JudicateMe

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FRBM Act: Explained with special reference to State of Kerala

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Introduction

Before determining the financial situation Kerala is facing or will face in the near future, it would be for the best if the reader understands what FRBM Act is.

FRBM Act stands for Fiscal Responsibility and Budget Management Act (hereinafter referred to as "the Act". This Act was first introduced in the Indian Parliament, in the month of December of 2000, as a Bill. Though the Act got passed on 16th of August, 2003, it came into effect only after 4th of July, 2004.

The objectives of the Act aimed at eliminating the revenue deficit by the year 2008-09 and thereby reducing the fiscal deficit which would not be more than three (3) percent of the GDP by the end of the year 2008-09. But since nothing happens as planned, due to global financial crisis and recession thereafter, the then Congress led government had to infuse the resources in Indian economy which would act as an instrument of fiscal stimulus (in the year 2008). This led to a temporary postponement of the fiscal targets which were to be initially achieved by the setting up of this Act.

On March 2012, Medium-term fiscal adjustment and its road map was introduced by the Central government so as to improve the fiscal situation at the Central level. Which meant that effective revenue deficit notion was introduced. This gave the power to the Centre to exclude some states from getting grants, when the states asked for such grants as a capital asset.

Since 2003, it has been four times that the Act's implementation has been stalled. It has been a long since the Act had not once been evaluated since its effect from 2003. So in the year 2017, a FRBM committee which was set up published its report regarding the Act in the month of April.

Objectives & Purposes of the Act

There are many objectives and purposes laid down by the Act, these are:

- *Transparency:* One of the major intentions which is to be achieved by the Act is that before the introduction of this Act the fiscal management system in India was obscure and ambiguous. But now, by introducing the Act, the legislature wants to create transparency between the people, centre/state and fiscal management system of India.
- *Fiscal stability:* The most important long term goal which the Act intends to attain is that India should achieve fiscal stability. Meaning, the total expenditure of the

government of India should not be more than the total receipts (ie. revenue).

- *Flexibility:* The legislature while making this Act kept the powers of RBI (Reserve Bank of India) in mind. This can be seen as by reading the above point, when fiscal stability would be achieved, then the Act intends to provide RBI, during inflation period in the nation, a flexible power to monitor the same.
- *Intergenerational equity:* The Act shifts the onus of responsibility to the Central Government for ensuring that while talking about fiscal management, the intergenerational equity must be maintained or made stable.
- *Limit:* The Act also makes the Central government bound to set up a limit beyond which the centre's debt & deficit cannot cross. Along with that, the limit is also set for each and every state, keeping in mind each state's limit is different as their requirement is different.

Salient Features of the Act

- *Contingent Liabilities:* Originally the Act stated that the assumption of contingent liabilities which were to taken as a guarantee would be percentage of the GDP. But the FRBM Rules of 2013 added that a statement should be provided in the Medium term Expenditure Framework. This statement must lay out the contingent liabilities that too in the form of a stipulated payment which must be paid over a time of multiple years.
- *Effective Revenue Deficit:* Though this was not included in the original text of the Act, but this was added through the FRBM 2013 Rules and Amendment of FRBM Act, 2015. The 2013 Rules stated that Central Government had reduced the deficit equal to 0.8% or more of the GDP by the FY end, and this began from 2013-14. But as this target failed, the 2015 Amendment made the Central government to decrease the deficit equal to 0.5% or more of the GDP by the end of the FY, which began from 2015-16.
- *Revenue Deficit:* The Act aimed to reduce the Revenue Deficit by the end of the financial year of 2008. And so the government should create revenue surplus. But the Amendment of 2015 stated that Revenue Deficit should not be more than 2% of the total of the GDP by 2018. Along with that, the annual reduction must be equal to 0.4% or more of the total of the GDP, starting from the year 2015-16.
- *Gross Fiscal Deficit:* The 2003 Act aimed at reduction of GFD by the end of FY 2018. But the 2015 Amendment Act stated that the GFD should not be in any way more than 3% of the GDP by the end of FY 2018. Along with that, the annual reduction should be equal to 0.4% or more of the total GDP.
- *Liabilities:* The FRBM Rules of 2004, amended by laying upon the Central Government to ensure that additional liabilities should not cross 9% of the GDP of FY 2004-05. Afterwards, in each FY, the 9% of GDP limit must be reduced slowly by a minimum of 0.1% of the GDP.

Key Features of the Act

The key features of the Act has been provided in the Act's preamble itself. The Act renders it compulsory for Central Government to put across the following annually in Parliament along with the Union Budget.

