State Fiscal Problems and Role of Central Assistance : The Case of North Eastern States of India

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Abstract

This paper examined the fiscal problems and role of the central assistance in the context of fiscal management at the sub-national level, particularly with reference to special category states in India like the North Eastern states. Observing the status of fiscal autonomy, fiscal dependency, the mismatch between revenue receipts and expenditure, the study examined how the Central Plan Assistance, which has been received on the basis of gap filling approach has been used by these states for non plan revenue expenditure. The paper observed that there should be policy initiatives so that the North Eastern states are able to increase their own revenue and at the same time, the Central government should not only devolve resources ; rather, there should be a mechanism regarding how to control their non plan revenue expenditure so as to make the plan assistance available only for developmental expenditure.

Key words: **fiscal problem, central assistance, gap filling approach, non-plan revenue expenditure**

JEL Classification : H2, H3, H7

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India is a federal country, and the fiscal performance of the country as whole depends on the fiscal performance of its constituent sub-national governments. Therefore, fiscal indiscipline at the state level has been given importance so as to implement discipline and to achieve micro economic efficiency and macroeconomic stability. In this context, the state governments argue that they suffer from financial constraints and the Centre should play a role to match the deficits since state governments are unable to do so on their own. This is being satisfied in terms of provision of central assistance from the central government to the state governments. In addition to this, there is a special provision assistance for the special category states like the North Eastern states. These states get special assistance from the Centre unlike other general category states.

However, over the time, the fiscal federal mechanism has been questioned due to its resource devolution mechanism and the provision has created a debate. The argument is that since the special category states are getting extra assistance, they should be in a position to maintain fiscal discipline. Furthermore, though in the recent days, the central government has already restructured the institutional mechanism like planning commission to NITI Ayog ; still, there is scope for better performance of the institutional mechanism to ensure sub-national level fiscal discipline. In this context, this paper is a modest attempt to analyze the fiscal problems of special category states with a special reference to North Eastern states and examine the role of central assistance at the sub national level for fiscal discipline.

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Literature Review

The fiscal problems of both central and state level government drew wide attention, and during the 1990s, policy measures focused on fine-tuning state government finances (Chelliah, 2005). Over the time, fiscal indiscipline at the sub - national level became the centre point of discussion among policy makers, academicians, and people in general. In addition to this, since India is a federal country, and there is a Centre-State financial relationship in terms of fiscal federalism and fiscal transfer, the role of Central transfer within the context of fiscal discipline of the sub national government became an important area of research.

There are many studies regarding fiscal federalism, and state government's fiscal discipline in general, like studies conducted by Lahiri (2000) ; Rao (2002) ; Rao (2003) ; Bagchi and Chakraborty (2004) ; Heredia - Ortiz and Rider (2005) ; Garg (2006) ; Singh (2006) ; and Dikshit, Viswanathan, and Raghunandan (2007). In the context of special category states, Srivastava and Rao (2009) undertook an empirical overview of the states' share in central taxes in India and observed that the special category states required a separate exercise for determining grants to ensure fairness within this group of states. Bhat and Scaramozzino (2013) analyzed the long-run relationships between federal transfers, NSDP per capita, and state fiscal deficit in India. The evidence supported the view that the Indian federal transfers system is indeed "gap-filling" in nature.

The federal transfers in India have been successful in directing resources towards the poorer states, but have been less effective in enforcing the incentives for local states to strengthen their fiscal discipline. It is important that policies should be directed at enhancing the revenue-raising capabilities of the states and at improving their fiscal discipline and accountability. Sen and Dash (2013) studied fiscal imbalances and indebtedness across Indian states and concluded that in the case of special category states, their adjustment efforts were, by and large, heavily dependent on central transfers, which is not surprising, given their dependence on the same. Two large adjustments in Arunachal Pradesh and Manipur are obvious examples of this. However, all of them, barring Sikkim, made significant efforts to raise their own revenues too. The study conducted by the Finance Commission for all states observed that the states did not show any effective result by the state governments for fiscal discipline, particularly in the context of the North Eastern states of India. In this line, Nayak, Roy, Mitra, Nochi, and Lama (2013) conducted a study for Arunachal Pradesh and suggested that the state's own-non tax revenue as a percentage of GSDP declined after 2008-09 onwards. This trend needs to be reversed.

Barua, Goswami, and Dutta (2013) conducted a study for Assam state finances. They observed the efforts taken by the state to work towards fiscal consolidation and enhance the level of fiscal sustainability evident in the successful attainment of the AFRBM targets and also in their subsequent consolidation, but observed leakages, short mobilization, and evasion of revenue both due to weaknesses in the system and also due to deliberate transgression by officials. Singh, Nepram, Singh, and Mangang (2013) observed that in the case of Manipur, the requirements of finances for development could not be met by the resources of the state, and the centre has to step in to meet the requirements of the state. The Finance Commission ("Evaluation of state finances with respect to Meghalaya : A study for the fourteenth finance commission," 2013) conducted a study for Meghalaya and found that the state government had also not been very proactive in effective and productive expenditure management as could be seen from high revenue expenditure at around 80 - 85%, leaving very little for capital expenditure which increases the productive capacity of the state.

Vanlalchhawna (2015) examined the fiscal transfers to Mizoram and observed that Mizoram's economy is basically driven by resource transfers from the central government. Sinha (2014) recommended that the state of Nagaland needs to boost its own tax and non-tax revenues to provide greater resources for much needed social and physical infrastructure. Kundu (2013) observed that for the state of Sikkim, there was a decrease in the debt-GSDP ratio, which was much below the normative assessment made by the XIII Finance Commission. Nath and Bhowmik (2013) examined the data for the state of Tripura, and observed that the contribution of tax from many sources had increased, while that of some declined over the years. An analysis of the tax structure reflected that an upward revision and effective implementation could help the government to increase its own tax collection. However, to observe fiscal performance after fiscal reform programs, Dash (2011) measured the fiscal performance of Tripura by evaluating its performance over the time period from 1990-91 to 2009-10 and concluded that Tripura should maintain its fiscal discipline in terms of deficit management and own revenue augmentation to have sustainable, long term financial stability.

