0.02	
Capital Outlay on Public works	0.62	2.23	3.83	2.01	1.31	1.35	2.31	0.98	
Education Sports Art and culture	17.58	17.24	17.24	17.09	17.58	17.08	15.65	15.35	
Medical and Public Health	6.73	6.63	5.90	5.49	5.40	5.54	7.41	5.61	
Water Supply Sanitation Housing and Urban Development	6.04	7.94	8.52	8.52	4.65	5.93	7.15	8.88	
Welfare of Scheduled Castes Scheduled Tribes and other Backward Classes	0.65	0.60	0.69	0.65	0.77	0.75	0.81	1.15	
Social Welfare and Nutrition	9.32	2.26	4.11	2.15	2.72	2.19	2.07	3.09	
Other Social Services (Total Exp.)	1.32	1.49	1.77	0.92	0.81	1.59	1.28	1.02	
Agriculture and Allied Services	7.65	6.49	6.15	6.57	7.01	5.81	5.22	6.36	
Rural Development	3.71	3.78	2.79	4.10	3.24	5.16	3.13	2.11	
Irrigation and Flood Control	1.37	1.82	1.46	0.50	0.78	0.64	0.76	1.19	
Energy	4.31	4.41	3.46	3.81	5.65	5.69	4.76	3.88	
Industry and Minerals	1.55	0.86	0.84	1.05	0.75	0.70	1.19	0.55	
Transport	7.64	12.35	10.48	8.60	7.44	8.36	13.46	12.34	
Science and Environment	0.09	0.06	0.06	0.07	-0.30	0.10	0.08	0.16	
General Economic Services	2.60	2.50	2.26	6.72	8.09	1.87	1.75	1.46	
Other Economic Services	0.58	0.54	1.09	0.54	0.56	0.65	0.42	0.54	

Source (Basic Data): Finance Accounts and State Budget 2020-21



### 3.5 Public Debt and Other Liabilities

Public debt and other liabilities of the State include internal debt, loans from the central government, small savings and provident fund, reserve funds and deposits. The last three items are part of public accounts and net of these items are utilized to finance fiscal deficit. The debt-GSDP ratio that is targeted under FRBM Act takes outstanding amount of all these items together. The FRBM Act of the state, usually defines the path of the debt-GSDP ratio by following central finance commission recommendations.

Annual borrowing limit for the state is fixed by the Union government, which now is pegged at the fiscal deficit limit prescribed by FRBM Act. The composition of state debt also has undergone changes after the recommendation of FC-XII limiting loans from central government. At the same time the recommendation of the FC-XII helped in reducing average cost of debt and debt burden of the States through debt restructuring formula. The debt restructuring formula was conditioned on states willingness to adopt fiscal rules and abide by the fiscal consolidation path suggested by the Commission. The FC-XIII recommended state wise debt-GSDP ratios, which became part of state FRBM Acts. The fiscal management principles contained in FRBM Act calls upon the state to maintain debt burden at sustainable level.

**Table 3.8**  
**Liabilities of the Government of Sikkim**

	(Percent of GSDP)								
	2011- 12	2012- 13	2013- 14	2014- 15	2015- 16	2016- 17	2017- 18	2018- 19	2019- 20
<b>Public Debt</b>	<b>22.05</b>	<b>21.17</b>	<b>23.39</b>	<b>17.29</b>	<b>17.85</b>	<b>18.69</b>	<b>18.99</b>	<b>18.61</b>	<b>16.65</b>
Internal Debt	20.18	19.57	22.03	16.46	17.16	18.10	16.31	18.25	16.34
Loans from the Central Govt.	1.87	1.59	1.36	0.83	0.68	0.59	2.68	0.36	0.31
<b>Other Liabilities</b>	<b>8.34</b>	<b>8.35</b>	<b>9.45</b>	<b>6.69</b>	5.96	<b>6.21</b>	<b>5.56</b>	<b>5.04</b>	<b>6.15</b>
Small savings, Provident Fund	6.89	6.68	7.34	4.89	4.50	4.43	4.11	3.75	3.58
Reserve Fund	0.22	0.14	0.55	0.84	0.51	0.50	0.26	0.24	1.45
Deposits	1.23	1.53	1.56	0.95	0.96	1.28	1.19	1.04	1.11
<b>Total Public Debt &amp; Other Liabilities</b>	<b>30.39</b>	<b>29.51</b>	<b>32.84</b>	<b>23.98</b>	<b>23.81</b>	<b>24.90</b>	<b>24.55</b>	<b>23.65</b>	<b>22.80</b>

Source (Basic Data): Finance Accounts, Relevant Years. For GSDP data, figures used in state budget are used here to find the ratios.

The FC-XIV in their fiscal roadmap for the states recommended anchoring the fiscal deficit at 3 percent of the GSDP. The states can avail the flexibility to increase this limit by 0.5 percentage points, 0.25 percent separately depending upon conditions prescribed. One of the major conditions was to limit the debt-GSDP ratio to 25 percent in the previous year. Thus, for all effective purposes the benchmark of debt-GSDP ratio was 25 percent. The aggregate level of indebtedness in 2019-20 indicates that the state government complied with the FC-XIV recommendations. The indebtedness of the Government of Sikkim, which was showing some decline since 2011-12, has started increasing in 2016-17 (Table 3.8). Taking all types of liabilities, it stands at 22.80 percent in 2019-20. Increase in internal debt of the Government was one of the factors for this rise.

