Government of Sikkim

THE REVIEW OF COMPLIANCE TO SIKKIM FRBM ACT FOR THE YEAR 2017-18

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1. Introduction

This report provides an independent review of the fiscal stance and compliance to the provisions of the Fiscal Responsibility and Budget Management Act (FRBM Act) of Government of Sikkim for the fiscal year 2017-18. The State 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) with the expectation of providing 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 relating to fiscal adjustment path in the country. The Government usually includes these changes in the Act through amendments. 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 FRBM Act, in accordance with the recommendations of the Thirteenth Finance Commission (TFC), provides for independent review of the fiscal policy of the Government and the compliance to the provisions of this Act. This provision has established an institutional process where the achievement of the fiscal targets and fiscal management principles has been examined to strengthen accountability system. The major objective of the review is to improve the credibility of the fiscal policy and transparency of the fiscal management process of the Government. It helps in providing an unbiased assessment of Government's compliance with the provisions of the fiscal rules and reasons for any deviations. The National Institute of Public Finance and Policy (NIPFP), New Delhi, has been assigned the task of reviewing the compliance of the Act.

As the report is placed in the State legislature, it becomes part of the institutional accountability structure relating to public financial management. Review of fiscal policy intentions, achieved outcomes, and deviations from the plans leads to enhanced legislative and public awareness regarding fiscal management. The process of independent review and its follow up increase public faith on the Government announcements on fiscal policy, plans and outcomes. The fiscal rules in the form of FRBM Act have become cornerstone of public financial management and a review of Government's compliance to its provisions assumes significance in our democratic governance system.

2. Contours of the Review Report

The objectives of the review include examining the concurrence of the State Government to the fiscal targets set under the provisions of FRBM Act in terms of deficit and debt stock relative to the State GSDP, observance of desirable fiscal management principles, data and information disclosures, and transparency measures. Limiting the fiscal deficit at 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 state finances of Sikkim continue to face uncertainties relating to Central transfer of resources. Given limited resource base of the State and high dependence on central funds for provision of public services in a difficult hilly terrain, fiscal prudence and risk management becomes crucial. The budget management in terms of budget projection has to be unbiased to avoid discrepancies in flow of funds to programs. Any review of fiscal management and adherence to FRBM Act has to take these issues into consideration. The review report includes the following;

- The report includes analysis of the macroeconomic outlook over the years and particularly for 2017-18. The state GSDP is considered to be a close proxy for tax base, which gives an idea about the capacity of the government to raise revenue.

- Recent trends of public finance including revenue generation, expenditure framework, and the debt burden have been assessed.
- Assessment of the achievement of fiscal targets during 2017-18 as prescribed in the FRBM Act of the State.
- Evaluation of budget outturns during the year 2017-18 as against budget projections to examine capacity of the Government to implement its budget while achieving FRBM Targets.
- Assessment of Medium Term Fiscal Policy (MTFP) presented along with the budget.
- The report reviews desired fiscal management principles contained in the FRBM Act to achieve the fiscal targets and transparency measures.

Senior officials of Department of Finance provided an overall perspective of state fiscal management including revenue mobilization efforts and rationale behind resource allocations to different sectors for this study. Discussions with tax department and major spending departments on revenue and expenditure trends and priorities helped this study immensely.

The rest of the report is organized as follows. Section 3 provides an overall assessment of macroeconomic outlook and sector composition of GSDP. Section 4 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 5. Issues related to revenue mobilization and expenditure pattern for the year 2016-17 as compared to the budget provisions are analyzed in Section 6. Concluding observations are contained in Section 7.

3. Macroeconomic Outlook

The macroeconomic outlook of the State is analyzed here to get a perspective of contribution of various sectors to the State economy and possible revenue implication. This is crucial in the context of fiscal policy in general and budgeting in particular. Indeed, macroeconomic outlook in the sub-national fiscal policy does not reflect on the degree of price level stability, effects on trade and on the balance of payments. It assumes significance for internal revenue effort and benchmarking fiscal variables over the years. Further, borrowing limit of the state government is determined by the Central Government as a proportion to state GSDP. This is based on assumptions regarding the growth rate usually made by the Central Finance Commission. Composition of gross state value added (GSVA) and growth rate of GSDP at both current and constant prices have been given in Table 1 since 2011-12. This is based on new GSDP series.

Table 1

Composition of GSVA (Constant Prices)

(Percent)

Item	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Primary	**8.35**	**8.50**	**8.39**	**7.97**	**7.60**	**7.78**	**8.35**	**8.38**
Agriculture, forestry and fishing	8.28	8.42	8.30	7.88	7.50	7.70	8.27	8.30
Mining and quarrying	0.07	0.08	0.09	0.09	0.09	0.09	0.08	0.08
Secondary	**62.83**	**60.13**	**59.87**	**61.20**	**62.30**	**63.51**	**63.46**	**64.14**
Manufacturing	39.54	38.96	40.06	41.56	43.53	46.29	46.06	47.18
Construction	6.16	5.70	5.71	5.28	5.28	4.47	4.62	4.42
Electricity, gas, water supply & other utility services	17.13	15.47	14.10	14.36	13.49	12.75	12.78	12.54
Tertiary	**28.82**	**31.37**	**31.73**	**30.83**	**30.10**	**28.71**	**28.19**	**27.48**
Transport, storage, communication & services related to broadcasting	2.60	3.05	3.22	3.18	3.14	3.33	3.30	3.34
Trade, repair, hotels and restaurants	2.89	4.60	5.23	4.77	4.50	4.55	4.48	4.33
Financial services	1.52	1.56	1.57	1.55	2.71	1.66	1.55	1.51
Real estate, ownership of dwelling & professional services	5.36	5.38	5.31	4.98	4.59	4.46	4.28	4.07
Public administration	6.80	7.21	7.19	7.09	6.56	6.20	6.33	6.16
Other services	9.66	9.57	9.22	9.26	8.61	8.51	8.25	8.07
TOTAL GSVA at basic prices	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	
Growth Rate								
GSVA Constant Growth		1.74	5.15	8.08	9.09	6.16	6.96	7.05
GSDP Constant Growth		2.29	6.07	7.90	9.93	7.15	6.95	7.05
GSVA Current Growth		9.87	11.28	11.48	16.15	13.65	12.57	14.00
GSDP Current Growth		10.51	12.35	11.14	17.05	14.71	13.57	14.00

Source: CSO, GoI

The composition of the State economy shows that industry sector has been the largest component with an average share of about 62 percent during 2011-12 to 2017-18 (Table 1). This is followed by services sector with a share of 30 percent and agriculture and mining with 8 percent share. Among these the relative share of industry sector has shown a small rise over the years as it has increased by 0.63 percentage points during 2011-12 and 2017-18. While the relative share of agriculture has remained same, there was a decline in share of tertiary sector. The manufacturing of pharmaceutical products and commissioning of hydropower has contributed to the industry sector. The relative share of service sector, which was showing a growing trend in the State, has declined in recent years.

Growth rate of GSDP in Sikkim, which peaked in 2015-16 as per the new series, remained more or less stable since then. Growth rate of GSDP at constant prices has increased from 6.07 percent in 2013-14 to 9.93 percent in 2015-16, which was the highest until up to 2018-19. Starting from 2016-17 up to 2018-19, the GSDP growth rate at contest prices remained at an average rate of 7 percent. Sikkim recorded a growth rate of 13.57 percent for GSDP at current prices in 2017-18. In addition, the growth rate of GSVA was recorded at 6.96 per cent at constant prices and 12.57 per cent at current prices in 2017-18 (Table 1).Growth rate both at constant and current prices, show a drop in 2017-18 as compared to the previous year. The drop is little more in current prices.