Similarly, Dash and Tiwari (2011) ranked the NE states according to their fiscal performance and conducted the nonlinear stationary test using the Ucar and Omay (2009) method. The authors observed that Arunachal Pradesh ranked first among all NE States, and the fiscal performance of Northern states of India was liner non stationary. Dash (2015) studied the growth performance and debt position of NE states and concluded that the growth performance was not satisfactory ; rather, the states suffered from huge mounting public debt. Furthermore, recently, Dash (2016) observed the deficit and debt scenario of the NE states for the period from 1999-2010 and concluded that though the NE states are special category states and are getting more grants than loans from the Central government ; still, these states are unable to attain revenue sufficiency and are going for debt. The average of debt as a percentage of GSDP showed an increasing trend for the NE states, which is negative from the view of point of revenue management and planning for developmental expenditure.

Objective and Research Methodology

The objective of this study is to examine the fiscal problems and the role of central assistance in the context of fiscal management at the sub - national level, particularly with reference to special category states in India like the North Eastern States. The study period was set over 1991 to 2010 so as to examine the scenario over the last 20 years. It is basically explorative by nature and is based on secondary data. We have used the latest available data collected from Hand Book of Statistics on State Government Finances published in the year 2010 by the Reserve Bank of India, which is widely accepted as authentic. Though there have been changes and the current data is available up to today, it has not yet been compiled, which can be used for a study like this. Data was analyzed and interpreted with appropriate statistical methods like percentage, average, and growth rates.

Data Analysis, Interpretation, and Results

Fiscal Problems

(1) Revenue Expenditure : Revenue receipts and their expenditure determine the fiscal condition of a state. The Table 1 shows that in the case of the North Eastern states (here after, NE states), the share of non-tax revenue is greater than the share of tax revenue ; whereas, in the case of the 14 major states, the share of tax revenue is greater than the share of the non-tax revenue. This is because of larger share of grants in the composition of non-tax revenue from the Centre because of special category status.

In the category of tax revenue, the share of shared tax from the Centre is more than the states' own tax revenue for NE states ; whereas, in the case of 14 major states, the share of states' own tax revenue is more than the share of shared tax revenue from the Centre. However, in the category of state non-tax revenue, even in the case of 14 major states, the share of state own non tax revenue is less than the share of grants from the Centre. Such a composition of revenue receipts of NE states, which largely consists of grants received from the Centre clearly indicates that the *NE states are basically dependent upon the central government's fiscal transfer in accumulating resources to meet their total revenue requirements.*

Out of the total revenue receipts, the revenue expenditure is made for the day to day administration and other expenditure in current , which are basically unproductive in the sense that it does not create any new infrastructure

Table 1. Sources of Revenue Receipt (As a Percentage of Total Revenue Receipt)

State	Time	TAX REVENUE			STATE NON-TAX REVENUE		
	Period	State Own Tax Revenues	Shared Tax From Centre	Total Tax Revenue	State Own Non-Tax	Grants from the Centre Revenue	Total Non-Tax Revenue
Average of NE States	1991-95	12	23.51	35.85	11.34	52.81	64.15
	1995-2000	11.32	26.54	39.86	14.73	28.17	60.14
	2000-05	23.54	25.15	48.73	11.66	45.35	51.27
	2005-08	18.05	25.39	42.34	15.91	64.46	57.66
	2008-09 (RE	16.85	24.46	39.85	12.76	71.15	60.15
	2009-10 (BE)	15.23	23.95	37.8	11.96	74.44	62.2
Average of 14 Major States	1991-95	44.41	21.35	65.76	15.52	18.71	34.24
	1995-2000	47.6	22.74	70.33	14.99	14.67	29.66
	2000-05	49.69	21.37	71.06	12.69	16.26	28.94
	2005-08	47.4	23.07	70.47	11.88	17.65	29.53
	2008-09 (RE)	58.54	30.74	58.54	14.11	27.35	41.46
	2009-10 (BE)	59.19	29.99	59.19	13.57	27.24	40.81

Note: The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Authors' calculation on the basis of data collected from Reserve Bank of India. (2010). Hand Book of statistics on state government finances.

Table 2. State Wise Revenue Expenditure (As a Percentage of Total Revenue Receipts)

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total (RE)	Total (BE)	Avg.
Arunachal Pradesh	69.95	79.49	94.79	90.21	73.19	75.26	79.09	110.75	85.7
Assam	97.72	102.13	109.01	87.47	83.83	83.16	91.91	126.91	94.66
Manipur	81.14	96.87	105.24	83.23	84.35	65.36	71.43	76.30	76.14
Meghalaya	91.48	92.72	97.82	95.82	89.08	92.34	85.88	94.27	91.48
Mizoram	80.93	92.5	110.16	96.01	87.2	93.53	91.15	94.12	92.4
Nagaland	104.91	102.53	94.61	90.91	80.13	85.85	89.31	81.07	85.46
Sikkim	86.33	98.14	90.02	90.02	89.18	87.03	80.11	85.88	86.45
Tripura	96.82	92.88	97.42	79.1	74.5	75.55	82.30	92.48	80.79
Average of NE States	88.66	94.65	99.88	89.09	82.68	82.26	83.90	95.22	86.63
Average of 14 Major States	105.98	116.15	120.94	101.63	95.31	93.12	98.55	104.01	98.52

Note: i) Avg. : Average ii) Note: The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Authors' calculation on the basis of data collected from Reserve Bank of India. (2010). Hand Book of statistics on state government finances.

to boost up the economic base. The remaining is used for the purpose of capital expenditure, which is considered to be important from the capital and infrastructural development point of view.