## **4. Compliance to Provisions of FRBM Act – 2019-20**

The assessment of compliance of the state government to the FRBM Act provisions for the year 2019-20 assumes significance as this year posed severe fiscal challenges due to significant decline in resource availability. The fiscal year 2019-20 is also important to evaluate state's capacity, commitment, and fiscal management practices in pre-pandemic period. This is the period, when the states were facing resource problem and fiscal stress was building up. It is demanding for a state like Sikkim to remain on fiscal consolidation path when confronted with large scale deterioration in resource envelope. Prudence in fiscal management needs to be calibrated keeping the state responsibilities and commitments in consideration.

Conventional budgeting is an open-ended process that does not restrict government spending based on popular demands beyond its resource capacity resulting in fiscal imbalances. Established budgeting rules and regulations also do not help in observing the agreed upon fiscal targets. It is the fiscal rules (in the form of FRBM Act) that facilitates budgeting within fixed constraints stipulated through annual targets, improves transparency and enhances political acceptance. However, it is crucial to acknowledge that economic condition generally determines its adherence.

The assessment report in addition to fiscal targets, looks into issues like establishing fiscal transparency, medium term framework for budget management, improving budget predictability, and improving institutional measures. These are key features of a sound public financial management system and are part of building blocks of FRBM Act.

### **4.1 Provisions of Sikkim FRBM Act**

Major milestones in fiscal consolidation process includes maintaining balance in revenue account, limiting fiscal deficit to fiscal rules targets and prudent debt management. The FRBM Act of the State, stipulates these fiscal targets and contains the broad fiscal management principles and transparency measures. The major provisions of the Sikkim FRBM Act are as follows:

- Present a Medium-Term Fiscal Plan (MTFP).
- Undertake appropriate fiscal management principles indicated in the Act to achieve the targets.
- Achieve fiscal targets relating to deficit, stock of debt, and outstanding guarantees.
- Take suitable measures to ensure greater transparency in the fiscal operation.
- Conform to the measures prescribed for enforcing compliance to the Act.

The rules associated with the Act further detail the requirements, documents to be prepared, and the quantitative limits of the fiscal indicators. The rules provide the form in which the medium-term fiscal statements are presented to provide relevant information about Government's activities and enhance transparency.

- **The Macro-economic Statement:** It is expected to give an overview of the state economy, analysis of GSDP growth, overview of state government finances and assessment regarding growth prospects and fiscal prospects.
- **Medium Term Fiscal Policy Statement:** The Medium-Term Fiscal Policy (MTFP) forms the core of the FRBM Act related documents. This statement gives two-year outward projection of fiscal outcomes like revenue deficit, fiscal deficit, and outstanding liabilities as percentage to the GSDP in addition to the revised estimates of current year and budget estimates of the ensuing year. The statement is supposed to include assumptions relating to the trend of fiscal variables leading to the projection of major fiscal outcomes. The MTFP gives assessment regarding the balance between revenue receipts and revenue expenditure and use of capital receipts for generating productive assets. Thus, the MTFP contains a fiscal plan of the state government for the ensuing budget year and three outward years.
- **The Fiscal Policy Strategy Statement:**
  - a) The fiscal policy strategy statement contains the fiscal stance of the state government with respect to fiscal targets for the ensuing year, revenue generation efforts, expenditure plan and consequent borrowing requirements.
  - b) The strategic priorities of the government;
  - c) The reasons for any major deviation in fiscal measures pertaining to taxation, subsidy, expenditure, administered pricing and borrowings;
  - d) An evaluation of the current policies of the Government based on fiscal objectives and fiscal principles enunciated in the Act.
- **Disclosures:**

The FRBM Act stipulates the governments to provide data and information on fiscal variables and outcomes of fiscal transactions. These are called disclosure statements and rules to the Act specifies the format in which this information is to be given. The wide range of data and information given in FRBM document is expected to enhance transparency in the system and help the policy makers to take informed decisions.

- **Half-yearly Progress Report**

Minister-in-charge of Finance is supposed to present a half-yearly progress report on achievement of FRBM Act provisions. If there is any shortfall in revenue or excess of expenditure over the half-year targets mentioned in the Fiscal Policy Strategy Statement, the minister is supposed to provide the account of corrective measures taken by the government.

The MTFP provides the fiscal plan of the Government for the budget year and two outward years delineating revenues raising efforts, resource allocation priorities, and borrowing plan in a transparent way. The Government of Sikkim presented the MTFP for the year 2019-20 based on the FRBM rule format that contains macroeconomic statement, projections of fiscal targets and fiscal management principles with regard to revenues and expenditures. This statement contains three-year rolling targets for revenue deficit, fiscal deficit, and the debt-GSDP ratio – for the ensuing year, and for two subsequent years synchronizing with the Act provisions. It also contains medium-term fiscal objectives, perspective on the growth of state economy, strategic priorities for revenues and expenditures, and conformity of the fiscal outlook of the Government with the fiscal principles enshrined in the Act. The first year of the MTFP projections is the budget estimates for the year 2019-20. The MTFP taking into account existing programs and new programs announced by the Government in its spending projection.

While MTFP is presented along with budget, the Act mandates the state government to present a half-yearly report card on progress to achieve the FRBM targets as part of enforcement mechanism. The rules to the FRBM Act detail the fiscal transparency measures, which are disclosures on fiscal operations and data and information to be given along with the budget to ensure greater transparency. Fiscal management principles enshrined in the FRBM Act are guiding principles to conduct the fiscal policy in the State to facilitate achievement of the required fiscal targets.

