India does need a Fiscal Council

Context:

- The fiscal situation in India has been under severe stress even before COVID-19 and the novel coronavirus pandemic has worsened it.

What is the fiscal situation of Union?

- The fiscal deficit of the Centre in 2019-20 as estimated by the Controller General of Accounts (CGA) was 4.6%, 0.8 percentage point higher than the revised estimate.
- For the 2020-21, even without any additional fiscal stimulus, the deficit is estimated at about 7% of GDP as against 3.5% estimated in the Budget due to a sharp decline in revenues.
- The consolidated deficit of the Union and States could be as high as 12% of GDP and the overall debt could go up to 85%.

What is the criticism with regard to Fiscal Consolidation:

- **Unaccounted Liabilities:** When off Budget liabilities are considered, the situation looks even more alarming.
- **Transparency**: Besides large deficits and debt, there are questions of comprehensiveness, transparency and accountability in the Budgets.
- **Obscure Actions undertaken to keep the liabilities hidden**: These include
  1. Special banking arrangements for covering arrears of fertilizer subsidy
  2. Issuing short-term bonds
  3. Unsecured loans and borrowing from the National Small Savings Fund (NSSF) by the Food Corporation of India towards meeting food subsidy and its arrears.
  4. Financing irrigation projects from the Long Term Irrigation Fund (LTIF) created by the NABARD

5. Financing of railway projects through borrowings from the Indian Railway Finance Corporation (IRFC)
6. LIC buying out the Industrial Development Bank of India and the Power Finance Corporation buying out the Rural Electrification Corporation (REC) and remitting the money to the government as disinvestment proceeds.

- To address the above challenges, **14th Finance Commission** recommended the establishment of an independent Fiscal Council.
- This council should be appointed by and reporting to Parliament by inserting a new section in the FRBM Act.

What is the mandate of Fiscal Council?

- A Fiscal Council is an **Independent fiscal institution (IFI)** with a mandate to promote stable and sustainable public finances The council assist in calibrating sustainable fiscal policy by making an objective and scientific analysis.
- The important tasks of these IFIs include:
  - ✓ Independent analysis, review and monitoring and evaluating of government's fiscal policies and programmes.
  - ✓ Developing or reviewing macroeconomic and/or budgetary projections.
  - ✓ Costing of budget and policy proposals and programmes.
  - ✓ Presenting policy makers with alternative policy options.

What are merits of Fiscal Council?

- **Watchdog of Public Finance:** An unbiased report to Parliament helps to raise the level of debate and brings in greater transparency and accountability.
- **Reduces Populism:** Costing of various policies and programmes can help to promote transparency over the political cycle to discourage populist shifts in fiscal policy and improve accountability.
- **Public Awareness**: Scientific estimates of the cost of programmes and assessment of forecasts could help in raising public awareness about their fiscal implications and make people understand the nature of budgetary constraint.

- **Upholds Spirit of Constitution:** The Council will work as a conscience keeper in monitoring rule-based policies, and in raising awareness and the level of debate within and outside Parliament.
- **International Trend**: According to IMF, there were 36 countries with IFIs in 2014 and more have been established in recent years.

How effective have these institutions been?

- A study by the IMF ("The Functions and Impact of Fiscal Councils", July 2013) shows that countries with IFIs tend to have stronger primary balances and more accurate macroeconomic & budgetary forecasts.
- **In Belgium,** the government is legally required to adopt the macroeconomic forecasts of the Federal Planning Bureau and this has significantly helped to reduce bias in these estimates.
- **In Chile**, the existence of two independent bodies on Trend GDP and Reference Copper Price has greatly helped to improve Budget forecasts.
- **In the U.K**., the Office for Budget Responsibility has been important in restoring fiscal sustainability.
- Cross-country evidence shows that fiscal councils exert a strong influence on fiscal performances, particularly when they have formal guarantees of independence.

Conclusion:

- A Fiscal Council is an important institution needed to complement the rule-based fiscal policy. Of course, it is not a 'silver bullet'; if there is no political will, the institution would be less effective.