CHAPTER IV

THE EXISTING INDIAN BUDGETING SYSTEM FOR DEFENCE

AND

ITS DRAWBACKS

Introduction

The existing Indian budgeting system for defence is "input oriented" and does not lend itself to a detailed analysis, for the use of various resources to assess, whether these have been utilised efficiently to achieve the desired objectives. In most cases, it is not even possible to discern the "activities" on which the expenditure has been incurred. According to Air Commodore Jasjit Singh (Retd), Director Institute of Defence Studies and Analysis (IDSA), the "budget" and the "expenditure" reflect only the value in current prices. There is no indication of the input of inflation and the changes in relative value of the rupee against foreign currencies: He states that "In the ultimate analysis, what is really important is to be able to see the extent of Defence capability that has actually been bought by the allocated budget." ¹

To appreciate the shortcomings of the existing system,

it is important to understand the existing budgeting system for Defence.

**Fiscal Provisions of the Constitution**

The fiscal provisions in Indian constitution concerned with budgetary procedures are as follows:

<table>
<thead>
<tr>
<th></th>
<th>Article</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a)</td>
<td>109-117 and 198-207</td>
<td>Financial procedure in Parliament and State Legislatures</td>
</tr>
<tr>
<td>(b)</td>
<td>264-267</td>
<td>General Principles Regarding the Receipt Custody and Drawl of Public Money</td>
</tr>
<tr>
<td>(c)</td>
<td>268-277 and 7th Schedule</td>
<td>Distribution of Revenue Between the Union and States.</td>
</tr>
<tr>
<td>(d)</td>
<td>280-281</td>
<td>Duties and Powers of the Finance Commission.</td>
</tr>
<tr>
<td>(e)</td>
<td>292-293</td>
<td>Borrowing Powers of the Union and State Governments.</td>
</tr>
<tr>
<td>(f)</td>
<td>360</td>
<td>How to Tackle Financial Emergency.</td>
</tr>
<tr>
<td>(g)</td>
<td>282-291</td>
<td>Miscellaneous Financial Matters.</td>
</tr>
</tbody>
</table>

**Structure of Central Budget**

The Central Budget is set out under Article 112 of the constitution, in an annual financial statement of estimated receipts and expenditure of Govt of India. This is laid
before the parliament in respect of every financial year, which runs from 1st April to 31st March: This Statement titled "Annual Financial statement" is the main Budget document, which shows the receipts and payments of Govt accounts held in:-

(a) Consolidated Fund
(b) Contingency Fund
(c) Public Fund

All revenue received by the Government, loans raised by it, as also its receipts from recoveries of loans granted by it, form the Consolidated Fund. All expenditure of Government is incurred from the Consolidated Fund and no amount can be withdrawn from the Fund without authorisation from the Parliament. The Contingency Fund is an imprest placed at the disposal of the President of India, to meet urgent unforeseen expenditure pending authorisation from Parliament (which is subsequently obtained): The Corpus of Fund currently authorised is Rs 50 Crores. Where the Govt acts as the banker, the money is kept in Public Account. For example, transactions such as provident funds, small savings collection and deposits which are received by the Govt and paid back to the claimants at later stage, the money is kept in "Public Account". Parliamentary authorisation for payments of Public Account is not essential.
Principles Underlying Preparation of Budget

The following principles are generally observed in preparation of budget:

(a) The budget should be balanced.
(b) The estimates should be on cash basis.
(c) There should be only one budget for all financial transactions. An exception is however made in the case of Railways: A separate Railway Budget is presented before the Parliament by the Railway Minister, a few weeks before the presentation of the General Budget.
(d) Budgeting should be 'gross' and not 'net'. The gross transactions in the case of both receipts and expenditure of each department, are shown separately. It is not permissible to deduct receipts from charges and frame the budget for net expenditure only. This is to ensure Legislature's control over Government expenditure.
(e) Estimating should be close.
(f) Budget should be on annual basis.
(g) The rule of 'Lapse': All appropriation accounts are made up and balanced and the surpluses/deficits are ascertained for each year. The funds not realised during an year lapse.
(h) The form of estimates should correspond to that of accounts since estimates, are but anticipated accounts.
Presentation of Budget

The various stages for the presentation of budget in the Legislature are:-

(a) Presentation of Budget by the Finance Minister in both the Houses.
(b) Presentation of Demands for Grants.
(c) Voting of Grants.
(d) Presentation, Voting and Passing of the Appropriation Bill.
(e) Presentation, Voting and Passing of the Finance Bill.

