1. The existence of black or parallel economy has serious implications for government finances. Do you agree? Substantiate.

Introduction

Parallel economy, is based on the unaccounted money of the people and is also know as the ‘Black Money’. An alternative term for it is ‘Black economy’. It is a great menace to the Indian economy. Black money is nothing but money generated in transactions which are hidden from Government in order to avoid tax. This is usually done in cash because cash transactions do not reveal the identity of the person carrying out the transaction. It’s elimination will help the society in more than one way.

Body

The following are some of the implications parallel economy on government

- A large underground economy and growth of black income lead to under-estimation of the true size and incorrect picture of the economy by the officially complied national income data.
- Black money is largely attributed to tax evasion. Its direct impact is the loss of the Government revenue. Since the Government fails to get sufficient tax revenue due to large-scale tax evasion, it is forced to resort to high taxation and deficit financing which again carry their ill-economic effects.
- When the Government resorts to progressive direct taxation to maintain equity in the distribution of the tax burden, the tax evasion and growth of black money affect the very concept of social justice by not allowing the desirable reduction in inequalities of incomes. Again, when underground activities like smuggling etc. could not be taxed, the Government will impose higher taxes on officially sanctioned activities.
- Growth of the black economy causes regressive distribution of income in the society. When the black money grows faster, rich becomes richer and the poor become poorer. By way of concentration of income and wealth in few hands, the black money widens the gap between the rich and the poor.
- Black money is disposed off by lavish spending on travels and tours, entertainment, ostentatious articles, financing of extravagant elections etc. This has also lead to many social evils and deteriorated the values of life of the common people.
- The black money has altered the choice coefficients in the market in favour of luxuries, which lead to the diversification of productive resources from essential goods to the non-essential goods.
- Black money holders are always in a position to put their prior claim over the scarce goods in the market due to their readiness and ability to pay more, thereby depriving the honest and poor people from their legitimate share.

This obviously reduces the net economic welfare of the Indian society at large.

- Black money is largely responsible for the deterioration of general moral standards of the society. Black income generation implies a deviation from the accepted norms in society and from the point of view of the society is unethical.
- As a consequence, the consumption pattern is titled in favor of the rich and elite, at the cost of encouraging production of articles of mass consumption. A rise in overall consumption leaves fewer resources for investment in priority areas, having an adverse effect on production.

Conclusion

The exact effect of black money on any economy shall be summarized as, Growth of economic dualism. Under-estimation of the true size of the economy, Tax evasion, thereby loss of revenue to Government, Undermining equity, Widening Gap between the Rich and Poor, Lavish Consumption Spending, Distortion of Production Pattern, Distribution of Scarce Resources, Deterioration of General Moral Standards of the Society, Effects on Production.

2. What are your views on the level of tax compliance in India? What measures have been taken by the government to increase tax compliance? Discuss

Introduction

Increasing tax compliance is a constant worry of tax authorities around the world and this is more pronounced for developing countries like **India** that seek to achieve numerous social and economic objectives through tax collection and inventives.

Body

Tax Compliance in India:

- Tax structure in India is divided into direct and indirect taxes where direct taxes are levied on taxable income earned by individuals and corporate entities while indirect taxes are levied on the sale and provision of goods and services.
- Every tax payer is required to undertake certain compliances like Annual filing of return of income, report of audit under the Income Tax Act, etc.
- Historically, rate of tax compliance is low in India with only 36% of all individual taxpayers in organised and unorganised sector filing tax returns (Finance Minister). But recent data shows this at even low level of 11.6% among individual taxpayers.
- Further, only 1.5% of Indians pay income tax out of which there are large disparities within the taxpayers too as bottom 23% of the income tax is

contributed by 93% of the taxpayers. This reflects at the macroeconomic level where India has a low tax to GDP ratio.
- Recent data further throws light on the low compliance rates where less than 50% of Doctors pay taxes and only 1/3 rd of the CA's pay taxes.

