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Page 8. GS II (International Relations)

Economic speed bumps yes, but no breakdown

Nepal's vulnerability is linked to the lack of pragmatic policy interventions and abrupt moves towards self-sufficiency

K.V. RAJAN & ATUL K. THAKUR

Nepal's economic challenges are real, but suggestions that it is already in deep crisis and may be going the Sri Lanka way are probably premature, unfair and unjustified. The surging trade deficit remains a big concern as it is expected to reach $18 billion this fiscal year. A Balance of Payments (BoP) deficit and a spiralling debt liability will pose a very grave risk to the economy that is already in deep trouble. Nepal's central bank statistics show the country's inflation averaged 7.14% in the current fiscal, which is the highest in the last 67 months.

Emerging scenario

There are other worrying trends. The country's debt to Gross Domestic Product (GDP) ratio has crossed over 40% as of the second quarter of the current fiscal year. What is needed is a prudent fiscal management plan. So is the need to boost demand and empower Micro, Small and Medium Enterprises (MSMEs) with soft institutional liquidity support. To emerge from the shocks caused by the BoP deficit to the tune of NR258.64 billion, the decrease in remittance inflow and the fall in the country's foreign exchange reserve by 16.3% to NR1,171 billion (in mid-March 2022 from NR1,399.03 billion in mid-July 2021), industry needs hand holding by the government and a rationalisation of taxes. Such a collaborative effort will help in increasing national economic productivity and mitigating the systemic risk on the economic front.

A lack of pragmatic policy interventions in Nepal and an abrupt move to reorient economic planning towards 'self-sufficiency' has exposed the structural vulnerability of Nepal's economy. It is also true, and unfortunate, that Nepal's economy is overtly politicised. Tensions between the Finance Minister, Janardan Sharma, and the Governor of the Central Bank, Maha Prasad Adhikari, with Mr. Sharma suspending Mr. Adhikari for alleged failures in discharging his responsibilities have undoubtedly contributed to the uncertainty. Mr. Adhikari has been reinstated on orders by the country's Supreme Court, but the damage has been done.

In the short run, the government's revenue and expenditure should be assessed for minimising the establishment cost. Especially so, it is needed for provincial governments where the operational part must be dealt with frugally to not burden the economy beyond a point. While several drastic measures such as an import ban on luxury goods and reducing working hours have been announced, these have not quite succeeded in allaying fears of an impending crisis. The ban on imported goods that have no competent alternatives in the domestic market will only hurt the economy until the production of domestically-consumable goods is increased. Fortunately, there are some positive signs of an economic recovery appearing, with tourism picking up thanks to the easing of visa and entry restrictions and foreign remittances also showing an upward trend. These need to be consolidated.

India will, undoubtedly, go the extra mile to help Nepal ensure a speedy and comprehensive recovery. India has not hesitated in being generous and in coming to Sri Lanka's help despite political considerations which might have suggested other approaches. In Nepal's case, Prime Minister Sher Bahadur Deuba is a known friend of India who likes to accord priority to development rather than playing to the political gallery.

His recent visit to India was successful in terms of reaching an important understanding on economic cooperation projects. It should be possible for Nepal to expect generous Indian support for its economic recovery to be based on broad-based consensus in Nepal which will also eventually help in resolving bilateral irritants that keep cropping up every now and then.

What Nepal's national economy is facing today is a sort of crisis in the making.

Of late, the government is finding it difficult to overlook the difficult trade deficit but unfortunately with wrongly-placed measures such as curbing the autonomy of the Nepal Rastra Bank (NRB) and vilifying import per se instead of making interventions for much-needed structural economic reforms. The NRB underlines problem areas such as rising inflation, BoP deficit, decreasing remittance inflow, depleting foreign exchange reserves and burgeoning imports beyond an acceptable level. The NRB's projection of a looming crisis has no takers in the Finance Ministry – that is on making strange short-term provisions rather finding the way out to avert a crisis in making.

Nepal is in dire need of augmenting its preparedness on the domestic economic front along with a need-based infrastructural haul to impart the right momentum to an economy that is overtly politicised and not inspiring enough for big business ideas to prevail and flourish. Nepal's political economy should get the traction of national consensus to fulfil the aspirations of the people and also reposition the country to the global state with its strengthened economic prowess.