- **Fiscal Targets**

The Government of Sikkim, as per the FRBM Act, is required to achieve the following mandatory fiscal targets;

1. Maintain revenue account balance beginning from the year 2011-12;
2. Reduce the fiscal deficit to 3.5 percent of the estimated Gross State Domestic Product in each of the financial year starting from 2011-12 and reduce the fiscal deficit to not more than three percent of the estimated Gross State Domestic Product at the end of 31<sup>st</sup> March 2014 and adhere to it thereafter. The FC-XIV provided flexibility to increase the fiscal deficit by 0.5 percentage points, 0.25 percentage points separately, based on certain conditions relating to fiscal outcomes in the previous years.
3. Cap the total outstanding guarantees within the specified limit under the Sikkim Ceiling on Government Guarantees Act, 2000 (21 of 2000).
4. Ensure that the outstanding debt-GSDP ratio follows a sustainable path emanating from the above targets of the deficit as specified by the Government beginning from the fiscal year 2011-12. The level of debt-GSDP is fixed based on the recommendations of the Central Finance Commission.
5. The FRBM Act of the State was supposed to take recommendations of the FC-XIV, if any, to revise its debt-GSDP targets. The FC-XIV, while anchoring the fiscal deficit at 3 percent of the State GSDP, recommended an increase of 0.5 percentage points, 0.25 percentage points separately, based on certain conditions relating to fiscal outcomes in the previous years. One of the conditions was to limit the debt-GSDP ratio to 25 percent in the second preceding year. The FC-XIV, however, gave an illustrative operation of fiscal rules in which they used debt-GSDP ratios to reduce the aggregate debt-GSDP ratio to the desired fiscal consolidation path. The state government took the debt-GSDP ratio worked out in this illustrative exercise as recommended targets for Sikkim and included them in the amendments in 2016. These targets were - 2015-16 – 20.63%, 2016-17 – 20.09%, 2017-18 – 19.66%, 2018-19 -- 19.32%, and 2019-20 -- 19.04%. These targets were less than what the state has been reporting since 2015-16. The debt-GSDP targets stipulated in the amended FRBM Act of 2016 looks little problematic from fiscal management point of view as it makes a sudden reduction from 55.90 percent in 2014-15 to 20.63 percent in 2015-16. However, for the purpose of this review report we have used debt-GSDP targets of 25 percent as the benchmark to assess the State's compliance.
6. The states in India faced fiscal stress in 2019–20, to a large extent due to adjustment of tax devolution by the central government amounting Rs. 58,843 crores due to lower collection

of central taxes in 2018-19. To provide relief to states on account of lower tax devolution in 2019-20, central government decided to allow additional borrowing of Rs. 58,843 crores in 2019-20. It cannot be claimed in subsequent years. This onetime special dispensation was subject to amendment of state's FRBM legislation for 2019-20. Under this onetime dispensation, Sikkim was allowed to borrow Rs. 216 crores in 2019-20.

7. Thus, for all practical purposes, after the amendment to the Act in 2019-20, the fiscal deficit target stood at 4.26 percent of GSDP. This included usual 3 percent FRBM Act target, 0.5 percent flexibility provided by FCXIV, and special onetime dispensation borrowing of Rs. 216 crores for 2019-20.

#### **4.2 Compliance of the State Government to the FRBM Act Targets: 2019-20**

The fiscal situation discussed in the earlier sections shows that it was very unfavorable in 2019–20 for the State. The revenue receipts of the state as percent to GSDP declined to 14.91 percent as against 22.29 percent in the previous year. The decline in revenue receipt was mostly driven by central transfers, which went down to 9.79 percent in 2019-20 as compared to 16.29 percent in the previous year. Own revenue of the state as percent to GSDP also showed a marginal decline. The year-on-year growth rate in 2019-20 shows that revenue receipts declined by 18.91 percent.

The impact of this massive fall in revenue receipts, however, was not seen in terms of similar spending adjustments in 2019-20. The revenue expenditure, which accounts for about 80 percent of total expenditure, fell to 19.05 percent relative to GSDP in 2019-20 as compared to 19.51 percent in the previous year. Indeed, a large part of the revenue expenditure was committed and thus, downward rigid. The state government also paid the arrears of salary and pensions as per the recommendation of 6<sup>th</sup> pay commission, which added to the revenue expenditure. It was the capital expenditure, which is treated as residual in the system, witnessed large fall to 2.27 percent of GSDP in 2019-20 as compared to 4.99 percent in the previous year.

The overall impact of this fiscal management was sharp rise in revenue and fiscal deficit way beyond the FRBM Act targets (Table 4.1).

- **Revenue Deficit/Surplus:** As against FRBM target of generating surplus in the revenue account, a sharp rise in revenue deficit was seen to the tune of 4.14 percent. In fact, during the post-FRBM period, this is the first time revenue account went into deficit.

**Table 4.1**  
**FRBM Act Targets and Fiscal Achievements during 2019-20**

Percent

	<b>Targets</b>	<b>Achievements</b>
Revenue Deficit (-)/surplus (+) % of GSDP	Surplus	-4.14
Fiscal Deficit % of GSDP	-4.26	-6.41
Total Debt Stock % of GSDP	19.04 – FRBM Act Target 25 – FCXIV condition for prudence in fiscal management	22.80
Outstanding Guarantees	Restricted to the limit under the Sikkim Ceiling on Government Guarantees Act, 2000	