Revenue and Capital Budgets

The Govt Budget comprises of Revenue and Capital Budget. The salient details are :-

(a) Revenue Budget. The Revenue Budget consists of revenue receipts of the Govt and expenditure met from these. Tax revenue levied by the Union Govt, interest, dividend on investments, fees and other receipts for services rendered constitute the 'revenue receipts'. 'Revenue expenditure' is the expenditure incurred on running the Govt Departments, interest charges on debt
and grants given to the State Governments. Broadly speaking, expenditure which does not result in creation of assets is treated as revenue expenditure.

(b) **Capital Budget.** Capital Budget consists of capital receipts and payments. The main items of capital receipts are market loans raised by Govt from Public, borrowing by Govt from Reserve Bank, loans received from foreign Governments and Bodies and recoveries of loan allotted to State Governments and Union Territories. Capital Expenditure comprises expenditure on acquisition of assets like land, buildings, or military hardware costing more than Rs 2 lakhs and having a life of more than 7 years.

**Demands for Grants**

Estimates of expenditure from the Consolidated Fund included in the Annual Financial Statement and required to be voted by the Lok Sabha, are submitted in the form of Demands for Grants, under Article 113 of the Constitution. Certain items of expenditure, like the emoluments of the President, salaries and allowances of the Chairman, Deputy Chairman of the Rajya Sabha and Speaker and the Deputy Speaker of the Lok Sabha, salaries, allowances and pensions of Judges, of the Supreme Court and the Comptroller and Auditor General of India, interest on and repayment of loans
raised by Government and payments made to satisfy decrees of courts, etc, are charged on the Consolidated Fund and are not required to be voted by the Lok Sabha. The Annual Financial Statement, shows the expenditure charged on the Consolidated Fund separately.

Generally, one Demand for Grants is presented in respect of each Ministry or Department. However, in respect of large Ministries or Departments, more than one Demand is presented. Each Demand normally includes the total provisions required for service: that is, provisions on account of revenue expenditure, capital expenditure, grants to State and Union Territory Governments, as also loans and advances relating to the service. The demands for grants are presented to the Lok Sabha, along with the Annual Financial Statement. Each demand gives the totals of "voted" and "charged" expenditure the "revenue" and "capital" expenditure and also the grand total of the amount of expenditure, for which Demand is presented. This is followed by the estimates of expenditure under different major heads of account. The break-up of the expenditure under each major head between "Plan" and "Non-plan" is also given. The amounts of recoveries taken in reduction of expenditure in the accounts are also shown.
Finance Bill

The proposal of Government for levy of new taxes, modification of the existing tax structure or continuance of the existing tax structure beyond the period approved by the Parliament are submitted to Parliament, through the Finance Bill.

Appropriation Bills

After the Demands for Grants are voted by the Lok Sabha, Parliament's approval to the withdrawal from the Consolidated Fund of the amounts so voted and the amount required to meet the expenditure charged on the Consolidated Fund, is sought through the Appropriation Bill. Under article 114(3) of the Constitution, no amount can be withdrawn from the Consolidated Fund without the enactment of such a law by the Parliament.

The process of detailed consideration of the Demands for Grants, is not completed before the commencement of the new financial year. To enable Government to carry-on its normal activities from 1st April of the year till such time as the Appropriation Bill is enacted, a Vote on Account is obtained from the Parliament, through an Appropriation (Vote on Account) Bill.
The budgetary requirements for the Defence Services, are included in the following five Demands for Grants presented to the Parliament:—

(a) Demand No 18, Defence Services - Army.
(b) Demand No 19, Defence Services - Navy.
(c) Demand No 20, Defence Services - Air Force.
(d) Demand No 21, Defence Ordnance Factories.
(e) Demand no 22, Capital Outlay on Defence Services.

The requirements for the Civil expenditure of the Ministry of Defence Secretariat, Defence Accounts Department, Canteen Stores Department, etc, including share capital contributions made/loans advanced to Defence Public Sector Undertakings and Defence Pensions, are provided— for in two separate Civil Demands, for Grants of the Ministry of Defence. The requirements of the Coast Guard Organisation and the Border Roads Organisation, are provided for by the Department of Revenue and the Ministry of Surface Transport, respectively.

The running or operating expenditure of the three Services and other Departments are provided for under the
first four Demands, which cater to the Revenue expenditure, while the fifth, viz. Capital Outlay on Defence Services caters to the expenditure incurred on buildings or acquiring durable assets. The first Demand (Defence Services-Army) caters to the revenue expenditure of Army, NCC, R&D and DGQA.