To not give an adverse response to the usual flow of goods and services, the government should lift the ban on imported goods which do not have competent alternatives in the domestic market. Until such time as Nepal makes a move to increase the production of domestically-consumable goods and end the cartel of businesses embracing competition and innovations, it would be helpful if Nepal remains open to successfully complete a mandatory transition of present sort.

There is no magic wand to ensure economic reforms and avert a crisis-like scenario. Nepal's neighbour and the world's largest democracy, India, is a fine example of a country that braved a severe BoP crisis in 1991 and transformed the economy through a sustained wave of economic reforms without letting political preferences override significant economic matters. In the time when isolation cannot steer the growth impulses of the economy, it is important for Nepal to cope with the shortage of industrial production and pressure of trade imbalance through excessive imports but without stopping to remain open to the world for healthy collaboration.

Geopolitical changes

The broad geopolitical and economic trends are also suggestive of doors opening to more active Nepali participation in the Indo-Pacific economic agenda, with the Nepalese Parliament approving the $500 million Millennium Challenge Corporation (MCC) grant from the United States; this could substantially upgrade energy cooperation between India and Nepal, and also India agreeing to the United Kingdom, the European Union and other major investment partners working together in third countries on development projects. Interestingly, the Nepalese seem to have independently made a reassessment of risks in recklessly deepening ties with China, thanks in large measure due to Beijing's missteps, and the style and the substance of Chinese-delivered assistance.

There is much greater receptivity and a "felt need" across the political spectrum and in public discussion of the genuineness of India's friendship aimed at contributing to the welfare of people of Nepal. The decision of the Government of India to set up an inter-ministerial standing group under the chairmanship of the Foreign Secretary, to coordinate sections and ensure more rapid follow-up of project decisions is also a welcome step.

Business leaders in India should be encouraged to be proactive in looking for new opportunities in expanding and diversifying trade and investment ties with Nepal including exploring possibilities in the context of a reset of supply chains in the post COVID-19 situation. There is no doubt that the economic challenges in the post COVID-19 situation, and the overall churning in the geopolitical environment have created an opportunity for both countries to devise innovative approaches to long-standing issues and to aim for new horizons in bilateral cooperation.

It is vital that Nepal deepen its economic ties with India and facilitate joint ventures that create immense economic opportunities. India's unwavering commitment to peace and prosperity in Nepal and its complementarity in its relations with Nepal will help in creating a healthier economic ecosystem in Nepal. While the economic scenario is troubled – and it is unlikely that Nepal will emerge from it soon – it would be wrong to assume that a condition akin to a breakdown is inevitable in Nepal. Economic adversity has created the space for course correction and Nepal should be encouraged to devise a fresh approach to achieve this through calibrated efforts.

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Nepal - Surging trade deficit expected to reach $18 billion this fiscal year. Balance of Payments (BoP) deficit and a huge debt liability are serious dangers for Nepal. Nepal's debt to GDP ratio has gone over 40%.

Need is to empower the MSMEs and give them liquidity support. An abrupt move towards 'self-sufficiency' has exposed the structural vulnerability of Nepal's economy. Nepal's economy is overtly politicised with tensions between the Finance Minister and the Central Bank Governor.

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luxury goods and reducing working hours have been announced, but have been unsuccessful.
Some positive signs - Tourism picking up due to easing of visa restrictions and foreign remittances also showing an upward trend. India has been generous towards Sri Lanka and should do the same in case of Nepal.

Nepal's crisis is its own making - curbing the autonomy of Nepal Rastra Bank and banning exports was a bad step. The central bank points towards the problems of inflation, BoP deficit, decreases remittances, etc – but govt never took it seriously. Government should lift the ban on imported goods which do not have competent alternatives in the domestic market. India's BoP crisis of 1991 is a good example to learn from – transforming economy without political reforms won't succeed.
Nepal is now starting to play a more active role in Indo-Pacific as well, with the Nepalese Parliament approving the $500 million Millennium Challenge Corporation (MCC) grant from the USA, signalling a move away from China. India has set up an interministerial standing group under the chairmanship of the Foreign Secretary, to coordinate sections and ensure more rapid followup of project.