Measures by Government to increase tax compliance:

Age old wisdom of Chanakya needs to guide the tax collection and compliance in India where he opined that taxes should be collected like bee collecting honey i.e. in right amount and without inflicting pain. Such an ideal would help in improving tax compliance and government has undertaken following measures to make India a tax conpliant society:

- **Demonetisation** - the act of stripping a currency unit of its status as legal tender which was undertaken to combat tax evasion via 'black money' held outside the formal economy. It helped in increasing formalisation of economy and the consequent scrutinizing of bank deposits.
- **Goods and Services Tax** - introduction of GST in 2017 has been termed as one of the biggest indirect tax reforms in country. It is a comprehensive multistage, destination based tax which follows a dual model. This has helped in reducing compliance costs considerably.
- **PAN-Aadhaar Linkage** - has helped in getting rid of fake PAN cards, identify tax evaders, curb black money circulation and make it easy for Taxpayers to file returns. Further, legitimacy of returns has also been improved due to foolproof authenication and verification procedures incorporated.
- **Project Insight** - a tax tracker based on big data where government will put to use a range of non-traditional but effective sources of information to help tackle tax evasion and aviodance. This is inspired from 'Connect' program of United Kingdom.
- **Form26AS changes** - the annual consolidated tax statement which is based on PAN which has helped in simplification of tax procedures and compliance.
- **Digitalisation** - promotion of digital transactions and increasing formalisation of economy have helped in reducing the possibilities of hiding income. Further, tech interventions have helped taxpayer's in easing compliance and assessments.
- **Behavioural economics** - incorporation of behavioural economics and employing social norms to nudge individuals to pay their taxes has helped improve compliance. Largescale advertisements by CBDT are efforts in this direction.
- **Rationalisation measures** - incorporated through 2018-19 budget have empowered agencies and enforcement authorities towards greater scrutinizing powers which have helped in better compliance.

These measures along multi- sectoral efforts on part of government is helping towards the goal of making India a tax compliant society from a non-tax compliant society.

Conclusion

A healthy functioning economy is based on equal participation of all stakeholders where law-abiding entities are favoured towards the goal of making India a low tax rate, high tax compliance nation where each person pays a moderate rate of tax.

3. What is existing mechanism to address fiscal deficit? What are your views on the current trends of fiscal deficit? Examine the need for setting up a fiscal council to monitor fiscal deficit in India.

Introduction

Fiscal deficit is an indication of total borrowings needed by the government. As per the OECD around 3% of GDP is a healthy fiscal deficit for any economy. Indian economy has been successful to keep its fiscal deficit under control. Yet, there are some concerns regarding the fiscal deficit targets that are being achieved.

Body

Background:

15th Finance Commission's Chairman NK Singh has pitched for an institutional mechanism like a 'Fiscal Council' to enforce fiscal rules and keep a check on the Centre's fiscal consolidation.

Mechanism to address fiscal deficit:

At present, the fiscal deficit targets are set as per recommendations of FRBM review committee under N K Singh. The fiscal deficit is finance through the following means:

- Market borrowings: G-sec and Treasury bills.
- Securities against small savings.
- State provident funds as well as internal debts and Public account receipts.
- The government may borrow from Reserve Bank of India against its own securities.
- External debt including external commercial borrowings.

Further, The fiscal policy statement, medium term fiscal strategy statements etc., in the budget gives information about the fiscal deficit of the government. The current trends show that reaching its peak in 2011-12, the fiscal deficit has reduced continuously in the consecutive years reaching the lowest of 3.4% GDP. However, the targets as set by FRBM act has been breached. Also the revised estimate is deviating from the budget estimates which is a cause of concern.

Need for setting up fiscal council:

- Poor Budgetary Forecasting: Budgets often overstate revenue projections (15 out of 20 years since fiscal 1998) and understate expenditures (12 out of 20 years since fiscal 1998).
- Limited Tax Buoyancy: Faster growth in nominal gross domestic product (GDP) usually leads to faster growth in tax collections. However, in India, tax buoyancy shows no stable pattern and hence, forecasting tax revenues is difficult.
- Creative Accounting: Moreover, fiscal deficits are also understated by the use of 'creative accounting' such as 'rolling over' a part of the overall subsidy bill & dues to the states to the next financial year; using PSEs like LIC to purchase divested stakes in the disinvestment process. Such "creative" accounting has led to a decline in the headline fiscal deficit number but failed to reduce India's public debt to GDP ratio, adversely impacting India's macroeconomic stability.
- Use of Extra Budgetary Resources (EBR): Over the years, the Govt's reliance on EBRs- such as funds of state- owned enterprises like LIC, SBI etc - to fund Govt. programmes has increased, but it doesn't appear in real time fiscal deficit numbers. E.g. 61.4% of all capital expenditure outlined in the 2018-19 Budget is to be financed through EBR, up from 54% in 2016-17.
- Absence of uniform fiscal consolidation rules for centre & states:
    - Various cesses and surcharges, in which States' have no share, are becoming a disproportionate portion of overall divisible revenue. This is against the spirit of fiscal federalism and financial devolution process.
    - For State Govt., Art 293(3) provides a constitutional check over market borrowings while no such restriction is there for the centre.
    - States have constraints in managing their finances as the RBI controls their deficit and cannot float a bond on a state's behalf without the Centre's approval.
- Non-adherence to Fiscal Responsibility and Budget Management (FRBM) Act targets: Since 2003 FRBM law came into effect, there have been four pauses in the deficit targets enshrined in it and many occasions where the targets have been flouted.
- Fiscal Populism: Political class has the tendency to make fiscal policy over-expansive, which increases burden on future government and thus, has detrimental long-run impacts e.g. loan waivers to farmers, tax waiver to MSMEs etc.
- Poor institutional infrastructure for monitoring: CAG has presented its audit report on Compliance of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 but the assessment is only post-facto.