The Revenue expenditure includes expenditure on pay and allowances, transportation, Revenue Stores (like rations, petrol, oil and lubricants, spares, etc), Revenue Works (which includes maintenance of buildings, water and electricity supplies, rents, rates and taxes, etc) and other miscellaneous expenditure. The Capital expenditure includes expenditure on land, construction works, plant and machinery, Naval Vessels, etc.

Approval of Parliament is taken for the 'gross' expenditure provision under different Demands for Grants. Receipts and Recoveries, which include items like sale proceeds of surplus/obsolete stores, receipts on account of services rendered to State Governments/other Ministries, etc and other miscellaneous items, are deducted from the gross expenditure to arrive at the net expenditure on Defence Services. What is accepted in common parlance as the Defence Budget, is the net expenditure thus arrived at.
The Budgeting Process

The Indian media goes on routinely questioning the Services as to why the maintenance costs of a 1.1 million strong, manpower intensive organisation like the Army are increasing year after year, when it is apparent that most of the administered prices of daily consumable, of railway and Air freight, of most vital construction material like steel and of necessary grades of fuel and lubricants have been rising steeply. The Defence budget, which has to cater for personnel costs as well as equipment costs, is structured in a manner which makes interpretation on a functional basis rather tricky. For example, if one were to question the present level of financial investment in the nation's air defence, one would have to undertake a separate study, just to arrive at a rough estimate of the cost of existing assets relevant to air defence, that are held by the three Services. To assess any cost benefit of an increment to such assets would be a far cry under the present system of budgeting and accounting for Defence expenditure.

The budgeting calendar runs as under :-

(a) "Forecast Estimates" for the ensuing financial year are submitted by Service Headquarters by 10 November.
(b) "Budget Estimates" for the ensuing year are sent by 20 December.
(c) "Budget" is presented to the Parliament by the Finance Minister on the last day of February.
(d) "Vote on Account" for two months expenditure, is passed by the Parliament during March/April.
(e) "Final vote" for the budget for the full year is taken during May.
(f) A "Preliminary Report" after reviewing the trend of expenditure in the first three months is sent by Service Headquarters by 20 August.
(g) A "Preliminary Revised Estimate" based on the review of the first six months is forwarded by 10 November.
(h) Revised Estimates are forwarded by 20 December and are reflected in the budget proposals alongside Budget Estimates for the ensuing year.
(j) "Modified Appropriations" for the current year are sent by 10 March.
(k) The actual expenditure is known only after the final closing of accounts in August/September of the following year.

As a result of these periodic reviews, it is possible to submit additional requirement of funds, either by way of re-appropriation from a budget head showing less expenditure
or as a supplementary grant, which can be voted by Parliament (when in session). For re-appropriation within a sanctioned head, Ministry of Defence can give the necessary sanction. It must be noted, that the data on which such reviews of current expenditure and forecasts of future requirements can be based, are the computerised compilations of monthly expenditure under each budget head brought out by the Comptroller General of Defence Accounts, which becomes available about four to six weeks after a month's accounts have been tallied.

Even though the Defence budget continues to demarcate expenditure under "Revenue" or "Capital" expenditure categories, it is a general practice to consider it as "Maintenance" and "Modernisation". This affects acquisition of modern weapon systems and other hardware, because it can either be a replacement of a worn-out item in service or a new induction necessitated mostly by the acquisition of a similar item by the enemy. The international arms trade thrives on feeding the fears of the Third World countries, who are the biggest importers of such wares.

Whereas the concept of Parliamentary responsibility and process of Defence Policy has seen shuffles and adjustments, much of Defence policy is also constrained by certain routine financial and budgetary procedures, as also the avail-
ability of economic resources, especially in foreign exchange. Primarily, it is the concern of the branches at the Service Headquarters to prepare the estimates, utilising the data supplied by the lower formations and their own plans. After initial discussions and vetting by the Ministry of Defence, these are discussed with their accredited Deputy Financial Adviser (Budget), who is the main co-ordinating authority. He scrutinises the estimates with reference to the trend of actual expenditure, major policy decisions bearing on the budget and general directions by the Ministry of Finance.

It may be recalled, that although the Central Budget including the Defence Budget is presented by the Finance Minister, it is the Defence Minister assisted by the Secretary - Defence and the Financial Adviser, who are responsible for defending and justifying the Defence demands before the Parliament.

Once the Appropriation Act is passed, funds are available for expenditure. Progress of expenditure is maintained by the controlling officers in the various formations, the Service Headquarters, the Ministry of Defence and the Ministry of Finance (Defence).