The Table 2 shows the revenue expenditure out of the total revenue receipts. The expenditure in the revenue account is observed to be a lion share and obviously, is more than the capital expenditure in the case of NE states.

Table 3. State Wise Revenue Deficits (₹ Cr)

State	1990-95	1995-00	2000-05	2005-08	2008-09 (RE)	2009-10 (RE)
	Average	Average	Average	Average	Total	Total
NE States						
Arunachal Pradesh	-3680	-200.4	-66.6	-540.0	-0,770	350
Assam	-1975	108.6	591.4	-2100.0	-1,886	6,206
Manipur	-2345	-11.8	57.2	-689.3	-1128	-949
Meghalaya	-935	-52.6	-27.6	-165.0	-522	-218
Mizoram	-2210	-54.4	74.4	-149.7	-239	-178
Nagaland	750	23	-128	-393.7	-368	-740
Sikkim	-720	-17.4	-153.8	-259.0	-592	-422
Tripura	-520	-73	-75.4	-796.0	-743	-347
Average of NE States	**-1454.37**	**-34.75**	**33.95**	**-636.6**	**-781**	**462.75**
Average of 14 Major States	**10767.85**	**2035.92**	**3800.85**	**-803.4**	**114**	**2,389**
All States	**133260.0**	**28,400**	**55091.6**	**-20262.3**	**-10701**	**32,295**

Notes: Minus Sign (-) indicates surplus in the deficit indicator.

Table 4. Developmental Expenditure as a Percentage of Total Revenue Expenditure

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total (RE)	Total (BE)	Avg.
Arunachal Pradesh	71.82	70.2	66.33	70.71	70.52	72.60	71.97	75.20	72.20
Assam	66.88	62.30	59.09	60.02	62.38	61.29	59.64	55.98	59.86
Manipur	65.68	65.56	56.24	64.14	63.84	59.36	60.49	58.27	61.22
Meghalaya	69.88	65.95	61.77	62.67	63.15	65.48	71.80	70.54	66.73
Mizoram	73.18	68.58	64.78	65.92	64.10	66.20	67.44	64.84	65.95
Nagaland	61.79	57.32	50.05	54.41	54.12	53.64	54.41	55.48	54.41
Sikkim	74.14	72.40	67.45	68.01	66.32	66.42	69.36	65.70	67.16
Tripura	71.42	68.43	63.36	58.14	57.24	56.75	61.92	58.63	58.54
NE States' Average	69.35	66.34	61.13	63	62.7	62.72	64.63	63.08	63.26
14 Major States' Average	66.77	61.74	55.51	56.04	56.96	58.64	61.81	59.74	58.64

Note: The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Authors' calculation on the basis of data collected from Reserve Bank of India. (2010). Hand Book of statistics on state government finances.

The important observation from the Table 2 is the allocation of more than 100% of total revenue receipts. If a state allocates more than 100%, then from where the extra amount of revenue is financed and for which reason there is need of extra amount of expenditure ? Such type of revenue expenditure planning affects the share of developmental and non developmental expenditure in the revenue account to understand the trend of developmental expenditure.

It can be observed from the Table 3 that Manipur had a deficit of ₹ 57.2 crores of deficit during 2000-2005 and Mizoram had a deficit of ₹ 74.4 crores during 2000- 2005. Nagaland had a deficit of ₹ 750 crores during 1990-

Table 5. Pensions, Salaries, and Wages as a Percentage of Total Revenue Expenditure

State	2001-05 Average	2005-08 Average	2005-06 Total	2006-07 Total	2007-08 Total	2008-09 Total(RE)	2009-10 Total(BE)
Arunachal Pradesh	--	--	--	--	--	--	--
Assam	58.15	--	--	--	--	--	--
Manipur	58.08	47.96	51.77	43.44	48.67	47.52	45.88
Meghalaya	--	--	--	--	--	--	--
Mizoram	46.17	--	39.61	40.59	--	--	--
Nagaland	54.91	56.45	56.23	56.35	56.77	50.89	56.69
Sikkim	34.77	--	30.56	25.37	--	--	--
Tripura	--	--	--	--	--	--	--

Note: '--' indicates about not availability of data relating to wages and salaries.

Source: Authors' calculation on the basis of Data Collected from A Study on State Governments Budgets 2011-12,RBI

1995, and a deficit of ₹ 23 crores during 1995- 2000. The NE states, as a whole, suffered from average deficit of ₹ 33.95 crores during 2000- 2005, and ₹ 462.75 crores during 2009- 2010 (RE).

The share of developmental expenditure as a percentage of total revenue expenditure has been tabulated in the Table 4. It is observed the *NE states as well as the 14 major states spent more than 60% of their total revenue expenditure for developmental expenditure, but it also shows a decreasing trend.* A decreasing trend of developmental expenditure is observed due to more expenditure for non developmental expenditure. It can be observed that the *NE states were spending more than 30% of their own revenue receipts for non developmental expenditure allocated for salaries, wages, and pensions.*

According to Vadra (2010), based on fiscal crisis at the state level, the most important reason behind fiscal crisis is non-planned, non developmental revenue expenditure where expenditure on salaries, wages, pensions, and interest payments constitute a major portion. These are the committed expenditures which have to be spent in spite of a limited resource base. The chief reason behind such exaggerated expenditure is the propensity of political leadership to counterproductive populism and avoidance of tough measures to stem the root causes. In addition to this, the impact of pay revision which pushes the state governments' expenditure and inefficient-under performance of the state-owned institutions like state electricity board and others reduce the states' own resources and cannot be avoided.