Advantages of Fiscal council:

- IFC's evaluation of budget announcements & forecasts would indicate how realistic government projections are. This would be a check on competitive

populism in Indian polity and would increase financial accountability of the government to the Parliament.
- An institutional mechanism for sound fiscal practices will bring in transparency, instill confidence among domestic & foreign investors and improve policy outcomes.
- It will promote the culture of proper disclosures and good accounting practices within the Govt.
- Most fiscal councils across the world are able to discipline lawmakers through 'comply or explain' obligations— requiring governments to at least explain the divergence from the fiscal council's views.
- International experience suggests that a fiscal council improves the quality of debate on public finance, and that, in turn, helps build public opinion favourable to fiscal discipline.
- An institutionalized fiscal council would enhance cooperation with Finance Commission and GST Council.

Conclusion

According to International Monetary Fund (IMF), IFCs are now an indispensable part in the design of fiscal frameworks aimed at guiding fiscal policymakers' discretion. Even as NK Singh committee noted and recommended, an independent fiscal council can bring about much needed transparency and accountability in fiscal processes across the federal polity.

4. How are the states placed in terms of managing their budgets? How important is it to update state-level fiscal responsibility legislation? Examine.

Introduction

- To advance rather than defer the desirable goal of fiscal prudence, India like several other countries, embarked in the mid-2000s on an ambitious project of fiscal consolidation, adopting fiscal rules aimed at curbing fiscal deficits and imbalanced sharing of revenues.
- Budgeting is the process of allocating finite resources to the prioritized needs of an organization. In most cases, for a governmental entity, the budget represents the legal authority to spend money.

Body

Position of States in terms of managing their budget

- In 2018-19, states are expected to spend 72% more than the central government, a significant change from 46% in 2014-15 (last year of the 13th Finance Commission). Thus, much of the expenditure that affects citizens is decided at the level of the state. Meanwhile, decisions on receipts are getting centralised at the level of the centre with the implementation of the GST.

- Most of the states depend on the centre for the large chunk of their revenue. There are different channels through which the centre transfer funds to states like Finance Commission(FC). Besides, the Gadgil-Mukherjee formula and Finance Commission formula also does the same.

According to the The report released by Reserve Bank of India (RBI) titled "State Finances: A Study of Budgets of 2019-20", States' Gross Fiscal Deficit (GFD) has remained within the Fiscal Responsibility and Budget Management Act (FRBM) threshold of 3% of Gross Domestic Product (GDP) during 2017-18 and 2018-19. For 2019-20, States have budgeted a consolidated GFD of 2.6% of GDP.

- In 2018-19, 52% of the revenue receipts of states is estimated to come from their own revenue, and the remaining 48% of the revenue in the form of transfers from the centre.
- Outstanding debt of states have risen over the last five years to 25 per cent of GDP.
- Some states spend more on Agriculture and some on industries. Eg Karnataka had become the first State in the country to come out with an exclusive Budget for Agriculture.

Importance of updating state level fiscal responsibility legislation

- Fiscal Responsibility Acts are important for fiscal prudence and better public expenditure quality.
- Adoption of fiscal policy rules built under responsibility legislation commits the government to a deficit or debt reduction path.
- The institutional framework of the fiscal legislation facilitates effective monitoring of fiscal performance of the government and encourages pursuit of fiscal management policies aimed at transparency, efficiency, responsibility, fairness and stability.
- The policies under fiscal responsibility seek to enhance the credibility of the Government through actions, which indirectly result in reduction of interest rate on borrowings of the state government, and take initiatives for growth in GSDP (Gross State Domestic Product), leading to a decline in debt-GSDP ratio.

Conclusion

While such legislations cannot be panacea for all fiscal ills and moreover, have their own drawbacks, but they provide a basis for political consensus to accomplish complex economic tasks and thereby enhance the credibility of the Government. Therefore, these policies should be aimed at being internally consistent and "not conflict with each other" and flexible to adapt to exogenous shocks.