Beyond the Writeup: India Nepal Outstanding issues

Efficient connectivity with India is topmost on Nepal's agenda. During his visit, Deuba and PM Modi virtually inaugurated the India financed Kurtha-Jayanagar passenger railway. The railway is to be extended to Dhalkebar in Nepal. Air connectivity - Nepal requested India to provide three additional entry routes and also requested an agreement on near-border operation for the Gautam Buddha International Airport. The airport, located less than 10 kilometers from the Indo-Nepali border, will start operations from May 20.

Nepal became an energy surplus country (during monsoon) in July 2021. As a result, it started selling 39 MW of electricity to India via the Indian Energy Exchange. Energy trade is mutually beneficial to both countries. The trade enables Nepal to sell the surplus energy it produces and opens up an opportunity for it to reduce the burgeoning trade deficit with India which is close to $5 billion. The Joint Vision Statement on Power Sector Cooperation, which was issued during Deuba's visit, could also form a key stepping stone to subregional energy trade between Bangladesh, Bhutan, India and Nepal (BBIN).

There is also debate about the Millennium Challenge Corporation (MCC) $500 million grant from the U.S. to improve Nepal's power and road networks. Indo-American interests do not converge as much in dealing with small South Asian countries as they converge in their concern of rising China. Thus, India has concerns about increased US. influence in Nepal, as it could lead to a relative decline in its influence.

Page 8. GS III (Economic Development)

Inevitable increase

The RBI's increase in interest rates was long overdue

The penny has dropped. After stubbornly holding off from acting to tame inflation, which has steadily eroded consumers' purchasing power and derailed broader economic momentum, the RBI's rate setting panel on Wednesday announced an 'off-cycle' increase in benchmark interest rates. The Monetary Policy Committee voted to raise the policy repo rate by 40 basis points to 4.4% with immediate effect. RBI Governor Shaktikanta Das rationalised that letting inflation remain elevated at current levels for too long risked 'de-anchoring inflation expectations' and consequently hurting growth and financial stability. While Russia's invasion of Ukraine and the subsequent western sanctions on Moscow have roiled the outlook for prices on a range of commodities, including wheat, edible oil, crude oil and coal, Indian households' perception and expectations of inflation have been running well above the RBI's upper tolerance threshold of 6% for more than two years. That the RBI has been forced to act now, after insisting that price pressures were 'transitory', is a belated yet welcome acknowledgment that the economic costs of failing to anchor price stability can potentially be far more deleterious to growth than a relative decrease in the availability of low-cost credit. To cite Mr. Das: "Sustained high inflation... hurts savings, investment, competitiveness and output growth. It has pronounced adverse effects on the poorer segments ... by eroding their purchasing power."

In explaining its decision to raise borrowing costs for the first time in 45 months, the MPC has acknowledged that the overall outlook for inflation has darkened considerably since it met last month. Prices are on a tear globally and inflationary pressures are broadening worldwide. The IMF last month posited that the war in Ukraine was poised to not only slow global growth in 2022 but would also cause inflation to accelerate by 2.6 percentage points to 5.7% in advanced economies this year, and spur a more appreciable quickening of 2.8 percentage points in the case of emerging market and developing economies. With central banks in advanced economies led by the U.S. Federal Reserve pursuing a path of policy normalisation, the prospects of volatility in capital flows adding pressure on the exchange rate and consequently heightening the risks of imported inflation have also surely queered the pitch for the RBI. The fact that the novel coronavirus is still lurking and it could trigger a fresh wave of infections, as seen in China, adds considerably to the uncertainty. Monetary authorities have also rightly pointed to the impact that the increases in domestic pump prices of petroleum products have had on inflation. The onus is now squarely on the RBI and fiscal authorities to move in lockstep and take every possible measure including cutting fuel taxes to keep inflation from running away and landing the economy in stagflation.

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RBI governor said, "Sustained high inflation... hurts savings, investment, competitiveness and output growth. It has pronounced adverse effects on the poorer segments ... by eroding their purchasing power."

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Beyond the Writeup: Why Monetary Policy Committee & how Repo rate impacts the economy?