It is important to note here that there was a lack of complete data relating to the state governments' expenditure on salaries and wages. However, to present the situation, we are thankful to RBI because of its compilation of data, which we have collected and have presented in the Table 5. It is clear that during 2001-2005, states like Assam, Manipur, and Nagaland spent around 55% of their total revenue expenditure for pensions, salaries, and wages. The entire blame for the increase in the state government's expenditure can be given to the Pay Commission recommendations where the state governments have no control.

(2) Capital Expenditure : Capital expenditure of a state indicates the state's expenditure for productive infrastructural development. The Table 6 presents the percentage of capital expenditure out of total expenditure. From the Table, it can be observed that on an average, the percentage share of capital expenditure of NE states and general category states shows that, on an average, the NE states spent 24.55% of capital expenditure out of total expenditure during 1991-1995, when the general category states spent 19.09%. In the next time period, that is, 1995-2000, there was fall in the share of capital expenditure to 19.75% and 16.66% for NE and general category states, respectively. However, the figure increased to 23.97% for NE states and 21.84% for general category states,

Table 6. Capital Expenditure as a Percentage of Total Expenditure

State	1991-95	1995-00	2000-2005	2005-08	2008-09	2009-10
	Average	Average	Average	Average	(RE)	(BE)
Arunachal Pradesh	33.98	29.89	28.66	29.75	40.25	21.09
Assam	21.69	17.41	22.60	14.70	18.83	16.22
Manipur	35.07	27.04	33.83	33.46	40.53	32.52
Meghalaya	25.13	21.48	22.98	17.79	19.96	21.69
Mizoram	25.32	22.81	22.24	25.80	23.01	18.81
Nagaland	27.09	22.17	24.51	27.52	29.92	33.64
Sikkim	22.75	8.81	16.37	16.83	29.87	27.34
Tripura	18.52	20.99	24.32	26.54	32.53	29.87
NE States' Average	24.55	19.75	23.97	21.42	25.63	21.27
14 Major States' Average	19.09	16.66	21.84	22.03	22.09	20.30

Note: The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Authors' calculation on the basis of data collected from Reserve Bank of India. (2010). Hand Book of statistics on state government finances.

Table 7. Interest Payment as a Percentage of Revenue Receipt

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total(RE)	Total(BE)	Avg.
Arunachal Pradesh	4.89	6.96	10.59	8.43	7.25	5.16	6.19	7.76	6.96
Assam	13.8	15.01	16.84	12.53	11.09	9.86	8.19	9.13	10.16
Manipur	8.26	9.63	16.55	9.87	10.09	8.52	7.97	8.43	8.98
Meghalaya	6.28	8.43	11.37	10.93	9.47	7.74	6.21	6.46	8.16
Mizoram	5.43	8.36	13.26	11.18	11.63	10.19	8.47	7.97	9.89
Nagaland	11.04	12.03	13.49	11.2	10.09	9.01	9.64	9.69	9.92
Sikkim	7.62	3.45	6.05	5.24	5.43	4.37	4.74	5.68	5.09
Tripura	9.43	11.05	14.4	12.26	11.64	10.7	9.36	8.45	10.48
NE States' Average	8.34	9.36	12.81	10.2	9.58	8.19	7.59	7.94	8.7
14 Major States' Average	14.45	18.7	24.32	19.49	17.56	16	14.39	14.46	16.38

Note: The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Authors' calculation on the basis of data collected from Reserve Bank of India. (2010). Hand Book of statistics on state government finances.

respectively. Furthermore, the expenditure decreased to 21.42% and 22.03% for NE and general category states during 2005- 2008, respectively.

✦ **Interest Payment :** Interest payment is an important component in the state government's expenditure allocation. This share of expenditure allocation shows the state government's effort for repayment of loan on the one hand, and the diversion of funds towards non developmental revenue expenditure.

The share of interest payment as a percentage of revenue receipts by Assam was the highest (registering 13.8%), Nagaland was the second highest (registering 11.04%), and Arunachal Pradesh was the state with lowest

Table 8. Interest Payment as a Percentage of Own Revenue Receipt

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total(RE)	Total(BE)	Avg.
Arunachal Pradesh	19.88	47.11	71.09	38.61	31.65	11.8	37.75	39.78	31.92
Assam	53.98	81.7	82.71	51.75	40.77	35.41	42.54	51.57	44.41
Manipur	75.36	102.20	235.42	156.58	79.83	90.61	80.77	80.48	97.65
Meghalaya	55.85	64.16	69.55	65.41	55.16	47.49	57.79	51.25	55.42
Mizoram	31.84	75.87	135.53	77.08	86.09	80.00	71.12	66.30	76.12
Nagaland	94.66	135.96	209.99	130.93	153.85	113.85	103.11	114.85	123.33
Sikkim	23.65	2.47	6.89	5.20	5.30	4.17	5.93	7.25	5.57
Tripura	133.41	139.61	118.93	289.84	204.21	172.17	147.74	123.42	187.48
NE States' Average	61.07	81.13	116.26	101.92	82.10	69.43	68.34	66.86	77.73
14 Major States' Average	47.40	62.58	95.95	87.64	73.64	64.68	66.71	69.29	72.39

Note: (I) "+" indicated Deficit and"-" indicates Surplus (ii) The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Source: Same as Table 7

spending (registering 4.89%) during 1991- 1995. In the next period, that is, during 1995-2000, the interest payment as a percentage of revenue receipts increased for all NE states except Sikkim. Assam continued to be the state with the highest spending, and Sikkim was a state with the lowest spending. In the case of Sikkim, the spending decreased from 7.62% during 1991-1995 to 3.45% during 1995-2000. During 2000-2005, interest payment as a percentage of revenue receipts for all NE states increased in comparison to the previous time period, and Assam continued to pay the highest percentage and Sikkim, the lowest. *The interest payment as a percentage of revenue receipts of NE states is less than the general category states* (see Table 7).