5. Without stronger, sustainable and inclusive growth India doesn't have the resources to expand the welfare schemes significantly. Discuss.

Introduction

Inclusive growth means economic growth that creates employment opportunities and helps in reducing poverty. It means having access to essential services in health and education by the poor. It includes providing equality of opportunity, empowering people through education and skill development. It also encompasses a growth process that is environment friendly growth, aims for good governance and a helps in creation of a gender sensitive society.

Body

Why India needs stronger, Sustainable and Inclusive Growth?

Inclusive growth as mentioned above is necessary for the sustainable and holistic development of all sections of the society. For economic, social and political empowerment of its citizens, Inclusive growth is indispensable to India.

- India is the 7th major country by area and 2nd by population. Yet, India is far away from development while our neighbour China is advancing at a faster rate to become the largest economy of the world.
- Poverty in India is at 22% according to the Tendulkar committee report.
- Low agriculture growth, low-quality employment growth, low human development, rural-urban divides, gender and social inequalities, and regional disparities etc. are the problems for the nation.
- Protests like the recent ones of Jats in Haryana, Patels in Gujarat will only rise if the issues of agriculture productivity, employment growth are not taken care of.
- Labour productivity is very low due to informalisation and poor skill development.
- Access to education and health is not the same for all sections of the population. Females are treated to be subordinate to males and are dependent on their families in all spheres. Inclusive growth is hence the key to women empowerment.
- Regional inequalities are the cause for the rise in distress migration, either intra-state or inter-state. Distress migration further creates problems of housing, accommodation, safety, hygiene, and sanitation.
- Financial Inclusion is the key to transforming the informal economy into the formal economy.
- Corruption is still rampant in the country and prevents inclusive growth.
- Political leadership plays a vital role in growth and development of the country. But implementation of many schemes is poor due to lack of political will.
- The importance of inclusive growth is indisputable for sustainable growth.

- Global warming and climate change affect poor more than the rich. Displaced population further increases distress migration and stress on states resources.
- MDG report for India (2015) suggests that out of 18 indicators, India is on-track only in four indicators. In the rest of the indicators, India is identified as either off-track or moderately on track . Achieving Sustainable Development Goals is not possible without concentrating on inclusive growth.

Steps Taken by India for stronger, sustainable and inclusive growth

- In agriculture, emphasis must shift to converting farmers to 'agripreneurs' by further expanding e-National Agriculture Markets (e-NAMs) and replacing the Agricultural Produce Marketing Committee (APMC) Act with the Agricultural Produce and Livestock Marketing (APLM) Act. The creation of a unified national market, a freer export regime and abolition of the Essential Commodities Act are essential for boosting agricultural growth.
- A strong push would be given to 'Zero Budget Natural Farming' (ZBNF) techniques that reduce costs, improve land quality and increase farmers' incomes. This is a tested method for putting environment carbon back into the land. Therefore, ZBNF allows India to significantly contribute to reducing the global carbon footprint.
- To ensure maximum employment creation, codification of labour laws must be completed and a massive effort must be made to upscale apprenticeships.
- With the completion of the Bharat Net programme in 2019, all 2.5 lakh gram panchayats will be digitally connected. In the next phase the last mile connectivity to the individual villages will be completed. The aim will be to deliver all government services at the state, district, and gram panchayat level digitally by 2022-23, thereby eliminating the digital divide.
- Successfully implementing the Ayushman Bharat programme including the establishment of 150,000 health and wellness centres across the country, and rolling out the Pradhan Mantri Jan Arogya Abhiyaan.
- Upgrading the quality of the school education system and skills, including the creation of a new innovation ecosystem at the ground level by establishing at least 10,000 Atal Tinkering Labs by 2020.
- As already done in rural areas, affordable housing in urban areas will be given a huge push to improve workers' living conditions and ensure equity while providing a strong impetus to economic growth.
- Implementing strategies to achieve regional equity by focusing on the North-East region and successfully rolling out the Aspirational Districts Programme.
- Implementing the recommendations of the Second Administrative Reforms Commission as a prelude to appointing a successor for designing reforms in the changing context of emerging technologies and growing complexity of the economy.
- A new autonomous body, viz., the Arbitration Council of India, may be set up to grade arbitral institutions and accredit arbitrators to make the arbitration

process cost effective and speedy, and to pre-empt the need for court intervention.

Conclusion.

Inclusive growth is of vital importance to fight inequality in all aspects and promote holistic development of individuals in the country. Digital technologies like mobile phones, the internet can be harnessed for financial inclusion to address social-economic challenges of the country.