MPC is a statutory and institutionalized framework under the Reserve Bank of India Act, 1934, for maintaining price stability, while keeping in mind the objective of growth. The Governor of RBI is ex-officio Chairman of the committee. The MPC determines the policy interest rate (repo rate) required to achieve the inflation target (4%). An RBI-appointed committee led by the then deputy governor Urjit Patel in 2014 recommended the establishment of the Monetary Policy Committee.

Repo Rate: Rate at which the central bank of a country (RBI in case of India) lends money to commercial banks in the event of any shortfall of funds. Here, the central bank purchases the security.

Reverse Repo Rate: Reverse repo rate is the rate at which the RBI borrows money from commercial banks within the country.

Marginal Standing Facility (MSF) Rate: MSF is a window for scheduled banks to borrow overnight from the RBI in an emergency situation when interbank liquidity dries up completely.

Inflation: An accommodative stance means the MPC is willing to either lower rates or keep them unchanged.

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Inflation control needs another model

Lasting inflation control would require placing agricultural production on a steady footing

PULAPRE BALAKRISHNAN
& M. PARAMESWARAN

Koyambedu market in Chennai. B. JOTHI RAMALINGAM

Inflation is back as a talking point in the public arena, some would say belatedly, for wholesale price inflation has been in the double digits for over 12 months. India's official measure of inflation, the rate of change of the consumer price index, has now breached the Reserve Bank of India (RBI)'s upper target of 6% for three months continuously. At the conclusion of the April meeting, the Monetary Policy Committee had already warned that the focus will henceforth be on inflation. Yesterday it raised the repo rate somewhat sooner than was expected by the market.

It may appear contradictory to ask whether the RBI's stated policy of 'inflation targeting', implemented through changes in the interest rate, can control inflation, but we show here why that would be justified.

Discourse on inflation

The discourse on inflation engaged in by Western central banks, which has been adopted in toto by their Indian counterpart, is so abstruse that it is not understood even by many economists. So, we begin with an explainer.

The starting point of this discourse is that inflation reflects an excess of output over its 'natural' level. Inflation targeting refers to the policy of controlling inflation by raising the interest rate over which the central bank has control, i.e. the rate at which it lends to commercial banks, the so-called 'repo rate'. This, it is argued, will induce firms to stay their investment plans and reduce inventories, lowering production. As economy-wide output declines, becoming equal to the natural level of output, inflation will cease. This story does not just legitimise a policy of output contraction for inflation but sees it as optimal. The natural level of output itself is the productive counterpart of the natural level of employment, the level that obtains in a freely functioning labour market. So, at the natural level of output, the economy is deemed to be at full employment.

It is left unstated, but salient in the context, that the natural level of output is unobservable. Hence inflation as a reflection of an "overheating" economy is something that must be taken on trust. Surely it is disturbing that India's official model of inflation control is based on so unscientific a foundation. At least, the view of inflation that had ruled the central banks of the west before they adopted inflation targeting was based on something tangible, namely, the growth of the money supply.

Not surprisingly for a theory based on an unobservable variable, the proposition that inflation is due to an overheating economy fares poorly when put to a statistical test for India. We are not aware of a single demonstration of the empirical validity of the model of inflation presented in the RBI report of 2014, which recommended a move to inflation targeting. On the other hand, in our published research, we explain inflation in India in terms of the movement of the prices of agricultural goods and, to a lesser extent, imported oil. The implication of this finding is damaging for the claim that monetary policy can control inflation, for neither the price of agricultural goods nor that of imported oil is under the central bank's control. The only route by which monetary policy can, in principle, control inflation is by curbing the growth of non-agricultural output, which would in turn lower the growth of demand for agricultural goods. As the demand for agricultural goods slows, so will inflation, but this comes at the cost of output and employment. At least, this is the theory. Whether this takes place in practice depends upon the extent to which changes in the repo rate are transmitted to commercial bank lending rates.

Agricultural goods prices

The implication for the policymaker that inflation is driven by agricultural goods prices, as is the case in India presently, is that the focus should be on increasing the supply of these goods. This could be a win-win solution, for as agricultural production grows faster, the economy expands without inflation. Ideally, food prices should decline, for the consequent rise in demand for other goods will propel the economy forward. But the product mix of agriculture becomes relevant here. Growing per capita income in India has shifted the average consumption basket towards foods rich in minerals, such as fruits and vegetables, and protein, such as milk and meat. But the expansion of the supply of these foods has been lower than the growth in demand for them. So a concerted drive to increase the supply of food other than rice and wheat holds the key. There was a time when the leadership of the RBI understood this, but now its leadership appears unwilling to acknowledge native wisdom.