The state government's allocation of their own revenue receipts is another important part to study since it is a common trend in the Indian states that states are burdensome with a huge amount of debt, and their repayment of the interest amount is more than the amount of their own revenue receipts. This refers to a situation when the state governments are using the shared revenue received from the Centre for debt servicing, which is supposed to be used for the developmental expenditure.

To study the state governments' own revenue receipts, excluding the receipts from the Centre and its share allocation for the interest payment, we have calculated the interest payment as a percentage of own revenue receipts. It can easily be understood that when the interest payment as a percentage of own revenue receipts will be more than the own revenue receipts, the state governments must have utilized the revenue receipts from the Centre for interest payment. The Table 8 shows that Tripura spent 133.41% as the average interest payment out of its own revenue receipts during 1991-1995. Similarly, during 1995-2000, there are many states which spent more than 100% - like Manipur (102%), Nagaland (135.96%), and Tripura (118.93%). During 2000-2005, the states that continued to spend more than 100% are Manipur (235.42%), Mizoram (135.53%), Nagaland (209.99%), and Tripura (118.93%). States like Nagaland (123.33%) and Tripura (187.48) continued to spend more than 100% during 2005- 2010. The average calculation for NE states and 14 major states shows that the percentage of interest payment as a percentage of own revenue receipts of NE states is always more than the 14 major general category states.

The Role of Central Grants & Assistance and NE State's Fiscal Discipline

There are several factors which are responsible for unsustainable fiscal imbalances at the state level. On the demand side, fiscal problems of both Centre and States are a result of 'populism' and deficits bias of unstable governments in a democracy. On the supply side, the softening of the hard budget constraint implicit in the constitutional restrictions on borrowing and inadequate oversight on the part of the Centre is responsible (Anand, Bagchi, & Sen, 2001). In this context, the weaknesses of the system of intergovernmental fiscal relations have been argued as a prime source of perverse incentives, leading to fiscal indiscipline in the states. In addition to this, heavy reliance on borrowing to meet their expenditures leads to large deficits in State budgets and their debt overhang causes problems for the macro management of the economy.

It is questionable that why the state governments are incurring large fiscal deficits, even though according to Article 293 of the Indian Constitution, borrowing by States already in debt to the Centre requires the consent of the Central government. Apart from this, the constitution also gives the Centre an upper hand in many other related matters (Dandekar, 1987).

Furthermore, so far as the debt of the NE states is concerned, they get special grants because of their special status, which should create revenue sufficiency and there should not be debt. Therefore, it is important to observe, what encourages these states to borrow to an extent that encumbers their budgets with the burden of debt that they cannot bear on their own? Since it is argued that intergovernmental fiscal relations are a prime source of perverse incentives and lead to fiscal indiscipline in the States, we observe the role of the Central grant in the context of the NE states' fiscal discipline.

✦ **Fiscal Dependency and Fiscal Autonomy of NE States :** It is already observed in the above sections that the NE states are basically dependent upon the Central fiscal transfer. To study the fiscal dependency in more details, we have taken into consideration the percentage of ratio between gross devolution and transfer of resources from the Centre to the States and the states' total expenditure. This shows to what extent the states are dependent upon the Central government.

The Table 9 presents the fiscal dependency of the NE states on the Central government. *It is observed that on an average, the NE states are dependent upon the central government for around 70% of their total expenditure. Looking at the trend of the dependency during 1991 to 2005, the dependency of states like Arunachal Pradesh, Meghalaya, Mizoram, Sikkim, and Tripura had decreased. However, for states like Assam and Nagaland, it had*

Table 9. Fiscal Dependency Ratios* of NE States (%)

State	1991-1995	1995-2000	2000-2005	2005-2008	2008-2009	2009-2010
	Avg.	Avg.	Avg.	Avg.	Total (RE)	Total
Arunachal Pradesh	88	87	72	76	68.24	62.92
Assam	65	68	52	63	64.86	48.88
Manipur	81	77	89	80	76.06	80.02
Meghalaya	77	74	68	69	78.68	69.21
Mizoram	85	82	71	73	76.96	78.49
Nagaland	76	78	81	79	71.41	75.30
Sikkim	65	29	42	39	47.81	46.45
Tripura	83	82	70	84	70.60	64.40
NE States Average	77	72	68	70	69.00	66.00
14 Major States' Average	39	35	28	31	32.00	33.00
Average of All States	43	38	30	34	35.90	35.21

Note: * Fiscal Dependency Ratio = Gross Devolution and Transfers from the Centre / Total Expenditure of the State X 100

Source : Same as Table 8

Table 10. Fiscal Autonomy** of NE States (%)

State	1991-95	1995-00	2000-05	2005-08	2008-09	2009-10
	Average	Average	Average	Average	Total	Total
Arunachal Pradesh	100	100	100	100	100	100
Assam	100	100	100	100	100	100
Manipur	100	100	100	100	100	100
Meghalaya	100	100	100	100	100	100
Mizoram	100	100	100	100	100	100
Nagaland	100	100	100	100	100	100
Sikkim	100	100	100	100	100	100
Tripura	100	100	100	100	100	100
NE States Average	100	100	100	100	100	100
Andhra Pradesh	97.61	88.66	88.59	102.3	103.6	103.14
14 Major States' Average	100	100	100	100	100	100
All States Average	100	100	100	100	100	100

Note: ** Fiscal Autonomy Ratio= (States' Own Revenue + Share in Central Taxes + Total Grants) / States Revenue Expenditure X 100

Source: Same as Table 9

increased. During 1991- 1995, when the states were dependent for 77% of their total expenditure requirement, it decreased to 72% during 1995-2000 and 68% during 2000-2005. Similarly, for 14 major states, the dependency decreased from 39% during 1991-1995 to 28% during 2000-2005.