The various Heads of accounts are broadly divided into
'Centrally Controlled' and 'Locally Controlled' Heads: Expenditure coming under the Centrally Controlled Head is mostly of obligatory nature, viz., pay and allowances, procurement of stores through DGS&D, equipment and weapons from abroad, etc. The expenditure is governed by policy decisions at higher levels and the expenditure against grants for these items is monitored by the Ministry of Defence and Service Headquarters respectively. Expenditure under locally controlled heads is controlled and regulated by the lower authorities, as it pertains to items like employment of temporary labour in store depots, local purchase of stores, maintenance of buildings, field firing, technical training, miscellaneous expenditure, etc.

A 'five tier classification' has been adopted for classification of expenditure in budget, accounts and plan, namely:–

(a) Sectoral classification.
(b) Major Head classification.
(c) Minor Head classification.
(d) Sub-Head classification, and
(e) Detailed Head classification.

Under Major Head, Capital outlay is compiled expenditure on construction of accommodation, purchase of Naval vessels (but not aircraft which are treated as weapon sys-
tems charged to Revenue account), advance stock pilling of stores, etc.

The expenditure under different heads actually in­curred, is reported in the Appropriation Account. However, the Appropriation Account in case of the Defence Services is prepared by the Financial Adviser (Defence). In case of other ministries, except those of some departments like Defence, Railways and Public Undertakings, the Appropriation Account is prepared by Comptroller and Auditor General.

The Financial Adviser functions in a dual capacity, as the principal representative of the Ministry of Finance in the field of Defence expenditure and the Chief Accounting Officer for the Defence Services. The Financial Adviser is also the administrative head of the Ministry of Finance (Defence). This division is in close and continuous touch with the Defence Ministry and with the various branches of the Service Headquarters. As it is under the Minister of Finance and forms part of the Ministry of Finance, it retains its essential independence. Thus, the functions of the Ministry of Finance (Defence), is therefore both of an advisory and of a controlling nature: The main purpose is for safe-guarding of economic efficiency and propriety in public finance.
The Controller General of Defence Accounts (CGDA) is the head of the Defence Accounts Department. It authorises payment of salaries, other payments, etc., maintains all the accounts related to defence services, does the internal audit and supplies and compiles figures to the administrative and financial authorities for the purpose of budgeting and control of expenditure. While the CGDA maintains most of Defence Accounts and also does an internal audit, the C and AG, in exercise of his statutory authority does `test audit'.

Thus, Defence budgeting is a means of considering next year's plans and targets in fiscal terms and for monitoring actual results with a view to applying correction in time. In practice, however, the traditional Defence budgeting system neither provides the information required to evaluate the various budget proposals, or a satisfactory basis for evaluating the subsequent performance. Typically, they are prepared by adjusting the rate of inflation to the previous year's actual cost and adding the cost of new programme and services. The base therefore, remains last year's spending level, usually accepted without examination. The test of a good Defence budget, thus becomes the test of budgeting skill rather than the performance.
Major Weakness of Existing Budgeting System

The existing Defence budgeting system is input oriented and enables only the control of expenditure. It does not reflect the resources utilised by a particular establishment or a unit, with the result that the cost of services provided is not known. There is no linkage between the resources utilised and the results achieved. Since the cost of achieving any activity is not reflected, there is no initiative or incentive for better and economical management of resources. There is therefore, no accountability for the efficient use of funds. Since costing of activities and unit is not part of the system, no economics can be exercised to effect savings.

The present budgeting system does not permit decision makers with adequate information, on alternative choices and substitution. While the present method of debiting the expenditure in current terms, may be suitable for budgeting and management of expenditure, its value in real terms must be indicated concurrently in the budget, to take objective view of resources commitment and the capabilities that are expected to be achieved. Some of the points in this regard are:

(a) Bids for funds are forwarded by lower formation in the form of Budgetary Estimates, mainly based on past
trends. Logically, these should be derived and determined by the targets to be achieved in the coming financial year.

(b) Quite often, the liabilities to be carried forward cannot be taken into account, since a clear-cut picture is not available to the estimating authorities.

(c) In the absence of an effective Management Information System (MIS), feedback and data on expenditure/cash outgo is not fully available to sanctioning authorities, thereby depriving them of effective control.

Present Management Information System
All India Compilation

Presently, "All India Compilation" is prepared by CGDA, indicating progressive expenditure under Minor Head, Sub Head & Detailed Heads. This does not indicate activity-wise expenditure, nor does it reflect the expenditure of any particular unit. This is inadequate for any decision making and can be only used for monitoring the progressive expenditure.