The year on year growth rate of components of GSDP shows that there has been a decline in the case of industry sector from 8.22 percent in 2016-17 to 6.88 percent in 2017-18. The growth rate of services sector has improved from 1.23 to 5.02 percent during these two years. There has been a good growth for agriculture sector as it has increased from 8.80 to 14.74 percent. Decline in growth of industry sector is a matter of concern for revenue generation purpose.

4. Review of State Finances of Sikkim

Fiscal overview

State finances of Sikkim are heavily dependent on Central transfers. After the recommendations of the Fourteenth Finance Commission (FFC), 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. The FFC recommended increasing the tax devolution to a high of 42 percent of all the Central taxes and refrained from giving specific-purpose grants. The only grants awarded by the Commission were disaster relief grants and grants for local bodies. The Commission recommended for revenue deficit grant to some states after assessing their post-devolution revenue deficits.

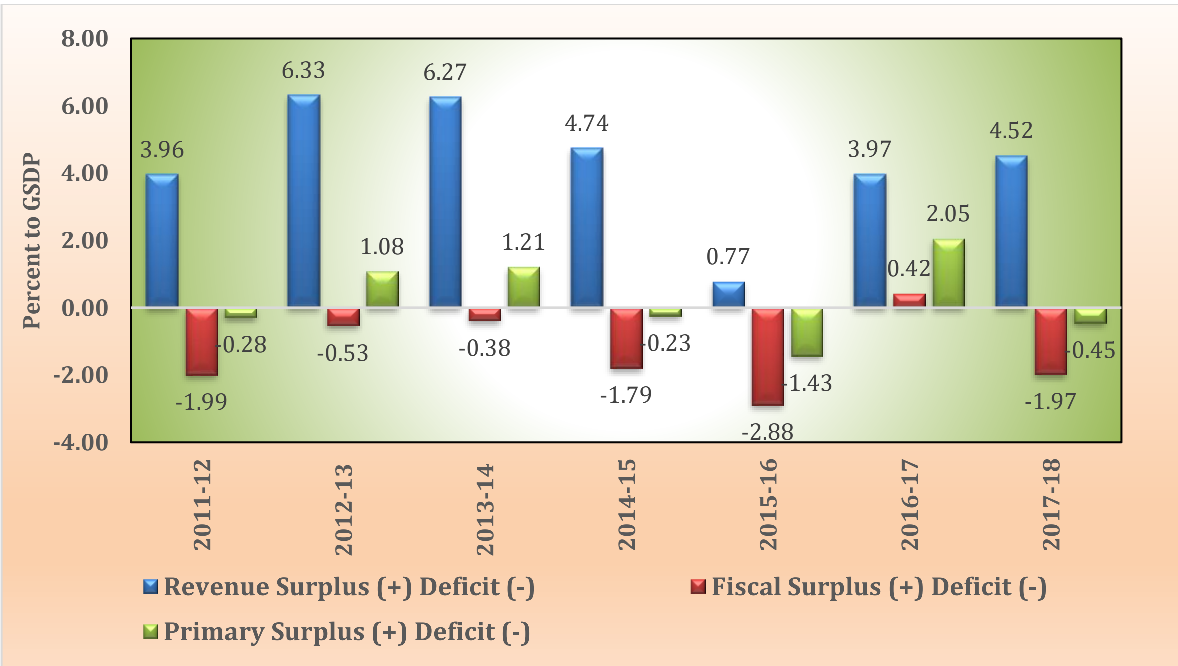
Following the recommendation of the FFC, the Central Government restructured plan grants to states in 2015-16 expecting reduction in net revenues available to it. Central Government subsumed Normal Central Assistance (NCA), Special Plan Assistance, Special Central Assistance in the FFC award and delinked 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.

Sikkim faced several challenges in fiscal management in 2015-16, due to changes in central transfer system. While the State received higher tax devolution, loss of plan grants created difficulties for ongoing projects. Overall impact of changes in transfer system was not favorable to the State. 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 FFC transfer was also designed based on a very unrealistic own tax projection for Sikkim.

Sikkim consistently achieves revenue surplus and this trend continued after the enactment of the FRBM Act as well. Revenue surplus is usual in state like Sikkim due to dominance of central transfers in the aggregate revenue. The State managed to contain fiscal deficit within the limits of the FRBM Act after its adoption. This is a positive development in fiscal management of the State. In 2016-17, the revenue surplus increased to 4.52 percent of GSDP, whereas the budget estimate of revenue surplus was 3.03 percent. This level of revenue surplus was quite large as compared to previous years. In 2017-18, Sikkim achieved fiscal deficit of 1.97 percent to GSDP, much below the allowed limit.(Figure 1).

High revenue surplus and consequent achievement of fiscal surplus in 2016-17 and limiting fiscal deficit below 2 percent in 2017-18 should not be overlooked, as the FRBM target of fiscal deficit was 3 percent of GSDP. As per the recommendations of the FFC, the State was entitled to take the fiscal deficit to 3.25 percent due to its prudent record of fiscal management. Enhanced level of revenue surplus and consequent lower fiscal deficit was mostly due to compression of revenue expenditure. The revenue expenditure declined from the level of 18.31 percent in 2016-17 to 17.67 percent in 2017-18. The compression in revenue expenditure helped the State to achieve a reasonably higher revenue surplus and enabled the Government to improve capital outlay. The capital outlay in Sikkim consistently remained large as percentage to the GSDP. This did not affect the fiscal deficit adversely due to having sizeable revenue surplus. The capital outlay has increased to 6.48 percent in 2017-18 over 3.56 percent achieved in 2016-17 as percentage to GSDP (Figure 2)

Figure 1
Fiscal Outcomes in Sikkim

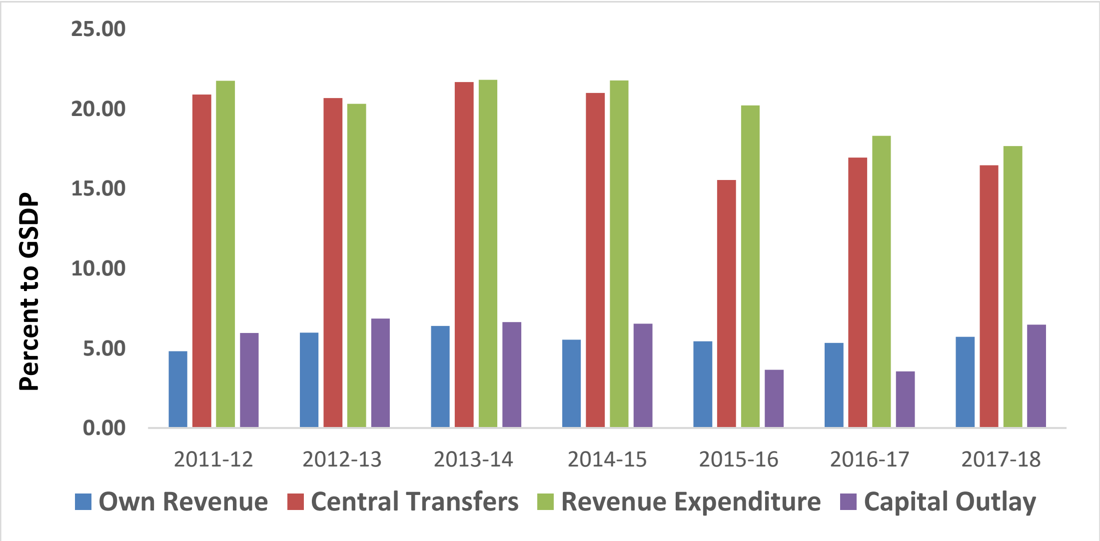


The unutilized fiscal space as is evident from fiscal outcomes for the year 2017-18needs introspection as the State achieved fiscal surplus in the previous year. Large revenue surplus in the State was due to high dependence on central transfers, all of which are usually booked under revenue receipts. 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. The availability of fiscal space in a year becomes favourable to the fiscal management as it helps increasing capital outlay. What is more important for the State is to improve efficiency to be able to utilize the unspent balances. The State Government needs to coordinate with the Central Government for better transfer mechanism and remove the hurdles in the implementation of programs.