When it comes to the context of fiscal autonomy, the states should maintain a stable and sound fiscal health. The share of the total own tax revenue and the non tax revenue receipts determine its total autonomy. This being so, the Central government transfer is used to bridge the deficit between revenue requirement and revenue receipts. Therefore, the fiscal autonomy of a state is determined by :

Fiscal Autonomy = States' Own Revenue + Share in Central Taxes + Total Grants received from the Centre

As it is evident from the Table 10, every state is able to maintain fiscal autonomy by equalizing the revenue receipts. Only in the case of Andhra Pradesh, the situation is unique where during 1991-1995, the state had autonomy of 97.61% , which decreased to 88.59% during 2000-2005. After this, the state started to attain a surplus in the subsequent years.

Role of Grants Recommended by Finance Commission (FC) in terms of Gap-Filling Approach in State Government's Expenditure Management (Fiscal Discipline)

The approach of the FC's grant for the federal transfers consists of:

(1) Assessment of overall budgetary requirements of the Centre and states to determine the volume of resources available for transfer with the Centre and required by individual states during the period of recommendation;

(2) Projecting states' own revenues and non-plan current expenditures ;

(3) Distributing assigned taxes, broadly on the basis of origin;

(4) Distributing sharable taxes- the personal income tax and union excise duties between the Centre and the states and among the states inter se.

In addition to the above recommendations, the FC projects revenue and expenditure after tax devolution for each state separately. Calculating the gap between state revenue receipt and the non plan revenue expenditure (NPRE) extends grants to bridge the gap. This can be interpreted as:

The grants (G_i) receivable by the i^{th} state is given by :

$$G_i = E_i - (R_{oi} + R_{ai} + R_{si})\ G_i \geq 0$$

where,
E_i : denotes projected non-plan revenue (current) expenditure of the i^{th} state,
R_{oi} : Projected own revenues of the i^{th} state,
R_{ai} : Projected assigned revenues of the i^{th} state and,
R_{si} : Projected shared taxes of the i^{th} state.

This approach of Finance Commissions is popularly known as the gap-filling approach. Finance Commissions act as the 'fiscal dentist' filling in 'budgetary cavities' so it is also known as fiscal dentistry approach of the finance commissions. In contrast to this, state government's expenditure under revenue accounts is made on two sub accounts such as plan account and non-plan account, and the expenditure pattern follows the following method:

BCR= [Shared Tax from the Centre + States Own Revenue] –Non-Plan Revenue Expenditure

PRE = Balance from Current Revenue + Additional Resource Mobilization + Central Assistance

(1) Balance from Current Revenue (BCR) : The state's own revenue (SOR), which is a summation of tax and non-tax revenue and the shared tax from Centre constitute the current revenue receipt (CRR) of a state. The state spends on plan revenue expenditure (PRE) from CRR, and the remaining is known as balance from current revenue (BCR). The significance of BCR can be realized from the fact that non-plan expenditure is expected to be met out of the revenue from tax and non-tax sources with the base, and the rate structure obtained in the base of a

Table 11 .Balance from Current Revenue (BCR) in ₹ Lakhs

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total(RE)	Total(BE)	Avg.
Arunachal Pradesh	-5996	-11846	-44586	-40739	-36368	-2299	-96361	-98689	-54896
Assam	-36330	-72666	-162369	-66102	-26232	-35029	-344204	-1100365	-314386
Manipur	-11306	-303382	-89087	-109732	-125571	-95006	-123221	-144322	-119570
Meghalaya	-11187	-14996	-48922	-43368	-40476	-44990	-37911	-75144	-48378
Mizoram	-6682	-20922	-66371	-64713.00	-62564	-68822	-90549	-115490	-80428
Nagaland	-21684	-31437	-102872	-118719	-124792	-143865	-163331	-151894	-140520
Sikkim	-4407	-11609	-18811.00	-15400	-7005	2793	-2441	-26288	-9668
Tripura	-15165	-26884	-102247	-121505	104024	-108100	-141135	-209013	-136755
NE States' Average	-14094.62	-61717.75	-53846.37	-72397.25	-39873.00	-61914.75	-124894.12	-240150.62	-11375.12
14 Major States' Average	786	-86247.5	-27456	241662	736038	695884	1361882	1062582	819610

Note:
(I) BCR= State Revenue Receipt(Tax+Non-Tax)-NPRE Source : Same as Table 10
(ii) '-' Indicates Shortage and '+' Indicates Surplus, (iii) The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal

Table 12. NET Balance from Current Revenue (BCR) After Getting Non Plan Assistance from the Finance Commission (₹ in Lakhs)

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total(RE)	Total(BE)	Avg.
Arunachal Pradesh	2262	-4544	-18511	-1,889	2386	35,731	-55633	-66133	-17108
Assam	-17,667	-40,652	-123,232	28717	44638	53537	13950	-883431	-148,518
Manipur	-3,043	-20,452	-44,318	-24807	-34095	1778	-20659	-41591	-23,875
Meghalaya	-5,160	-6,966	-13,393	-2765	6771	1111	6265	-34844	-4,692
Mizoram	1,626	-10,812	-35,315	-3633	3118	-964	-14411	-15002	-6,178
Nagaland	-11,193	-21,249	-15,068	-6222	-12496	-22577	-26171	-11597	-15,813
Sikkim	-3,329	-11,061	0,940	471.	-579.00	11495	4253	-23207	-1,513
Tripura	-4,562	-13,478	-48,584	7183	13172	18861	-15534	-82783	-11,820
NE States' Average	-5133	-16151.75	-37185.13	-368	-2864.38	12372	-13492.52	-144823.50	-28689.63
14 Major States' Average	22125	-81,503	-180,763	165559	413547.9	594511.6	510683.9	304294.78	397,719

Note: i) '-' Indicates Shortage and '+' Indicates Surplus,
ii) The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal
Source: Same as Table 11

plan, and the surplus BCR, if any, is to be deployed for financing the subsequent plan expenditure. So, the plan revenue expenditure is incurred by accumulating BCR, ARM (additional resource mobilization), and CA. Therefore, the trend of BCR plays a key role in determining plan expenditures in the state.