Increasing agricultural supply at steady if not declining prices is not going to be easy for political reasons. The States have not shown themselves to be particularly sensitive to the charge that they do little to ensure a supply of cheap food for the rest of the country, or even themselves in some cases. When they do produce surpluses, their only concern is that these be procured by the central government at the highest price. The stances of the leaders of wheat-producing northern States and rice-producing southern ones reflect this. Under these circumstances, a nation-wide project for producing food cheaply remains a distant dream. Now that the farm laws have been repealed, it is the time to initiate a discussion on how such a project can be taken forward. Costly food threatens the health of the population, as people economise on their food intake, and holds back the economy, as only a small part of a household's budget can be spent on non-agricultural goods.

Monetary policy manouvres, typified by the RBI's raising of the repo rate yesterday, is not an efficient solution for an agricultural price-driven inflation. Any lasting inflation control would require placing agricultural production on a steady footing, with continuously rising productivity. This would require a re-orientation of farm policy. Since the time of the Green Revolution, the focus has been on raising output, that too of the superior cereals. The inflation caused by continuously rising procurement prices for these crops and slow growth elsewhere in the food-producing sector has been swept under the carpet. The time has come to end this folly. Until then, inflation targeting by a committee accountable to no one will remain a charade.

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Inflation is back as a talking point in the country at large – wholesale inflation has been in the double digits for over 12 months. CPI has now breached the RBI's upper target of 6% for three months continuously. India committed the mistake of adopting the western concept of inflation.

Inflation targeting refers to the policy of controlling inflation by raising the interest rate over which the central bank has control. Problem – this is forcing the economic activities to slow down. Allowing full productivity would lead to more employment.

India's official model of inflation control is based on unscientific foundation. Neither the price of agricultural goods nor that of imported oil is under the central bank's control. The only way in which monetary policy can control inflation is by curbing the growth of non-agricultural output, which would in turn lower the growth of demand for agricultural goods. But this comes at the cost of output and employment.

The implication for the policymaker that inflation is driven by agricultural goods prices and thus focus should be on increasing the supply of these goods. Ideally, food prices should decline, for the consequent rise in demand for other goods will propel the economy forward.
BUT - Growing per capita income in India has shifted the average consumption basket towards foods rich in minerals, such as fruits and vegetables, and protein, such as milk and meat. But the expansion of the supply of these foods has been lower than the growth in demand for them.
So a concerted drive to increase the supply of food other than rice and wheat holds the key. RBI is unwilling to acknowledge this change.
The States haven't done anything ensure a supply of cheap. When they do produce surpluses, their only concern is that these be procured by the central government at the highest price. Under these circumstances, a nation-wide project for producing food cheaply remains a distant dream.
Monetary policy maneuvers like Repo rate is not an efficient solution for an agricultural price-driven inflation.
Any lasting inflationcontrol would require placing agricultural production on a steady footing, with continuously rising productivity.

Beyond the Writeup: India's agriculture productivity issues

Page 10. GS III (Economic Development)

The status of GST compensation dues

Why are funds owed to the States delayed? Are cess collections not growing fast enough? Will the compensation period be extended beyond five years?

VIKAS DHOOT

The story so far: At a meeting with Chief Ministers last week, Prime Minister Narendra Modi said that several non-BJP ruled States had failed to cut taxes on fuel products whose prices have surged sharply since March and urged them to do so in the interest of giving relief to the people facing high inflation. Most of the States he referred to – West Bengal, Tamil Nadu, Maharashtra, Kerala, Telangana, Jharkhand and Andhra Pradesh – countered the PM's pitch bluntly. West Bengal and Tamil Nadu said they had already reduced their VAT levies once. Maharashtra and Kerala pointed to States' resource constraints and pending dues from the Centre. The Mamata Banerjee administration said slashing State levies on petrol and diesel will be possible only if the Centre clears its outstanding dues of over ₹97,000 crore, which includes compensation for implementing the Goods and Services Tax (GST).

What is the status of the outstanding GST compensation due to the States?