The Revenue Side of the Budget in 2017-18

Sikkim witnessed large fall in revenue receipts relative to the GSDP after the recommendations of the FFC in 2015-16. There was a turnaround in revenue receipts in 2016-17. In 2017-18, the aggregate revenue receipts show a marginal decline to 22.19 percent relative to the GSDP from 22.29 percent achieved in the previous year. Although Own revenue receipts show a marginal rise in 2017-18as percentage to GSDP, mainly due to better performance of non-tax receipts, central transfer was not favorable. The trends in own revenue receipts, central transfers, revenue expenditures and capital outlay (on general, social and economic services together) are given in Figure 2.

Figure 2
Broad Fiscal trends in Sikkim



The increase in own revenue receipts from 5.34 percent in 2016-17 to 5.71 percent in 2017-18 relative to GSDP was small and was driven by rise in non-tax revenue. There has been a steady decline own tax revenue as percentage to GSDP in recent years and this was also evident in 2017-18 when it declined from 3.15 percent achieved in the previous to 2.93 percent of GSDP. The peak in the recent years was in 2013-14, when the own tax revenue was 3.79 percent to GSDP (Table 2). Central transfers, which constitutes about three-fourth of the aggregate revenue receipts suffered a decline from 16.95 percent to 16.47 percent of GSDP. It was mostly due to the decline in grants component. Rise in tax devolution from 10 percent to 11.21 percent could not compensate the loss in grants.

The own non-tax revenue reported a rise in 2017-18 as compared to 2016-17 as percentage to the GSDP. The non-tax revenue in Sikkim contains large contributions from lottery operations and sale of electricity as the State Government manages the power sector through a department. The income from lottery operations has declined due to adverse market conditions and unfavorable policies by other State Governments.

Trend of Individual State Taxes

The composition of own tax revenue for the year 2017-18 as percentage to GSDP contained in Table 2 shows that state taxes did not increase in the fiscal year. It was only sales tax and SGST taken together marginally increased to 1.79 percent over 1.76 percent achieved in the previous year. The fiscal year 2017-18 was the first year of implementation of goods and service tax. (GST) Because of the teething problems in the implementation process and decline in national growth rate, GST could not become a buoyant source of revenue for the states. Other individual taxes declined in 2017-18 as compared to the previous year relative to GSDP.

The buoyancy coefficients, reflecting the response of tax growth relative to the growth of state economy, for two periods are given in Table 3. The longer period buoyancy coefficients, from 2004-05 to 2007-08 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 VAT.

Table 2
Revenue Receipts in Sikkim

Percent to GSDP

Heads	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Own Revenues	**4.82**	**5.98**	**6.40**	**5.53**	**5.43**	**5.34**	**5.71**
Own Tax Revenues	**2.63**	**3.53**	**3.79**	**3.42**	**3.14**	**3.15**	**2.93**
Sales Tax	1.11	1.84	2.07	1.83	1.81	1.76	1.06
SGST	0.00	0.00	0.00	0.00	0.00	0.00	0.73
State Excise Duties	0.86	0.90	0.87	0.85	0.79	0.76	0.64
Motor Vehicle Tax	0.15	0.13	0.13	0.13	0.12	0.12	0.12
Stamp Duty and Registration Fees	0.07	0.04	0.05	0.04	0.05	0.06	0.06
Other Taxes	0.44	0.61	0.67	0.57	0.38	0.45	0.31
Own Non-Tax Revenues	**2.19**	**2.45**	**2.61**	**2.10**	**2.29**	**2.18**	**2.79**
Central Transfers	**20.91**	**20.67**	**21.69**	**21.01**	**15.55**	**16.95**	**16.47**
Tax Devolution	5.48	5.66	5.50	5.25	10.37	10.00	11.21
Grants	15.43	15.01	16.19	15.75	5.18	6.95	5.26

Source (Basic Data): Finance Accounts, State Budget 2019-20, and CSO

Tax bouncy estimated for more recent years from 2011-12 to 2017-18, shows an improvement as aggregate buoyancy coefficient has exceeded 1. This implies, the tax growth rate has overtaken the GSDP growth rate, albeit marginally. The buoyancy of sales tax has come out strongly, which 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
Buoyancy of State Taxes

	2004-05 to 2017-18	2011-12 to 2017-18
Own Tax Revenues	0.610	1.028
Sales Tax + SGST	0.740	1.416
State Excise Duties	0.653	0.660
Motor Vehicle Tax	0.736	0.833
Stamp Duty and Registration Fees	0.620	1.072
Other Taxes	1.175	0.393

Source (Basic Data): Finance Accounts and State Budget 2018-19

The Transfers from Centre

The central transfer to the State is large, which constitutes little more than three-fourths of the total revenues. High dependency on central funds implies distortions in the resource allocation in case there is any deviation from the budget estimates. The central transfer has increased from Rs. 2334 crore in 2011-12 to Rs. 3870.08 crore in 2017 - 18 in nominal terms. However, as percentage of GSDP, the Central transfer has decreased from about 20.9 percent to 16.5 percent during this period. In absolute terms, the amount of central transfers was reduced in 2015-16 as compared to the previous year due to closure of options of the plan transfers after the recommendations of the FFC. However, this has been reversed in 2016-17, as in absolute terms the State received higher transfers as compared to the year 2015-16.