The Table 11 presents balance from current revenue (BCR) of all NE states and 14 major states. From the Table, it can easily be observed that *all the NE states have been having negative BCR since 1991 - 2010*. However, the average comparison between NE states and the 14 major states shows that when all NE states are having negative BCR, 14 major states (in average) are having positive BCR except during 1995-2000 and 2000-2005.

(2) Net BCR After Getting Non-Plan Assistance from the Finance Commission : Even after getting non-plan assistance from the FCs, the states are suffering from negative BCR. The Table 12 envisages that except Mizoram, all other NE states were having negative BCR during 1991- 1995, but during 1995-2000, all NE registered negative BCR. However, on an average, all NE states were having negative BCR over all the time periods. Such a trend indicates that the states must be diverting plan assistance to bridge the revenue gap in the revenue account.

(3) Percentage of Plan Assistance Diverted Towards Non-Plan Revenue Expenditure : As it is already mentioned, the plan revenue expenditure (PRE) is incurred by accumulating BCR, ARM*, and CA. So, the role of BCR and CA, which comes as plan assistance, plays a key role in the context of financing plan expenditures in the states.

The additional resource mobilization by the state governments are negligible or nil, so the pressure is on BCR and CA. But from the Table 12, it is observed that the NE states are accumulating negative BCR because of their exaggerated NPRE and insufficient state own revenue,and shared tax from the Centre. The state government gets the finance commission grant (in terms of gap filling approach) to fill the gap between NPRE and state revenue receipt (SOR + STC), that is, negative BCR. *It has been observed that even after getting the grant from the finance commission, the BCR is not positive.* So, the states must be making BCR zero or positive by diverting plan assistance towards NPRE.

Table 13. Percentage of Plan Assistance Diverted Towards Non-Plan Revenue Expenditure

State	1991-1995	1995-2000	2000-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2005-2010
	Avg.	Avg.	Avg.	Total	Total	Total	Total (RE)	Total (BE)	Avg.
Arunachal Pradesh	8.59	-8.06	-26.33	-2.04	1.61	24.99	-23.60	33.26	-6.46
Assam	-16	-28.97	-57.89	8.57	12.01	13.29	1.82	-95.25	-11.91
Manipur	-12.94	-43.79	-78.81	-23.71	-28.20	1.06	-10.77	-21.17	-16.56
Meghalaya	-24.5	-19.41	-27.98	-4.67	9.23	1.24	3.11	16.41	-1.5
Mizoram	12.89	-30.47	-60.9	-5.60	3.72	-1.22	-11.47	-11.42	-5.2
Nagaland	-46.61	-51.67	-29.95	-9	-11.13	-19.94	19.53	-7.05	-13.33
Sikkim	-25.41	-42.27	3.57	0.97	-1.01	17.53	3.70	-18.79	0.48
Tripura	-17.64	-22.72	-55.96	7.38	10.89	14.60	-9.57	-43.25	-3.99
NE States' Average	4.1	-30.92	-35.19	-3.51	2.53	6.44	-3.41	-18.4	-3.99
14 Major States' Average	37.86	-43.85	-171.65	83.93	129.98	179.01	74.81	20.25	86.81

Note:
(I) '+" indicates surplus in the year and have not been diverted, "-"indicates deficit in the year and plan revenue have been diverted.
(ii) The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal
Source: Same as Table 12

The Table 13 shows that Arunachal Pradesh and Mizoram were the only states having a surplus after having the finance commission grant and there was no diversion of plan assistance during 1991-1995. During this time period, all other states had diverted the plan assistance for spending NPRE. Nagaland is the state which diverted highest (46.61%) of its plan assistance, and Manipur diverted the lowest (12.94%) among all NE states. During 1995-2000, all NE states diverted the plan assistance. Nagaland continued to divert the highest percentage (51.67%), which is more than the percentage of diversion it made in the previous time period. Arunachal Pradesh had surplus during 1991-1995, but diverted 8.06%. It will be worthy to note here that, on an average, all the NE states diverted 30.92% of their plan assistance for NPRE, and similarly, the counted average percentage of plan assistance diversion by 14 major states during this period was 43.85%. The diversion percentage of plan assistance during 2000-2005 for all states increased, except for Sikkim, which had a surplus of 3.57%. During this time period, Manipur diverted around 78.81% of plan assistance for NPRE, even after getting the finance commission grant. The average percentage of plan assistance diversion by the NE states increased to 35.19% when it was 171.65% for the 14 major states. However, 2005 onwards, the plan assistance diversion decreased for all states in the coming years. The average percentage of diversion for all the NE states was 3.99%, but the 14 major states had a surplus of 86.81% during 2005- 2010. Diversion of plan assistance for NPRE indicates that when the plan assistance is used for the NPRE, the plan developmental expenditure must be getting affected.