- Fiscal Deficit:** The target for 2019-20 was revised upwards to 4.26 percent of GSDP by including the flexibility of 0.5 percent allowed by FCXIV and one time borrowing facility of Rs. 216 crores allowed by the central government to give relief on account of lower tax devolution in 2019-20. The fiscal deficit, however, increased by large amount to 6.41 percent of GSDP. As pointed out earlier, large deterioration in revenue receipts and not containing revenue expenditure adequately in response to lower revenue receipts resulted in large fiscal deficit.
- Outstanding Debt-GSDP Ratio:** There are two benchmarks to assess outstanding debt burden of the state as percent to GSDP. Strictly according to the FRBM Act provisions, the outstanding debt-GSDP ratio of 22.80 percent exceeds the target of 19.04 percent in 2019-20. However, as discussed earlier targeting this level debt-GSDP ratio in the context of award period of FC-XIV is severely restricting. Thus, a target of 25 percent, which the FC-XIV held as prudent to allow the state the flexibility of enhancing fiscal deficit is a much better benchmark to compare with. If we go by this, then the outstanding debt as percent to GSDP has remained within the limit.
- Outstanding Guarantees:** Guarantees are contingent liabilities on the Consolidated Fund of the state in case of default by the borrower for whom the guarantees are extended. The Sikkim Government Guarantees Act, 2000, stipulates that the total outstanding Government guarantee as on the 1<sup>st</sup> day of April of any year shall not exceed thrice the State's Tax receipts of the second preceding year. Thus, the outstanding guarantees in 2019-20 should be compared with three-times the tax receipts of the state in the year 2017-18. The outstanding guarantee in 2019-20, according to the Finance accounts of the state, stood at Rs. 3543.53 crores and interest on this was Rs. 205.79 crores. This has remained below the permissible level following the stipulation of the Guarantee Act. Outstanding



guarantees, however, has increased significantly. It needs to be pointed out here among the guarantees listed in the Finance Account the largest is the guarantees of Rs .2688.44 crores given to SPICL (TEESTA URJA LTD) Stage III.

Financing of fiscal deficit in the fiscal year 2019-20 shows that the net market borrowing of the state government was limited to Rs. 432 crores (Table 4.2). The major financing items have come from net public accounts. The suspense and miscellaneous was the largest financing item amounting to Rs.1392.35 crores. Other big financing items was the reserve fund. The suspense and miscellaneous include all the cash investments by the state governments in various financial instruments, which was used to finance the deficit. While, fiscal deficit has increased significantly in 2019-20, the outstanding debt did not rise to that extent because of using public account funds financing fiscal deficit.

**Table 4.2**  
**Financing Fiscal Deficit**

Rs in Crore

	2015-16	2016-17	2017-18	2018-19	2019-20
Market Borrowings	449.46	550.41	744.13	790.29	432.07
NSSF	23.34	-7.72	-23.61	-15.05	-13.46
Loans from Financial Inst.	-6.91	-2.12	-2.1	-0.6	-2.39
Loans from GoI	-7.14	-3.48	-7.6	-5.33	3.21
Small Savings, PF	(+) 37.65	(+) 83.3	(+) 80.57	(+) 93.93	157.21
Deposits and Advances	21.64	80.11	24.17	15.53	81.69
Suspense and Miscellaneous	-5.42	-827.7	-13.18	-587.95	1392.35
Remittances	82.51	70.96	179.89	130.65	-115.86
Reserve Fund	59.89	124.82	35.72	5.25	407.27
Cash Balance	(-) 36.86	(+) 102.63	(-) 484.99	(+) 476.9	(-) 260.91
Gross Fiscal Deficit	-519.92	86.3	-461.88	-642.32	-2081.18

Source Finance Accounts, Budget Documents of relevant years

Note: The figures are net of disbursements/outflows during the year

### 4.3 Fiscal Management Principles

The State FRBM Act includes guiding fiscal management principles to enable the government to take appropriate public financial management decisions. The fiscal management principles reflect the necessity of strengthening PFM institutions. The Act does not fix any targets or give any indicator to assess these principles like those for mandatory fiscal targets. The broad fiscal management principles include the following:

- To maintain prudent debt level

- Manage guarantees
- Ensure borrowings to be used for productive purposes
- Pursue revenue expenditure policies to provide impetus to economic growth

The objective of including fiscal management principles in the FRBM Act is to influence the policy making to achieve policy objectives and facilitate adherence to agreed-upon fiscal strategy. These principles aim at enhancing accountability and help in achieving mandated fiscal targets. The principles reflect broad objectives of economic policies governments at any level. These can be properly assessed only over a reasonably long period with continuous monitoring of relevant fiscal data. In the context of Sikkim, the fiscal management principles assume significance due to the challenges like lack of adequate resource base, a large committed spending, and provision of public services in a difficult terrain, which becomes costly. The important fiscal management principles enshrined in the FRBM Act are discussed here.

### ***Prudency in Debt Management***

Debt management policy of any government aims at meeting the financing needs at the lowest possible long-term borrowing costs and to keep the total debt within sustainable levels. State governments in India are not free as far as their borrowing powers are concerned. A state need Centre's consent to borrow in case the state is indebted to the Centre over a previous loan following Article 293(3). In practice Ministry of Finance, Government of India, determines the limit for state government borrowing. As RBI manages the public debt of state governments facilitates their investment of their surplus cash balances, the states do not face the test of the market based on their fiscal capacity and economic

The practice of determination of borrowing limit by the central government acts as an external control in rule based fiscal management. Since the recommendations of the FC-XIII, the central government fixes the borrowing limit of a state based upon the fiscal deficit target stipulated in the FRBM Act. Due to favorable cash balance position, the state government sometimes does not exhaust the borrowing limit. In the fiscal year 2019-20, as it has been pointed out earlier, the debt burden of the state did not rise to the extent of the fiscal deficit due to utilization of ash investment.