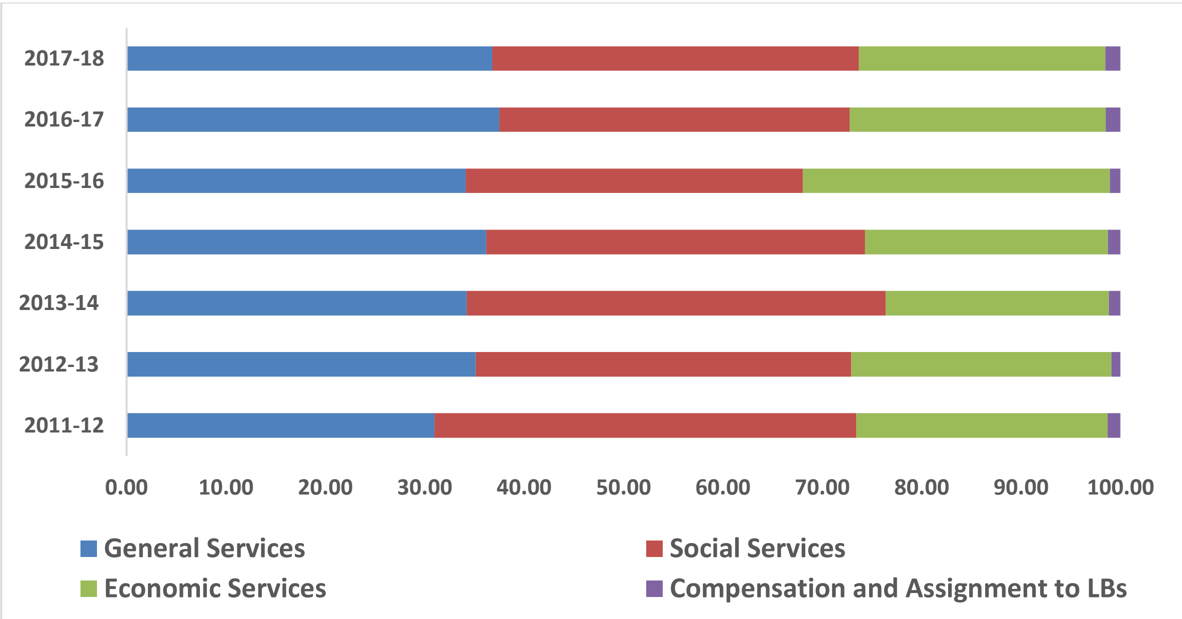
In 2015-16, following the 14th Finance Commission's recommendations the share in central taxes has more than doubled as compared to 2014-15, but grants from Centre has declined significantly in 2015-16. The share of grants from Centre to GSDP in 2015-16 came down to 5.18 percent, compared to 15.75 percent in 2014-15 and 16.19 percent in 2013-14. 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. Although in 2017-18 there has been rise in transfers in nominal terms, as percentage to GSDP there has not been any improvement as compared to the previous year. The year-on-year growth of components of central transfer shows that, while share in central taxes increased by 13.56 percent in 2017-18, the growth rate of grants declined by 14 percent. Including the share in CGST, the overall growth rate of central transfers in 2017-18 was 10.38 percent, which was lower than the growth rate of nominal GSDP. It was the decline in grants as percentage to GSDP that constrained the aggregate transfers, despite some improvement in tax devolution. The transfer dependency of the State has seen some decline as relative share of central transfers declined from 76.05 percent in 2016-17 to 74.24 percent in 2017-18.

Spending Pattern in Revenue and Capital Accounts

The annual average growth rate of revenue expenditure in Sikkim, during 2011-12 to 2017-18, was 11 percent. The revenue expenditure grew at the rate of 10 percent in 2017-18 over a very low growth of 3.9 in the previous year. This implies the Government has kept control over the growth rate of revenue expenditure, which helped in achieving higher revenue surplus. As percentage to the GSDP, the revenue expenditure declined by 0.64 percentage points from 18.31 in 2016-17 to 17.67 percent in 2017-18. .

Resource allocation to different sectors in the revenue account assumes significance as the public expenditure is dominated by the revenue expenditure. The composition of revenue expenditure, given in Figure 3, shows that the relative shares of social services dipped from 42.46 percent in 2011-12 to 37 percent in 2017-18. However, there has been an increase in the share between 2015-16 and 2017-18 by almost 4 percentage points. While, the average relative share directly productive economic service was about 26 percent in total revenue expenditure during 2011-12 to 2-17-18, its share declined to 24.77 percent in 2017-18 as against 25.78 percent in the previous year. The share of general service seems to have been growing in the State, as its share increased from 30.97 percent in 2011-12 to 36.81 percent in 2017-18. 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.

Figure 3
Composition of Revenue Expenditure in Sikkim



Composition of revenue expenditures can also be examined from the point of expenditures' view that is contractual, committed, and pre-determined in nature. 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 been increasing in total revenue expenditure. Its share has increased from 59.08 percent in 2011-12 to 63.24 percent in 2017-18 (Table 4). Spending and salary and wages drives the committed spending. This has shown increasing trend in last two years.

Table 4
Committed Revenue Expenditure in Total Revenue Expenditure

(Percent)

Committed Expenditure	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Interest Payment	7.85	7.93	7.31	7.14	7.19	8.56	8.72
Pension	7.15	8.98	8.62	9.92	11.04	11.79	12.17
Salaries and wages	44.08	37.09	44.65	36.83	37.25	44.36	42.35
Total	**59.08**	**54.00**	**60.58**	**53.89**	**55.48**	**64.71**	**63.24**

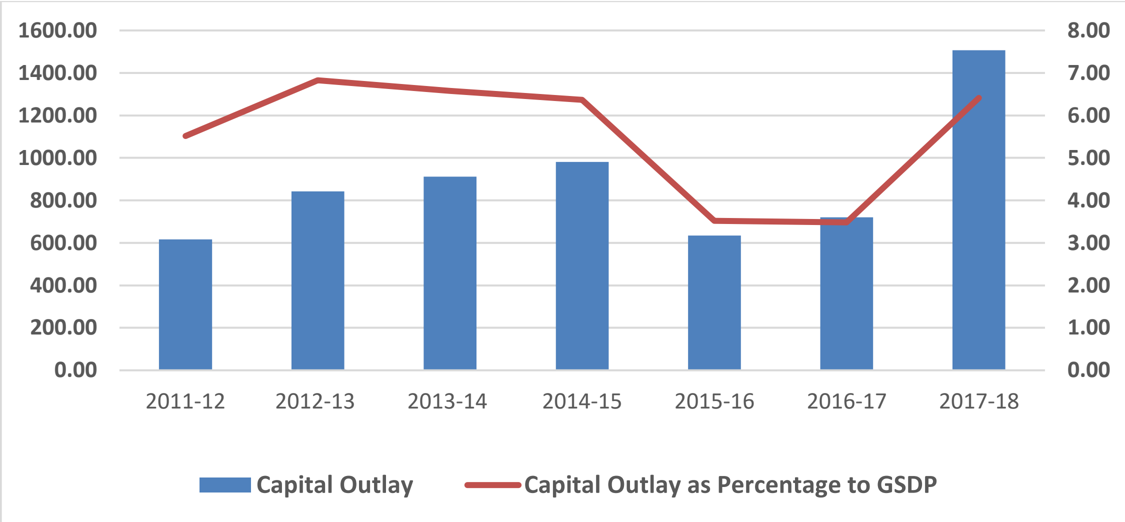
Source (Basic Data): Finance Accounts and State Budget 2019-20

Capital outlay, spending on social and economic infrastructure, quite often becomes residuary in the system depending upon availability of resources and other recurrent expenditure. While it remained reasonably high in the State as percentage to GSDP, stress on resources after the recommendations of FFC brought it down significantly. The capital outlay on various services (general, social, and economic) increased from Rs. 615.76 crores in 2011-12 to Rs. 980.71 crores in 2014-15 (Figure 4). However, in 2015-16, the capital outlay declined in nominal terms to Rs.633.98 crores. As percentage to GSDP, the capital outlay declined to 3.52 percent in 2015-16 from 6.37 percent in 2014-15 (net lending not included here). The decline in Central grants after the recommendations of the FFC played an important role in the resource allocation relating to capital investment. This implies the residual nature of capital outlay in the system. There was a marginal revival in 2016-17. In 2017-18, the capital outlay improved significantly to 6.41 percent of GSDP. In terms of nominal numbers, the capital outlay was Rs.720.29 crore in 2016-17, which increased to Rs.1506.78 crores in 2017-18. A onetime grant of Rs.500 crore received by the State in 2016-17 was actually allocated to capital outlay in this year, which improved the aggregate spending.