(4) Shortage for Plan Expenditure : After diverting plan assistance for NPRE, the remaining amount should be used for plan revenue expenditure. Since the NE states are special category states and receive 90% as grant, they should not suffer from revenue scarcity for their plan revenue expenditure. However, it is observed (Table 14) that there are states which suffer from revenue scarcity for their plan revenue expenditure. During 1991- 1995, Nagaland had a deficit of 19.14% for its plan revenue expenditure, which is because of diversion of 46.61% of plan assistance for NPRE. Similarly, during 1995-2000, Assam suffered from 6.07% of deficit, and again, Nagaland continued to suffer from 12.14% of deficit for plan revenue expenditure. During 2000-2005, there are three states such as Assam (37.37%), Manipur (34.26%), and Mizoram (26.91%) that suffered of the deficit. In the time period from 2005- 2010, Manipur suffered from 162.86% of the deficit.

Table 14. Shortage for Plan Expenditure

State	1991-95	1995-00	2000-05	2005-06	2006-07	2007-08	2008-09	2009-10	2005-10
	Avg.	Avg.	Avg.	Total	Total	Total	Total(RE)	Total(BE)	Avg.
Arunachal Pradesh	153.57	87.2	16.34	25.12	85.69	71.27	74.62	-20.88	47.15
Assam	14.31	-6.07	-37.37	70.95	113.32	130.24	31.95	-93.37	50.59
Manipur	102.95	16.31	-34.26	102.76	106.69	253.33	193.38	158.17	-162.86
Meghalaya	41.39	33.08	13.99	14.74	41.43	26.03	33.62	14.01	25.96
Mizoram	80.49	29.96	-26.91	13.49	44.09	20.24	27.34	18.01	24.63
Nagaland	-19.14	-12.14	33.23	48.93	123.08	87.74	51.76	93.79	81.06
Sikkim	55.55	17.21	104.23	66.87	68.05	83.59	98.61	72.64	77.95
Tripura	11.51	27.46	24.43	153.38	173.63	156.84	102.58	46.96	126.67
NE States' Average	55.07	24.12	11.71	62.03	94.49	103.66	76.73	36.16	33.89
14 Major States' Average	2.07	-65.85	-128.79	-0.45	41.22	53.92	-3.73	-32.96	11.60

Note: (i) '-' Indicates Shortage and '+' Indicates Surplus, (ii) The 14 Major States include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal
Source: Same as Table 13

Research Implications and Conclusion

The following are the implications and conclusions that are derived from the present study :

(1) The NE states are basically suffering from increasing revenue expenditure requirements, and at the same time, there is a decline in their own revenue receipts collection, which is because of fall in own revenue receipts. Though, the revenue deficit is not so significant in comparison to the general category states, it is important to note here that this is because a major portion of their revenue expenditure is catered to by the Central fiscal transfer in terms of grants because of their special category status. On an average, the NE states are dependent upon the Central government for around 70% of their total expenditure. In addition to this, even after getting grant from the finance commission, the balance from current revenue (BCR) is not positive.

(2) Though the NE states spend more than 60% of their total revenue expenditure for developmental expenditure, there is a substantial increase in the non plan revenue expenditure. The substantial increase in the revenue expenditure is due to the interest payment both in volumes of liabilities and average rate of interest. It will be worthy to note here, when an increasing share of revenue expenditure is used for revenue expenditure, it creates a vicious cycle between higher interest payments and increasing expenditure, pushing the state into further larger borrowing.

Another principal reason for increase in revenue expenditure is the pay and pension revision. The impact of pay revision has been much more severe on the states than the Central government because the share in salary expenditure in states is higher since the revision has to be extended to aided institutions and local bodies (Rao, Sen, & Jena, 2008). NE states were spending more than 30% of their own revenue receipts for non developmental expenditure like salaries, wages, and pensions.

(3) As it has been observed that there is a diversion of Central plan assistance towards non plan revenue expenditure, the developmental expenditure is getting affected. To meet the developmental expenditure, the NE states are dependent mostly on the Central funding for any developmental activities. Furthermore, there is no additional resource mobilization by these states which, in turn, creates inefficiency in the context of revenue generation.

Policy initiatives should be taken to make these states increase their own revenue and at the same time, the Central government should not only devolve resources ; rather, there should be a mechanism in place to control their non plan revenue expenditure so as to make the plan assistance available for developmental expenditure only. The conclusions derived from our study are almost similar to the observations made by recent studies like Nayak et al. (2013) for Arunachal Pradesh ; Barua et al., (2013) for Assam ; Singh et al., (2013) for Manipur ; "Evaluation of state finances with respect to Meghalaya : A study for the fourteenth finance commission," (2013) for Meghalaya ; Vanlalchhawna (2014) for Mizoram ; Sinha (2014) for Nagaland ; Kundu (2013) for Sikkim ; and Nath and Bhowmik (2013) for Tripura.

Limitations of the Study

Since this study has considered data from 1991 to 2010, the analysis is limited up to 2010. Apart from this, the study has mostly used the compiled data and not the disaggregated data from the root source. Therefore, the accuracy of data at the root level interpretation may differ marginally. However, this study contributes to the literature in the sense that the North Eastern states have not yet received sufficient research, particularly in the field of state finances. Even though these states have been receiving grants, but no significant self-sufficiency has been observed. Rather, the importance of the North East region of India has increased, particularly after the Look East policy of the government.

Scope for Further Research

This study has basically analyzed the fiscal problems of the North Eastern states and has compared the same with 14 major states. Though we have tried to incorporate every important aspect, it is understood that each state is having its own individual problems and constraints at the root level. To recommend the policy for micro economic efficiency at the state level, there is need for further detailed analysis regarding possible sources of resources for increasing states' own revenue receipts, debt management mechanism, and transfer mechanism from the Center to the States.

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