The set of principles relating to debt management suggested in the FRBM Act of Sikkim are the following;

- Borrowing responsibly to maintain debt at a prudent level
- Manage guarantees and other contingent liabilities within stipulated limits, and;
- Using borrowed funds for productive purposes to create capital assets. This is akin to the golden principle of not using borrowed resources for financing recurrent expenditure.

The debt stock as percentage of GSDP at 22.80 percent in 2019-20 satisfies the test of prudence as suggested by the FC-XIV. High fiscal deficit of 2019-20 should not be repeated, which will make the debt management unsustainable.

The state government kept the guarantees within the limit set under the Guarantees Act of 2000. As borrowing under letter of comfort given to SPICL Stage III is accounted for under the guarantees, the aggregate guarantee in 2019 has come very close the limits under the Act. This issue needs to be considered as fiscal risk in future year fiscal management.

Entire borrowed funds are utilized to create capital assets where the revenue account is balanced. If there is any surplus in the revenue account, that is used in capital outlay. As the revenue account was deep in deficit in 2019-20 and constituted about 64 percent of fiscal deficit, a part of the borrowed fund is utilized to finance revenue account deficit.

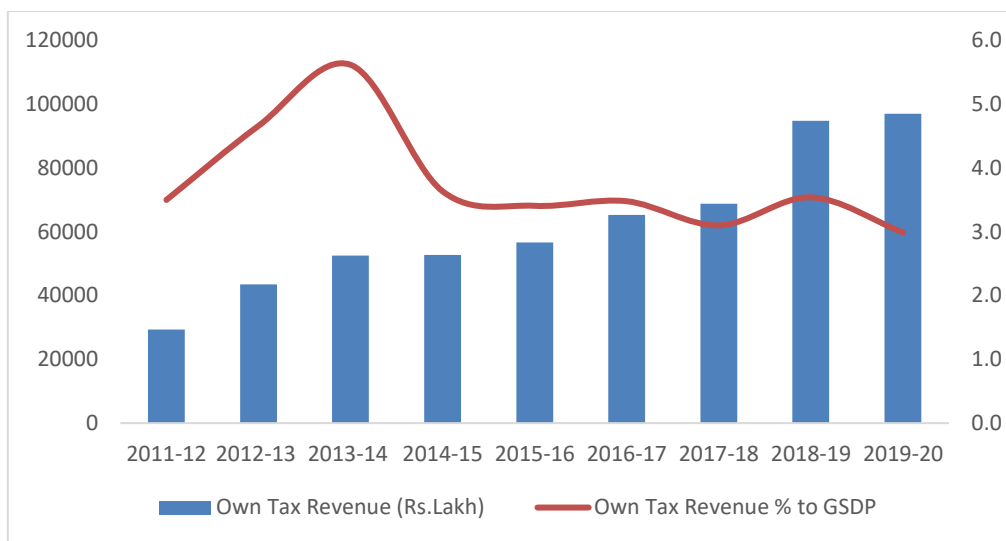
### ***Simplifying Tax Policy and Administration***

The FRBM Act requires the State Government to maintain integrity of the tax system by minimizing discretionary policies like special incentives, concessions and exemptions. It also emphasizes on pursuing the tax policy with due regard to economic efficiency and compliance cost. Collecting sufficient revenues to carry out functional responsibilities without distorting economic decisions of people relative to saving and consumption and market behavior imparts economic efficiency to the tax system.

Own tax revenue constituted about 16 percent of total revenue receipts in 2018-19, which increased to 20 percent in 2019-20. The change in relative share was more due to sharp

deterioration in central transfers. As percentage to GSDP, it declined from 3.54 percent to 2.99 percent (Figure 4.1). One of the important features of a good tax system is to maintain stability and predictability in the level of tax burden. There have not been many changes in tax rate of individual State taxes. While, the VAT regime, introduced in 2005 had stabilized in terms of rate and base structure in the State, the newly introduced GST has emerged as an important source of revenue for the government. Decline in growth own tax revenue in 2019-20 is the precursor to more difficult year of Covid-19 affected 2020-21.

**Figure 4.1**  
**Own Tax Revenue as Percentage of GSDP**



Cost recovery and equity have been the core themes in the case of non-tax revenues according to the fiscal management principles enunciated in FRBM Act. Non-tax revenue of the state on an average contributes about 10 percent to the aggregate revenue receipt. The major share of non-tax revenue of the State comes from provision of electricity and transport and lottery operation. In addition to these sources, the non-tax revenue includes income from interest earnings, police, and forestry. The lottery income has not proved to be stable source of income. The scope for reducing subsidy and improving cost of recovery from other services provided by the government in the social and economic sectors seems to be limited. However, the Government should make efforts to improve recovery cost in economic sectors by improving the quality of the service provided.

### ***Expenditure Policy and Institutional Measures to Improve Quality of Expenditure***

The FRBM Act calls upon the state government to focus on economic growth, poverty reduction, and improvement in human development in allocating resources. The fiscal management principles also require the Government to improve institutional framework to maintain physical assets, increase transparency, minimize fiscal risks associated with public sector undertakings (PSUs), and formulate realistic budget formulation to minimize the deviations during the course of the year. The achievement of these goals needs to be assessed over a long period.

In an earlier section we have shown emerging priority sectors of the state by analyzing relative expenditure shares of different sectors. While the interest payment, pension, and administrative services have remained important spending items, education, health, agriculture, rural development, transport, electricity, and water supply and sanitation and urban housing continue to be large spending departments in Sikkim. This spending pattern reveals the focus areas of the Government, which broadly includes rural, and agriculture sector and infrastructure.