The size of the capital outlay in the State usually is related to the provisions made in the CSS and other Central programs through NEC and NLCPR schemes. The quantum of grants and committed spending on revenue account influenced capital outlay. 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. 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. It contributes to growth more directly. The State government should finance identified public investments with high social returns.

Figure 4
Capital outlay in Sikkim



Aggregate Spending Pattern

The aggregate sector expenditure, taking both the capital and revenue expenditure, gives overarching 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 96 percent during 2011-12 to 2017-18(Table 5). The relative share of debt repayment and loans and advanced was 3.28 and 0.54 percent respectively during the same period. The relative share of debt repayment has been showing an increasing trend from 1.55 percent in 2011-12 to 5.70 percent in 2017-18.

Table 5
Composition of Total Expenditure

Heads	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Total Expenditure net of debt repayment	96.89	97.78	97.55	97.45	95.04	94.48	94.02
Public Debt	1.55	2.08	2.20	1.96	4.36	5.16	5.70
Loans and Advances	1.56	0.15	0.25	0.60	0.60	0.36	0.28

Table 6
Composition of Total Expenditure (Net of Debt Repayment)

Percent

Heads	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Interest Payment	6.27	5.94	5.62	5.52	6.13	7.20	6.41
Pension	5.71	6.72	6.62	7.68	9.40	9.90	8.93
Administrative Services	9.20	9.87	10.07	8.84	9.59	10.01	8.26
General Services (Rev. Exp.)	3.53	3.77	3.98	5.95	3.95	4.40	3.43
Compensation to Local Bodies	1.03	0.68	0.90	0.96	0.91	1.23	1.12
Capital Outlay on Police	0.19	0.21	0.38	0.47	0.12	0.15	0.12
Capital Outlay on Public works	0.64	2.28	3.93	2.06	1.38	1.43	2.45
Education Sports Art and culture	18.14	17.63	17.67	17.53	18.49	18.08	16.65
Medical and Public Health	6.95	6.78	6.05	5.64	5.68	5.86	7.88
Water Supply Sanitation Housing and Urban Development	6.24	8.12	8.73	8.75	4.89	6.28	7.61
Welfare of Scheduled Castes Scheduled Tribes and other Backward Classes	0.67	0.62	0.71	0.66	0.81	0.79	0.86
Social Welfare and Nutrition	9.62	2.31	4.21	2.21	2.86	2.32	2.20
Other Social Services (Total Exp.)	1.36	1.52	1.81	0.94	0.85	1.68	1.36
Agriculture and Allied Services	7.90	6.64	6.30	6.74	7.38	6.15	5.55
Rural Development	3.83	3.86	2.86	4.21	3.40	5.46	3.33
Irrigation and Flood Control	1.41	1.86	1.50	0.52	0.82	0.68	0.80
Energy	4.45	4.51	3.55	3.91	5.94	6.02	5.06
Industry and Minerals	1.60	0.88	0.86	1.08	0.78	0.74	1.27
Transport	7.88	12.63	10.75	8.82	7.83	8.85	14.31
Science and Environment	0.09	0.06	0.06	0.07	-0.31	0.10	0.09
General Economic Services	2.68	2.56	2.32	6.90	8.51	1.98	1.86
Other Economic Services	0.60	0.55	1.12	0.55	0.59	0.69	0.45

Source (Basic Data): Finance Accounts and State Budget 2019-20

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 6). These three spending heads taken together constituted 23.60 percent of total expenditure in 2017-18. 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.

Debt Burden of the State

The indebtedness of the Government of Sikkim, which was showing some decline since 2011-12, has started increasing in 2016-17 (Table 7).Taking all types of liabilities, the total debt stock decreased from 22.86 percent of GSDP in 2011-12 to 21.97 percent in 2015-16. However, in 2017-18 it stands at 24.50 percent in 2017-18. Increase in internal debt of the Government was one of the factors for this rise. The FRBM Act of the state stipulated specific debt GSDP ratios until 2014-15 as per the recommendations of the 13th Finance Commission. The 14th FC, while not specifying debt-GSDP targets in its fiscal consolidation recommendations, held that the States could increase their fiscal deficit limit by a total of 0.5 percent based on certain conditions relating prudency. The debt GSDP ratio of 25 percent was one of the conditions. The aggregate level of indebtedness in 2017-18 indicates that the State Government complied with the TFC recommendations and its own FRBM targets.

Table 7
Liabilities of the Government of Sikkim

(Percent of GSDP)

	2011-12	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
Public Debt	**16.59**	**16.03**	**15.77**	**16.29**	**16.47**	**17.51**	**18.95**
Internal Debt	15.18	14.82	14.85	15.51	15.83	16.96	18.49
Loans from the Central Govt.	1.41	1.21	0.92	0.79	0.63	0.55	0.46
Other Liabilities	**6.27**	**6.32**	**6.37**	**6.30**	**5.50**	**5.82**	**5.55**
Small savings, Provident Fund	5.18	5.06	4.95	4.61	4.15	4.15	4.10
Reserve Fund	0.17	0.11	0.37	0.80	0.47	0.47	0.26
Deposits	0.93	1.16	1.05	0.90	0.89	1.20	1.19
Total Public Debt & Other Liabilities	**22.86**	**22.35**	**22.14**	**22.60**	**21.97**	**23.33**	**24.50**

Source (Basic Data): Finance Accounts, Relevant Years.

5. Compliance to FRBM Act Targets

5.1 FRBM Targets and Fiscal Achievements of the State Government

The major milestones in fiscal consolidation process include maintaining balance in revenue account, limiting fiscal deficit to fiscal rules targets and prudent debt management. The FRBM Act of the State, with amendments in 2011, 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 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 2017-18 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 2017-18. The MTFP is 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 details 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.

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 31stMarch 2014 and adhere to it thereafter;
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.

The FRBM Act of the State was supposed to take recommendations of the FFC, if any, to revise its debt-GSDP targets. The FFC, 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 FFC, 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 then in the amendments in 2016. 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.

As discussed in an earlier section, the State managed to generate larger revenue surplus in 2017-18 as compared to previous year as percentage to GSDP due to reduction in growth of revenue expenditure. Aggregate revenue receipt declined as percentage to GSDP in 2017-18 due to lower receipt of Central transfers and own revenue. However, due to compression of revenue expenditure, the State achieved revenue surplus and improved spending on capital outlay.

The aggregate revenue receipts, as percentage to the GSDP in 2017-18 was 22.19 percent, as compared to 22.29 percent in 2016-17. The revenue expenditure at 17.67 percent in 2017-18 was lower by 0.64 percentage points as compared to the previous year. The capital outlays increases significantly by 2.93 percentage points in 2017-18 as compared to the previous year. The onetime grant of Rs.500 crore received by the State Government in 2016-17, was mostly utilized for capital outlay in 2017-18. Fiscal outcomes for 2017-18 indicate that the State remained within the FRBM Act fiscal targets.

The State could have expanded its spending program in view of its eligibility to increase the fiscal deficit target and resultant availability of fiscal space. The rationale behind limiting the fiscal deficit below 2 percent of GSDP was not clear. While limiting growth of revenue expenditure and raising capital outlay conveys positive fiscal management principles, there is a need to improve capacity to implement programs and conceive socially productive projects..

