

UPSC Civil Services Examination

UPSC Notes [GS-III]

Topic: Fiscal Policy - UPSC Economy Notes

What is Fiscal Policy?

Fiscal Policy deals with the revenue and expenditure policy of the Govt.

The word fiscal has been derived from the word 'fisk' which means public treasury or Govt funds.

This is an important topic for the [IAS Exam](#).

Tools of fiscal policy:-

- Taxation
- Public expenditure
- Public debt
- Plan and Non-Plan Expenditure

Public Debt means debt on the Govt -It is accumulated borrowing of the Govt

Components of Public Debt

- Internal Debt or liabilities
- Other Liabilities
- External debt

Types of Govt. funds

- Consolidated Fund of India
- Contingency Fund
- Third Fund also called Public accounts

To know more about the different [government funds](#) in detail, refer to the linked article.

Debt Trap – Situation where the borrower has to borrow again for the payment of an instalment on the previous debt. A borrower unable to meet debt service obligations without borrowing is known to be in debt trap.

Fiscal Responsibility and Budget Management Act (FRBMA), 2003

The objective of this [FRBM Act](#) is to impose fiscal discipline on the government.

It means fiscal policy should be conducted in a disciplined manner or in a responsible manner i.e. government deficits or borrowings should be kept within reasonable limits and the government should plan its expenditure in accordance with its revenues so that the borrowing should be within limits.

Targets under this FRBM Act

- Fiscal deficits should be less than 3% of GDP or less by 2008
- Fiscal deficit should be reduced by 0.3% point per annum
- In 2004 the fiscal deficit was slightly above 4.3% and further reduces considerably by 0.3% every year.
- Revenue deficit must be 0 by 2009. It can be achieved by reducing revenue deficit by 0.5% points per annum.
- Government should not borrow directly from RBI.
- Government has to present the trends of receipts and expenditure in Parliament on a quarterly basis.

Fiscal Federalism

It refers to the distribution of resource between centre and states.

Distribution of taxes between centre and states is mentioned in the 7th schedule of our constitution.

There are 3 lists where the taxes are distributed

- Union List
- State List
- Concurrent List

Taxes are classified under 5 categories

- Central taxes or Central Govt. Taxes
- Shareable taxes – Income tax and Union Excise duty
- State taxes
- Taxes imposed and collected by Centre and appropriated by the state
- Taxes imposed by centre but collected and used by state – Stamp duties and agriculture properties.

This 5 classification arrangement has been amended and the last two categories have now been merged. Now they are called central shareable taxes. 10th Finance commission headed by K.C. Pant recommended these amendments.

By the 80th constitution amendment in 2003, the first two taxes were merged leaving all taxes shareable.