Sharp decline in capital outlay in 2019-20 is a matter of concern relating to quality of expenditure. The Government needs to expand its own resource base in addition to adopting better expenditure management practices to get value for money in the utilization of resources in the priority sector.

The achievement of socio-economic development in Sikkim has been significant. The State economy has experienced substantial growth in recent years and the per capita income of the state has increased from Rs.1, 81,842 in 2011-12 to Rs. 4, 61, 904 in 2019-20 at current prices. The major socio-economic indicators for the State show commendable improvement. The poverty ratio has declined to 8.19 per cent as compared to all India average of 21.92 per cent in 2011-12. The literacy rate at 81.40 per cent in 2011-12 is significant achievement. The IMR has gone down to 24 per 1000 in 2011 as compared to the all India average of 44.

Fiscal transparency measures enunciated in the FRBM Act requires the state government to minimize the secrecy and disclose data and information relating to the fiscal operations. The rules to the Act specify the data and information to be disclosed along with the budget

documents. However, these disclosure statements containing data and information do not cover all aspects of budget management.

The public financial management system in general and budgeting system in particular suffer from lack of predictability in fund flows resulting in discrepancies between intents and achievements. The fiscal management principles enshrined in the Act cautions to avoid such divergences by improving efficiency of budget management practices. The State is heavily dependent on central transfers that includes share in central taxes and central grants. In addition to centrally sponsored schemes, grants from agencies like DONER and NEC for infrastructure projects form significant part of funding. Many a times the expenditures planned in the budget go awry due to non-receipts of components of these funds and late receipt of grants towards end of the financial year. It is important for the State Government to step up coordination with the Central agencies to improve the fund-flow to planned projects and programs.

#### **4.4 Budget Credibility: Projections and Outturns**

The FRBM Act in the state calls upon to establish stability and predictability in the fiscal management for which the budget should be formulated in an objective manner with due regard to the general economic outlook and realistic revenue prospects and minimize deviations during the course of the year. Although, there are procedures to adjust the budget through supplementary demands to take care of exigencies and to use surplus funds from other programs, these adjustments should not be too large to reduce the sanctity of the budget.

The performance of sub-national governments, in terms of service delivery and achieving policy goals, depends upon the performance of their budget. State governments in India bear major functional responsibilities following constitutional provisions spanning over social and economic sectors. Spending at states level is also higher than the central government due to the larger functional responsibilities. As the central government has more buoyant source of revenues, there is system of resource transfers to states following recommendation of central finance commissions and through centrally sponsored schemes (CSS). Given the functional responsibility and dependence on central resources, a credible budget becomes crucial to implement the planned policies.

A realistic budget minimizing deviation from budget estimates implies the capacity of the Government to deliver the public services as promised in budget. Ability to raise the projected revenue and utilize the budgeted expenditure becomes crucial in this context. The importance of this feature lies in avoiding bias in forecasting the revenues and allocating resources to various programs. Higher projection of revenue to fund announced programs creates huge inconsistencies in budget execution. At the same time underestimating the revenue results in utilization of excess funds without proper planning and going through established accountability framework. As Sikkim depends considerably on the central transfers, realizing the estimated resource depends upon the actual flow of grants.

Comparison of actual revenue generated, and expenditure incurred with the original approved budget and the extent of deviation from the projections gives the measure of budget credibility. In this section, a comparison between budget estimates and outturns of revenue receipts and expenditure for the year 2019-20 is provided in Table 4.3 to show the deviation from budget estimates. This exercise on budget credibility helps understanding many of the observation made earlier relating to revenue effort and spending pattern.

**Table 4.3**  
**Budget Estimates and Outturns for the year 2019-20**

(Rs. Lakh)

	2018-19	2019-20	2019-20 (BE)	Difference (Actual to BE – 2019- 20)	Difference in % to BE
<b>Revenues</b>	<b>597040</b>	<b>484127</b>	<b>739744</b>	<b>-255617</b>	<b>-34.55</b>
<b>Own Tax Revenues</b>	<b>94802</b>	<b>97040</b>	<b>122022</b>	<b>-24981</b>	<b>-20.47</b>
<b>Own Non-Tax Revenues</b>	<b>65778</b>	<b>69340</b>	<b>70454</b>	<b>-1114</b>	<b>-1.58</b>
<b>Central Transfers</b>	<b>436460</b>	<b>317746</b>	<b>547268</b>	<b>-229522</b>	<b>-41.94</b>
Tax Devolution	278961	229556	296952	-67396	-22.70
Grants	157499	88190	250316	-162126	-64.77
<b>Revenue Expenditure</b>	<b>522658</b>	<b>618508</b>	<b>712909</b>	<b>-94401</b>	<b>-13.24</b>
General Services	196025	241977	282590	40613	-14.37
Social Services	207177	225369	252676	27307	-10.81
Economic Services	112817	142776	167790	25014	-14.91
<b>Capital Expenditure</b>	<b>133611</b>	<b>73738</b>	<b>112135</b>	<b>-38397</b>	<b>-34.24</b>
Capital Outlay	129131	72061	110970	-38909	-35.06
Net Lending	4480	1677	1164	513	44.02
<b>Revenue Deficit</b>	<b>-74382</b>	<b>134381</b>	<b>-26835</b>	<b>161216</b>	
<b>Fiscal Deficit</b>	<b>59229</b>	<b>208118</b>	<b>85299</b>	<b>122819</b>	
<b>Primary Deficit</b>	<b>15924</b>	<b>157150</b>	<b>31581</b>	<b>125569</b>	
<b>Outstanding Debt</b>	<b>633507</b>	<b>740067</b>	<b>711404</b>	<b>28660</b>	

Source: Basic data – Finance Accounts and Budget Document for the relevant years

Note: Negative sign for revenue deficit indicates surplus

The sharp decline in growth of aggregate revenue receipt in 2019-20 over the previous year has already been discussed. In 2019-20, the government budgeted the aggregate revenue receipt at Rs.7397.44 crores and managed to generate Rs. 4841.27 crores. When compared to the budget estimates, the actual receipts fell short of Rs.2556.17 crores, which amounts to a large 34.55 percent of budget estimates (Table 4.3). Such a large deviation from budget estimates has the potential to distort all the spending plans of the government. According to Public Expenditure and Financial accountability (PEFA) framework, deviation above 8 percent gets the lowest score of D in an ordinal scale between A to D.