The fiscal targets specified in the FRBM Act and the outcomes for the year 2017-18are shown in Table 8. Against the Act requirement of maintaining balance in the revenue account, and limiting the fiscal deficit to 3 percent of the GSDP, the State Government achieved a revenue surplus of 4.52 and incurred a fiscal deficit of 1.97 percent of GSDP. In nominal terms, the amount of revenue surplus increased to Rs. 1060.95 crore in 2017 -18 from Rs. 822.22 crores in 2016-17. As eluded above lower fiscal deficit indicates that the State Government had flexibility to expand its expenditure program.

Outstanding debt burden, an outcome of the fiscal management the State, at 23.20 percent relative to the GSDP remained within broadly accepted debt-GSDP ratio specified by the FFC at 25 percent. The other fiscal target, outstanding guarantees, remained within the specified limit of Sikkim Ceiling on Government Guarantee Act 2000. The fiscal outcomes for the year 2017-18 indicate that the State complied with the fiscal targets stipulated in the FRBM Act.

Table 8
FRBM Act Targets and Fiscal Achievements during 2017-18

Percent

	Targets	Achievements
Revenue Deficit % of GSDP	0	-4.52
Fiscal Deficit % of GSDP	3.00	-1.97
Total Debt Stock % of GSDP	25	23.20
Outstanding Guarantees	Restricted to the limit under the Sikkim Ceiling on Government Guarantees Act, 2000	

Note: Negative sign for deficit figures indicate surplus

5.2 Fiscal Management Principles

The State FRBM Act includes guiding fiscal management principles that call on the Government to maintain prudent debt level, manage guarantees, ensure borrowings to be used for productive purposes, and pursue revenue expenditure policies to provide impetus to economic growth are unique features of sub-national fiscal rules in India. The Act does not fix any targets or give any indicator to assess these principles like those for mandatory fiscal targets. The objective of giving a set of fiscal management principles is to inculcate accountability to achieve the statutory targets. In many ways these are inherent to the economic policy making of governments at any level and 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.

Prudent Debt Management

The debt management principles of the FRBM Act require the State Government to borrow responsibly to maintain debt at a prudent level, manage guarantees and other contingent liabilities within stipulated limits, and use borrowed funds for productive purposes to create capital assets. It is akin to the golden principle of not using borrowed resources for financing recurrent expenditure. Indeed, the 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. The debt stock as percentage of GSDP at 23.20 percent in 2017-18 satisfies the test of prudency as suggested by the 14th FC.

State Governments in India are not free so far as their own borrowing powers are concerned. States need Centre's consent in order to borrow in case the state is indebted to the Centre over a previous loan following Article 293(3). In practice Central Government fixes the limit for State Government borrowing. This limit acts as an external control in rule based fiscal management. Since the recommendations of the 13th FC, 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. The accumulated debt stock continued to decline, as the growth of the nominal GSDP has remained high in Sikkim. Although there has been some increment in debt GSDP ratio since 2016-17, it has remained within the FFC prescribed limits.

Borrowing and repayment for the year 2017-18 shown in Table 9 reveals that actual public debt that includes internal debt (market and institutional borrowing) and loans from Central Government was more than the budget estimates. At the same time actual repayment of loans was less than what was planned in the budget. As the Government borrowed more than what was budgeted and repayment was less, overall debt-GSDP ratio increased in fiscal year 2017-18. Achievement of higher revenue surplus helped reducing the fiscal deficit below 2 percent of GSDP.

Table 9
Borrowings and Repayments: 2017-18

(Rs. Crore)

	Budget Estimates	Actual	Difference
Public Debt Receipts			
Internal Debt	881.53	1050.93	169.40
Loans Advances from Central Government	0.07	2.54	2.46
Public Debt	**881.60**	**1053.46**	**171.86**
Small Savings and Provident Fund	**355.5**	**309.66**	**-45.84**
Total	**1237.10**	**1363.12**	**126.02**
Debt Repayments			
Internal Debt	317.49	332.49	15.00
Loans Advances from Central Government	10.21	10.13	-0.07
Public Debt	**327.70**	**342.63**	**14.93**
Small Savings and Provident Fund	**342.4**	**229.09**	**-113.31**
Total	**670.10**	**571.71**	**-98.38**

Source: Finance Accounts and Budget Document for the year 2017-18 & 2019-20

The FRBM Act calls upon to follow the "Golden Rule" of government spending which implies that a government should only increase borrowing in order to invest in projects that will pay off in the future. Under the Rule, existing obligations and expenditures are to be financed through taxation, and not issuing new sovereign. Given the high revenue surplus, this target has been satisfied. The capital outlay in Sikkim has remained reasonably high due to tied nature of the plan grants coming to the State. High revenue surplus has provided fiscal space to the Government to increase the capital outlay and keep the debt burden sustainable.

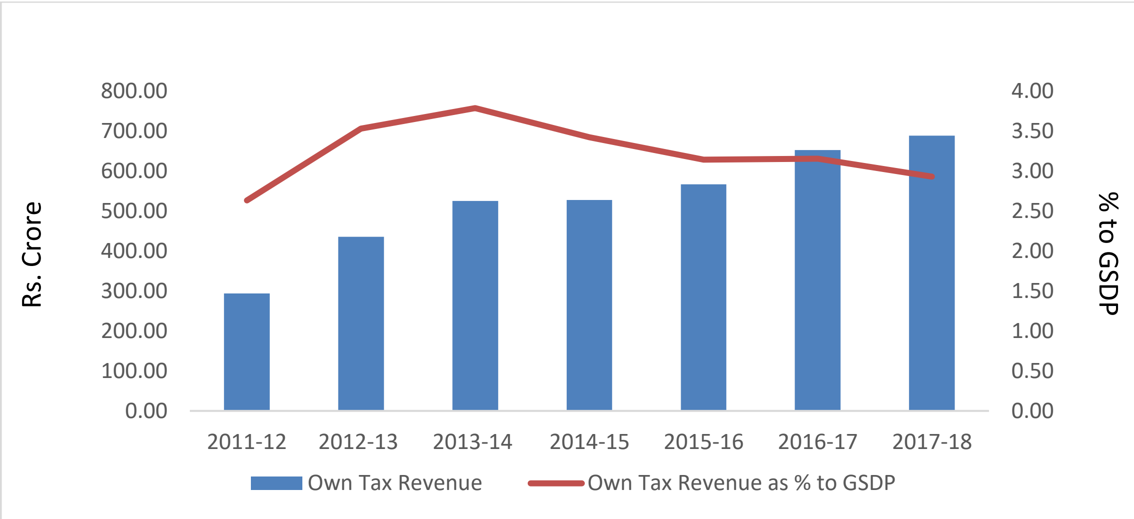
Simplifying Tax Policy and Administration

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 constitutes about 13 percent of total revenue receipts of Sikkim. Although, own tax receipt has not emerged as driving force of the resource envelopes, it has not been a volatile source of income (Figure 5). 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 2005had stabilized in terms of rate and base structure in the State, the newly introduced GST in 2017-18 continues to face teething problems. The State Government has made efforts to modernize the tax administration and introduced electronic payment taxes, e-filing of returns and generation of Waybills and statutory forms on electronic mode.

Cost recovery and equity has been the core themes in the case of non-tax revenues according the fiscal management principles enunciated in FRBM Act. Non-tax revenue of the State on an average contributes about 9 to 10 percent to the aggregate revenue receipt. As percentage of GSDP, it has shown an increasing trend in 2017-18. 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. In the year 2016-17, interest receipts, power sector, transport and forestry sector provided higher income to the State. 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.