- Medium Term Fiscal Policy Statement
- Macroeconomic Framework Statement
- Fiscal Policy Strategy Statement

It is also provided by the Act that Medium term fiscal policy statement must include revenue deficit, tax revenue, etc. as a percentage of the GDP.

Case Study: Request for relaxation under the Act by State of Kerala

1.1. Frame of reference

Since Kerala was one of the first states affected by COVID-19 pandemic, and rather affected the state in a very adverse manner. The state government diverted most of its finances into dealing and controlling the pandemic, due to this the state government did not want their overall finances to be impacted. Hence, they have requested the Centre to be flexible towards them in respect to the FRBM Act and its guidelines thereof.

1.2. Inceptive remedial measures taken by State of Kerala

As Kerala had succumbed to the viral outbreak at the very beginning, as compared to the other states in India, the State Government of Kerala had at the very inception announced a Rs. 20,000 Crore economic package so as to tackle firstly, the impact of COVID-19 on the livelihood of the citizens, and secondly, to mitigate the effect of this pandemic on the overall economy of the state. But as money does not come flying to the State funds, the State government decided to borrow Rs. 12,500 Crore in the month of April from the market.

1.3. Call for help in the mist of seeking flexibility

According to the current fiscal position of the country and State of Kerala specifically, the State is in a position to borrow Rs. 25,000 Crore during the 2020-21 Financial Year. Assuming Government of Kerala plans to collect half that amount of debt during the first month of the new FY, then the State Government is perturbed that the harsh borrowing cap under FRBM Act should in no manner limit the ability of the State to spend and borrow over the residual eleven months. This is of the paramount importance to the State government, as Kerala would not only need money for mitigating the pandemic in the remaining 11 months, but would also need funding for post recovery, and routine affairs.

1.4. Relaxation under FRBM Act, 2003

Section 4(2) is a provision under the FRBM Act which is also known as an “escape clause”. Simply putting forth that if an act committed by the State which makes them liable to repay the Centre will not make the State liable if the situation caused was due to the reasons as stated in Section 4(2) of the Act. What Section 4(2) states is that Centre has the opportunity to exceed its annual fiscal deficit target, but only and only if an exceptional situation arises. There are certain exceptions provided in the said provision. These are national security, war, national calamity, collapse of agriculture, and more.

1.5. How State of Kerala falls under the garb of the exceptional clause

This incessant pandemic, due to its global atrocities and unavailability of vaccines, satisfies itself to be called a 'national calamity', which is an exception stated in Section 4(2) of the Act. In addition to this, the present 21-day lockdown so as to fight the pandemic will surely cause the economic output to contract. Hence it would be for the best if the Centre along with the State's fiscal deficit targets are suspended for the time being. This step would allow the Centre along with multiple states like Kerala to tackle the rise in expenditure due to the current pandemic.

Conclusion

This is a live example of how escape clause will be tested in practicality and the Central government will also get to know the efficacy of the Act as well as the practical aspects involved in a situation where a state genuinely seeks exemption under the provisions of Section 4(2) of the Act. In fact the representation of the state of Kerala may be a precursor to many more state falling in the same situation including the centre as well. Thus the following weeks or months would establish practically whether the intention of the legislature in enacting the FRBM Act with all its clauses has succeeded in implementing the purposes for which the same was promulgated.

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Under this Scheme, the Directorate of Plant Protection, which is in Haryana, organizes various programmes purely for the benefit of the farmers. This is carried out by the 35 Central IPM Centres located all over the country. A 2 to 5 days training program is conducted for the farmers in State- run institutions for educating the farmers through the farmer field schools i.e., Krishi Vigyan Kendras about various aspects such as management, kinds of pesticides, seeding, fertigation etc., some of those areas which would have been known to a farmer only by experience. Basically, farmers are provided technical know-how about farming which ultimately helps them in increasing the quantum of their produce and as a result, their sale.

The condition of the farmers nowadays is very poor. They believe in all kinds of superstitions. In such a situation, these schemes act as ray of hope for them and hence they expect that these will certainly change their present situation. Agriculture is a State subject and the State Governments are basically in charge of the development and advancement of farming area in their individual States. The Government supplements the endeavours of States through fitting arrangement measures and budgetary help. Currently the approach of the Government of India has moved from production driven to income driven stage in the agriculture sector and the above plans are being actualized for making cultivating practical. Improvement in the situation of the agriculture will lead to enhancement of the condition of the farmers.