The components of revenue receipts shows that the deviation of actual receipts over budget estimates for central transfers is the major reason for large shortfall in revenue receipts. The aggregate central transfers fell short of the budget estimates by Rs. 2295.22 cores in 2019-20, which constituted 41.94 percent of budget estimates. Tax devolution to the state fell short of budget estimates by Rs. 673.96 crores or 22.70 percent of the budget estimates. The shortfall in grants from Centre was even larger. Taking all kind of grants, the actual receipt was less by Rs.1621.26 crore from the budget estimates, which forms about 64.77 percent of the budget estimates. The budget projection in the case of both tax devolution and grants has gone totally awry in 2019-20.

In addition to decline in central transfers over the budget estimates, the own revenue receipts also fell short of budget projections. Own tax revenue outturn fell short of budget estimates by Rs.249.81 crores, which amounts to a deterioration of 20.47 percent over the budget estimates. Decline in non-tax revenue, however, was less at 11.14 crores, which amounts to 1.58 percent of budget estimates. Generating less revenue as compared to the budget target, when there was a massive fall in central transfers, further reduced the aggregate revenue receipts as compared to the budget estimates. The GST outturn in 2019-20 exceeded the budget estimates by about 9.61 percent.

The aggregate spending outturns for the year 2019-20 shows that both revenue and capital expenditures fell short of budget estimates, the latter witnessing a large decline. While revenue expenditure fell short of 13.24 percent over budget projections, capital outlay was reduced by a massive 34.24 percent over the budget projections. The shortfall in revenue expenditure was Rs. 944.01 crores and in the case of capital outlay it was Rs. 383.97 crores. Restricting capital outlay reduced it to 2.27 percent of GSDP in 2019-20 as compared to 4.99 percent in 2018-19. The components of revenue expenditure – general services, social services and economic



services reflect similar level of deviation as was witnessed at aggregate revenue expenditure level.

The Government planned to generate revenue surplus of Rs. 268.35 crores amounting to 0.94 percent of GSDP. But the year ended with deficit of Rs.1343.81 crores, which formed 4.14 percent of GSDP. While budget projected a fiscal deficit of Rs. 852.99 crores amounting to 3 percent of GSDP, the overrun was Rs.2081.18 crores, amounting to 6.4 percent of GSDP. As discussed earlier the government managed to finance the deficit utilizing cash investment in public accounts in addition to resorting to market borrowing. Thus, the impact of large fiscal deficit was limited on outstanding debt. The debt stock in 2019-20 exceeded the budget estimates by Rs. 286.60 crores.

The footprint of large decline in revenue receipts as compared to budget estimates is visible in spending plan of government taking both revenue and capital expenditure. Given uncertainties in flow of funds, the government needs to improve efficiency of budget management process to improve prioritization when faced with resource shortfall. The inability to spend the available funds, non-receipt of the entire central funds as budgeted, and late receipts central funds in some CSS programs are the major reasons for this shortfall. Some of the budget heads under capital expenditure indicate that budget estimates were based on several central grants, NEC projects, and NLCPR components of DONER. Under many of these projects, funds were not received during the year for which the actual expenditure fell short of the budget estimates. The predictability of availability fund has remained low. The deviation in capital expenditure is also closely related to non-receipt and delayed receipt of central grants resulting in large unspent amounts. The delay in implementing the projects in the infrastructure sector due to several inadequacies also stops the flow of funds.

Uncertainties created due to non-receipt of central transfers and late receipt of funds, which could not be utilized during the year, is another that needs to be addressed for better utilization budgeted resources. It becomes a challenge to utilize the resources, if large proportion of central transfers received during the last quarter of the fiscal year. In 2019-20, the unspent amount remains high at Rs.517.91 crores. The receipt of central funds in the last quarter was Rs.350.71 crores, which forms about 38 percent of total receipts (Table 4.4). Although, the government usually includes the unspent amount in the spending plan for the following year on the projects conceived in the budget year, the spending plan of the budget for the current year is not met.

**Table 4.4**  
**Central Funds Received during End of the Fiscal year and the Unspent Amount**

Scheme Name	Total Receipts	Receipts in March	Receipts during January to March	Unspent Balances
<b>2014-15</b>				
Plan Central Sector	1100.03	106.61	422.08	328.65
CSS	572.23	46.90	164.35	187.41
<b>Total</b>	<b>1672.26</b>	<b>153.51</b>	<b>586.43</b>	<b>516.06</b>
<b>2015-16</b>				
Plan Central Sector	314.81	6.49	140.51	158.74
CSS	536.14	72.87	150.58	47.67
<b>Total</b>	<b>850.95</b>	<b>79.36</b>	<b>291.09</b>	<b>206.41</b>
<b>2016-17</b>				
Plan Central Sector	247.07	20.57	56.23	397.52
CSS	642.11	89.52	140.69	170.34
<b>Total</b>	<b>889.18</b>	<b>110.09</b>	<b>196.92</b>	<b>564.86</b>
<b>2017-18</b>				
Plan Central Sector	328.47	88.02	108.05	383.35
CSS	1022.25	249.48	304.35	500.73
<b>Total</b>	<b>1350.72</b>	<b>337.50</b>	<b>412.40</b>	<b>884.08</b>
<b>2018-19</b>				
Plan Central Sector	481.06	110.09	179.69	202.18
CSS	1085.43	205.59	280.04	397.84
<b>Total</b>	<b>1566.49</b>	<b>315.68</b>	<b>459.73</b>	<b>600.02</b>
<b>2019-20</b>				
Plan Central Sector	307.73	22.46	90.99	141.02
CSS	616.47	101.76	259.72	376.89
<b>Total</b>	<b>924.20</b>	<b>124.22</b>	<b>350.71</b>	<b>517.91</b>