Figure 5
Own Tax Revenue as Percentage of GSDP



Expenditure Policy and Institutional Measures to Improve Quality of Expenditure

The FRBM Act underlines the importance of spending pattern of the State Government providing impetus to economic growth, poverty reduction, and improvement in human development. 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.

The relative expenditure shares of different sectors have been analyzed in an earlier section that reflects emerging priority 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. Although a longer term trend is pertinent, increased capital outlay in 2017-18 cannot overlooked. 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.3, 59,807 in 2017-18 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, the 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.

6. Budget Credibility: Projections and Outturns

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, underestimating the revenue results in utilization of excess funds without proper planning and going through established accountability framework. The fiscal management principles, enshrined in the FRBM Act, require that the budget should be formulated in a realistic manner to minimize the deviations from the projections. As Sikkim depends considerably on the central transfers, realizing the estimated resource depends upon the actual flow of grants.

There are procedures to adjust the budget through supplementary demands to take care of exigencies and to use surplus funds from other programs. However, the budget adjustment through supplementary demands should not be too large to reduce the sanctity of the budget. In this section, a comparison between budget estimates and outturns of revenue receipts and expenditure for the year 2017-18 is provided in Table 10to 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. In nominal terms aggregate revenue receipt in 2017-18 was higher by Rs.602.5 crores as compared to the previous year. When compared to the budget estimates of 2017-18, the actual receipts was less by Rs.113.52 crores, which amounts to 2.13 percentage points (Table 10). This amount of deviation is small and according Public Expenditure and Financial accountability (PEFA) framework, deviation below 3 percent gets a top ranking implying good performance.

Looking at State Government's performance in internal revenue generation, the actual receipts exceeded the budget estimates by Rs.246.74 crores. While own tax revenue outturn exceeded the budget estimate by 2.81 percentage points, the non-tax revenue exceeded considerably by 53.45 percent. Generating more revenue as compared to the budget target would be considered favorable to the Government. As we have discussed earlier, underestimating the revenue potential does not bode well for taking resource allocation decisions.

The aggregate central transfers fell short of the budget estimates by about Rs.360 cores in 2017-18, which constituted 8.52 percent of budget estimates. While tax devolution to the State surpassed what was budgeted by Rs.157 crores or 6.33 percent of the budget estimates, there was a large shortfall in grants from Centre. Taking all kind of grants, the actual receipt was less by Rs.517 crore from the budget estimates, which forms about 30 percent of the budget estimates. The budget projection in the case of both tax devolution and grants has been way of the mark. Preparation of budget based on anticipated central component for various schemes did not materialize entirely.

Table 10
Budget Estimates and Outturns for the year 2017-18

(Rs. Crore)

	2016-17	2017-18	2017-18 (BE)	Difference (Actual to BE – 2017-18)	Difference in % to BE
Revenues	**4610.30**	**5212.79**	**5326.31**	**-113.52**	**-2.13**
Own Tax Revenues	**652.56**	**688.33**	**669.51**	**18.82**	**2.81**
Own Non-Tax Revenues	**451.64**	**654.38**	**426.46**	**227.92**	**53.45**
Central Transfers	**3506.10**	**3870.08**	**4230.34**	**-360.26**	**-8.52**
Tax Devolution	2069.19	2634.66	2477.78	156.88	6.33
Grants	1436.91	1235.42	1752.56	-517.14	-29.51
Revenue Expenditure	**3788.08**	**4151.85**	**4613.48**	**-461.63**	**-10.01**
General Services	1420.77	1528.13	1650.67	-122.55	-7.42
Social Services	1335.07	1532.15	1544.28	-12.13	-0.79
Economic Services	976.60	1028.25	1352.04	-323.79	-23.95
Compensation and Assignment to LBs	55.63	63.32	66.49	-3.17	-4.76
Capital Expenditure	**735.92**	**1522.82**	**1279.85**	**242.97**	**18.98**
Capital Outlay	720.29	1506.78	1263.60	243.18	19.25
Net Lending	15.63	16.04	16.25	-0.21	-1.31
Revenue Deficit	**-822.22**	**-1060.95**	**-712.84**		
Fiscal Deficit	**-86.30**	**461.87**	**567.01**		
Primary Deficit	**-410.70**	**99.70**	**197.35**		
Outstanding Debt	**4671.19**	**5451.04**	**5042.62**		

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

The spending outturns for the year 2017-18 shows that, there has been a large contraction in revenue expenditure to the tune of 10 percent and considerably higher spending in capital outlay by about 19 percent, as compared to budget estimates. While, the deviation in aggregate revenue was small, the changes in actual spending pattern seems to be the interplay of many factors. In revenue expenditure, the spending on social services remained close to the budget projections. While general services fell short of 7.42 percent, the contraction in economic services was of the order of 24 percent of the budget estimates. The compression of the revenue expenditure resulted in generating larger surplus in the revenue account as compared to budget estimates (Table 10). Larger capital expenditure as compared to budget estimates has not affected the fiscal deficit as it remained below 2 percent. Expansion of capital outlay beyond the budget estimates could be partly explained by the onetime grants received in the previous year was available for capital outlay this year.

While, the Government planned to generate revenue surplus of Rs.712 crores amounting to 3.03 percent of GSDP, the actual surplus was much higher at Rs.1061 crores, which was 4.52 percent of GSDP. While budget projected a fiscal deficit of 2.42 percent of GSDP, in reality it ended up with a 1.97 percent fiscal deficit. The debt stock exceeded the budget estimates by Rs.408 crores.

The comparison of the budget outcomes and estimates reveal several issues pertaining to expenditure management and budget projections. While the State Government managed to improve upon its own revenue receipts, projected in the budget, the decline in central transfers, particularly the grants, pulled down the aggregate resources by about 2.13percent as compared to the budget estimates. The fiscal year 2017-18was the third year of a changed fiscal transfer system in which tax devolution was raised and the plan grants were considerably curtailed. The tax devolution being a formulaic transfer, the difference in budget estimates and actual receipts was less.

Although the difference in actual and budget estimates in revenue and capital outlay was not planned to generate higher surplus and low fiscal deficit, the inadequacies in budget management practices seems visible. In addition to non-receipt of grants creates problems for project implementation, the process of execution, release of state’s share, and structural hurdles also affects the actual spending. While the deviation in general services in revenue expenditure could be considered as economy move to control revenue expenditure growth, large deviation in economic services hampers the service delivery and prospects of future projects as this sector is considered as a productive government sector.