Projecting central grants for various programs in anticipation has resulted in biased view of resources. There is a need to take realistic perception of central program funds and prepare the budget accordingly. Otherwise, it will be construed as an overestimation of revenues to accommodate ever-increasing budget size. The state government has to address capacity constraint to undertake infrastructure building. Enhancing the capacity to conceptualize projects and implement them properly and removing ground level bottlenecks in the implementation process are important issues that needs to be addressed. The structural issues like acquiring land, improving coordination among departments, improving efficiency in project management should get attention. It is important for the State Government to improve coordination with the Central Government for better fund flow system to enable timely availability of funds for programs.

## 5. Concluding Remarks

The State government faced highly stressed situation in the fiscal year 2019-20. The revenue receipts declined by 18.91 percent over the previous year. The government managed to generate 34.55 percent less than what they budgeted for in the fiscal year. The central transfers taking both tax devolution and the grants together declined by 27.20 percent, which affected the aggregate revenue receipts. The State received 41.94 percent less than the budget projection in the case of central transfers. The own revenue of the State remained subdued in 2019-20. The loss of revenue to the state was not foreseen as could be seen from the budget estimates. The State breached the deficit target stipulated in the FRBM Act.

The decline in central transfers to the states was partly due to adjustment of tax devolution on account of lower collection of central taxes in 2018-19. Central government, acknowledging the fiscal problems of the states, provided the relief in the form of special onetime dispensation of higher borrowing in which Sikkim was allowed to borrow Rs. 216 crores. But the decline in central transfers as compared to budget estimates was much higher at Rs. 2295.22 crores. The GDP growth in the fiscal year also remained low at 4 percent which did not help the collection of higher central taxes. The grants to the state declined at a much higher rate of 44 percent in 2019-20 over the previous year and declined by Rs. 1621.26 crores as compared to the budget estimates. The projection of central transfers at such higher rate did not correspond to existing economic situation in the country.

The decline in revenue receipts had its impact on the level of spending of the state. While the state spent Rs. 944.01 crores less than the budget estimates in revenue expenditure, the capital outlay was less by Rs. 389.97 crores. These adjustments were significant. However, given the size of the revenue expenditure the impact of revenue shortfall was less. As percent to GSDP, it declined marginally from 19.51 percent in 2018-19 to 19.05 percent in 2019-20. The adjustment in capital outlay has been large as it declined from 4.99 percent to 2.27 percent.

Revenue expenditure proved to be rigid downward due to large share of committed spending like salary, interest payment and pension outgo. The salary and pension component increased in 2019-20 due to payments of arrears of Six Pay Commission. While revenue declined considerably, the government did not reduce the revenue expenditure commensurately, increasing revenue deficit which in turn increased fiscal deficit.

The spending adjustment, however, could not reduce the fiscal deficit, which increased to 6.4 percent in 2019-20. The state could increase the fiscal deficit to 3.5 percent based on the flexibility granted by the FC-XIV and increase the borrowing by Rs. 216 crores allowed by the central government. These two increments taken together brought the fiscal deficit to 4.26. But the fiscal deficit outturn exceeded the allowed fiscal deficit to a large extent.

While fiscal deficit increased to a high of 6.4 percent of GSDP, the state government resorted to utilizing cash investments in public accounts to finance the fiscal deficit in addition to borrowing instruments. The outstanding debt did not rise to the extent of increment in fiscal deficit. Earlier the central Finance Commissions and the CAG had advised the states to utilize cash balance instead of resorting to borrowing to finance fiscal deficit.

The fiscal imbalance heightened by resource problem presented several fiscal management issues that needs to be considered. Fiscal rules provide self-restraint to politicians and executive to observe fiscal discipline, which is foremost factor to improve allocative and operational efficiency in public finance. Expanding the spending programs and committing to new programs which have severe resource requirements at the time of uncertainties in resource flow, brings in fiscal imbalance. In response to Covid-19 pandemic and consequent pressure on resource generation, states were allowed to increase borrowing. According to the recommendations of FC-XIV, states have to come to the consolidation process gradually starting from 2021-22. Strengthening PFM system and adherence to amended FRBM Act targets will be important. The independent review of fiscal policy and FRBM Act is an excellent institutional framework within which reform measures can be assessed. The state government can widen the ambit of the independent review to include assessment of PFM reforms and their working along with compliance to FRBM Act provision.

In addition to fiscal targets, the Act calls upon the government to achieve a set of guiding fiscal principles. The principles include generating surplus in revenue account to create capital assets, raise non-tax revenue giving due regard to cost-recovery and equity, prioritize capital expenditure, and pursue expenditure policies that would provide impetus for economic growth, poverty reduction, and improvement in human welfare. Judging from the fiscal management in 2019-20, many of these principles remained challenging to observe.