Table 11
Non-receipt of Central Funds

Head	Unreleased Grant	Amount (Rs. In crore)
2702-MINOR IRRIGATION	Surface Water-Division Schemes	95.92
2401-CROP HUSBANDRY	National Mission on Sustainable Agriculture	60.00
2505-RURAL EMPLOYMENT	National Rural Employment Guarantee Scheme	48.51
2202-General Education	National Education Mission	43.48
2702-MINOR IRRIGATION	Pradhan Mantri Krishi Sinchai Yojana-Har Khet do Pani	37
4215-CAPITAL OUTLAY ON WATER SUPPLY AND SANITATION	Drainage and Sewerage system in South District	36.17
4801-Power	Schemes under Non-Lapsable Pool of Central Resources (NLCPR)	31.54
5452-CAPITAL OUTLAY ON TOURISM	Tourist Centre-Other Development Projects	28.54
4217-CAPITAL OUTLAY ON URBAN DEVELOPMENT	ADP Project (EAP)	20.80
4801-Power	Schemes under North Eastern Council (NEC)	18.35
2401-CROP HUSBANDRY	National Horticultural Mission	17.60
4215-CAPITAL OUTLAY ON WATER SUPPLY AND SANITATION	Water Supply Scheme for South District	15.83
4801-Power	Schemes under Ministry of New and Renewable Energy (100%CSS)	14.76
2852-INDUSTRIES	National E-Governance Action Plan (NeGAP)	14.48
2435-OTHER AGRICULTURAL PROGRAMMES	Agriculture Department	12.50
2235-SOCIAL SECURITY AND WELFARE	I.C.D.S. Programme	12.69
2070-OTHER ADMINISTRATIVE SERVICES	Skill Development Mission	10.34
2435-OTHER AGRICULTURAL PROGRAMMES	National Food Security Mission (NFSM)	10.10
4217-CAPITAL OUTLAY ON URBAN DEVELOPMENT	Projects/Schemes for the benefit of N.E. Region and Sikkim (Central Share)	10.05

The components of revenue and capital expenditure show deviations in terms falling short of or at some places exceeding the budget estimates. The appropriation account gives details of department wise savings and exceeds spending. Some of the budget heads are given here in Table 11 to illustrate the problems existing in implementing the programs.

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. There are instances, where the State Government failed to provide the State's share in several CSS projects for which, the next installments of central funds were not received. Given the requirement of infrastructure building in hilly State like Sikkim, better coordination to avail the full benefit of the central funds is necessary. 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.

Providing utilization certificate in timely manner, minimizing the layers of authorities involved in clearing the project proposals, and effectively utilizing the contractors (cooperative societies at grassroots level) should be crucial factors in implementing the projects. Issues like delay in clearance for acquiring forestland, delay in starting of the work, delay in utilization of previous installment, non-receipt of State's share and non-receipt of central grants and NEC grants are some of important factors that need to be addressed. Land acquisition is another issue that continues to bedevil the departments building infrastructure projects. Further, overarching principles involving investment management system that includes selection of projects, estimating cost, planning and budgeting, monitoring and control system should be improved for better utilization of public resources and achievement of the stated objectives.

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. The non-receipt of central transfers is the difference between what was budgeted and what was actually received from the Central Government. The non-receipts of central funds for various programs is detailed in Table 10 that includes CSS, NEC, NLCPR, NABARD and so on. There could be two major reasons for non-receipt of funds budgeted for the fiscal year. First, the inability of putting State's share in central programs stops the release of the second installment of already agreed upon fund flows. The second is the anticipated projection of flow of funds that was not materialized.

Table 12

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
2011-12				
Plan Central Sector	1198.52	45.46	466.35	143.58
CSS	165.07	14.94	48.60	71.43
Total	**1363.59**	**60.40**	**514.95**	**215.01**
2012-13				
Plan Central Sector	1362.22	112.86	441.36	273.36
CSS	191.49	8.44	38.53	68.96
Total	**1553.71**	**121.30**	**479.89**	**342.32**
2013-14				
Plan Central Sector	1863.27	197.74	412.74	262.33
CSS	235.75	59.99	71.42	190.31
Total	**2099.02**	**257.73**	**484.16**	**452.64**
2014-15				
Plan Central Sector	1100.03	106.61	422.08	328.65
CSS	572.23	46.90	164.35	187.41
Total	**1672.26**	**153.51**	**586.43**	**516.06**
2015-16				
Plan Central Sector	314.81	6.49	140.51	158.74
CSS	536.14	72.87	150.58	47.67
Total	**850.95**	**79.36**	**291.09**	**206.41**
2016-17				
Plan Central Sector	247.07	20.57	56.23	397.52
CSS	642.11	89.52	140.69	170.34
Total	**889.18**	**110.09**	**196.92**	**564.86**
2017-18				
Plan Central Sector	328.47	88.02	108.05	383.35
CSS	1022.25	249.48	304.35	500.73
Total	**1350.72**	**337.50**	**412.40**	**884.08**

The funds received during the last quarter of the fiscal year could not be put to use and large part of it remains as unspent amount. In 2017-18, while the unspent amount remains high at Rs.884.08 crores, the element of delayed receipt in it was Rs.412.40 crores. While this amount varied over the years, the amount received late in 2017-18 was quite large and higher than previous two years (Table 12). The large part of unspent amount from the central grants was spread over all through the year due to variety of reasons. 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.

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.

7. Concluding Remarks

State finances of Sikkim for the fiscal year 2017-18 shows that the fiscal management taking in to consideration the available revenue receipts from various sources and spending priorities, the fiscal outturns complied to the provisions of FRBM Act. While the State Government managed to improve on own revenue efforts, predominance of Central transfer became major driving force as it declined relative to state GSDP. The aggregate revenue receipts remained lower than the previous year as percentage to GSDP. The State Government effectively controlled the growth revenue expenditure resulting in large revenue surplus. This has helped limiting the fiscal deficit below the FRBM Act limits and facilitated higher capital outlay. The continuing rise in capital outlay as percentage to the GSDP after massive decline in 2015-16, could be construed as positive outcome in state fiscal management. The debt burden in 2017-18 was below the benchmark set by the 14th FC. Overall, with large revenue surplus, low fiscal deficit, and prudent debt management, Sikkim complied with the FRBM Act requirements.

The challenges posed by the recommendations of the 14th FC and consequent changes in fiscal transfer system continued to affect the State finances. Sikkim is one of the few States, which did not gain from the change of the fiscal architecture. The gain in the tax devolution following the recommendations of the 14thFC, could not manage to compensate for the loss of plan grants. This was again became visible in 2017-18 when aggregate transfers declined as compared to previous year relative to GSDP. While tax devolution showed a growth rate of 13.56 percent, the grants declined by 14 percent. In addition to declining growth of grants from center, there were several uncertainties in fund flows to the programs. While the 14th FC expected that, the higher tax devolution would provide more flexibility to the State to manage its spending pattern, overall decline in Central transfers due to reduction in grants put the State in difficulty.

Although, the Central transfers to Sikkim did not rise following 14th FC recommendations and there was a decline in Central grants. The State, however, did not face fiscal stress since 2015-16 due to control over spending. In the first year of 14th FC award, i.e., 20151-6, the State Government reduced government expenditure and the decline in capital outlay was considerable. Following a one time performance grant in 2016-17, the revenue surplus increased in 2016-17. The fiscal year 2017-18 was also not a stressed year as the state managed to generate revenue surplus and limited the fiscal deficit.

Large amount of unspent amount helps State Government to generate revenue surplus. The money received at the end of financial year could not be put to use. Generating large revenue surplus and Low fiscal deficit implies availability of fiscal space. The State Government needs to address the issue of how best to utilize the fiscal space and continue to adhere to fiscal deficit targets. As the Government is allowed to increase the fiscal deficit beyond 3 percent of GSDP, it is crucial to remove the hindrances for better utilization of available resources.

Budget credibility analysis by comparing actual fiscal outcomes with the budget projections for the fiscal year 2017-18 explains the fiscal outcomes. While the State remained close to the revenue targets set in the budget, it missed the revenue expenditure target considerably and exceeded the capital outlay targets significantly. A credible budget assumes significance to improve service delivery and trust of the people on the governance system. The State needs to address the existing problems in the budget forecasting and implementing the programs. Best use of available public resources as per the agreed upon plan would reduce fiscal risks in the future years. In this context improving program management, building efficient information base, enhancing the capacity of the staff, and coordination with the Central Government are some of the essential features needed to establish robust public financial management process in the State.