The GST regime entailed doing away with multiple State and Central levies to create a simplified tax system for businesses. As this meant that States had to give up several taxation powers in the process, they were assured that revenue losses will be compensated for five years. The compensation was to be calculated by assuming a 14% year-on-year growth over revenues in 2015-16 from the State taxes subsumed in GST, and remitted from a compensation cess fund backed by cess levies on sin and luxury goods like pan masala, tobacco, coal and cars.

Hours after the meeting, to counter these States' arguments about pending dues, the Finance Ministry said that outstanding GST compensation dues to States for 2021-22 stood at ₹78,704 crore, equivalent to four months of such accruals. This means that dues have been remitted to States for the eight-month period of April 2021 till November 2021. The ministry, which had last released GST compensation of ₹18,252 crore to States and Union Territories during March, indicated its inability to pay the dues immediately owing to 'inadequate balance' in the compensation cess collections fund. "Normally, compensation for 10 months from April-January of any financial year is released during that year and the compensation for February-March is released only in the next financial year. The pending amount will also be released as and when amount from cess accrues in the compensation fund," the Ministry assured.

On top of the ₹78,704 crore due to States, ostensibly for the period of December 2021 to March 2022, compensation for the April to June period – the last quarter for which such dues will accrue – also need to be arranged. Chief economist of rating agency ICRA Aditi Nayar has estimated that this could be another ₹60,000 crore, taking total dues that remain to be paid to States close to ₹1.4 lakh crore.

How much GST compensation has been paid so far to States and when will this cess levy end?

From July 2017 when the GST regime kicked off till now, about ₹7.35 lakh crore has been released as GST compensation to States. It had nearly doubled from ₹83,000 crore in 2018-19 to ₹1.65 lakh crore in 2019-20, before the pandemic hit the economy and revenue collections across the board. The Finance Ministry said that ₹2.78 lakh crore of compensation has been released to States for the year 2020-21 itself. Because GST as well as compensation cess inflows had dried up due to the COVID-19 lockdowns, as much as ₹1.1 lakh crore was financed through special borrowings from the market. In effect, the Centre borrowed these funds and lent them onwards to States as 'back-to-back' loans staggered through the year. Similarly, ₹1.59 lakh crore was raised in 2021-22 to pay States' compensation dues as per estimated shortfalls in the cess fund collections, and these funds were disbursed entirely by October by resorting to front-loading of the borrowings during the financial year. At the time, the Finance Ministry had expected the overall compensation payouts for the year to be ₹2.59 lakh crore, which it said would exceed the amount of compensation accruing to States in 2021-22, indicating it included pending compensation shortfalls for 2020-21.

The levy of the compensation cess, which was to cease on June 30 this year, has been extended till March 2025-26 with a view to use the receipts to repay the principal and interest on these special loans. Several States, worried about income sources falling off a cliff once the assured compensation ceases to accrue from July 1, have urged the Centre to extend the GST compensation period beyond the five-year promise. But these demands have been stymied so far, citing the legal provisions enabling GST, and are unlikely to gain traction.

Will the record GST collections in recent months help?

To the extent that States get a larger share of higher GST collections, of course. With April and May both clocking fresh highs in GST revenues of ₹1.42 lakh crore and over ₹1.67 lakh crore, the Centre and States' share, after making adjustments, was a robust ₹1.32 lakh crore and ₹1.36 lakh crore, respectively, over the two-month period. However, GST compensation cess collections are still not growing as rapidly as the overall kitty. Giving States some clarity on when outstanding GST compensation dues will be released, will help them plan their borrowings for the year, which will be particularly tricky from July. While the expected step-down in GST compensation flows from July 2023 may enlarge State borrowings this year, the timing of the release of the pending funds would impact their plans significantly, Ms. Nayar noted.

Moreover, with States expected to aggressively push capital spending this year, which is critical to spur growth, an early release of funds, be it the devolution of other tax collections, or GST compensation, would help them plan and execute public infrastructure projects quicker.

Mamata Banerjee administration said slashing State levies on
petrol and diesel will be possible only if the Union govt clears the
outstanding dues of over ₹97,000 cr which includes
compensation for implementing the GST.
Under GST, the states were assured that revenue losses will be
compensated for 5 years. The compensation was to be calculated by
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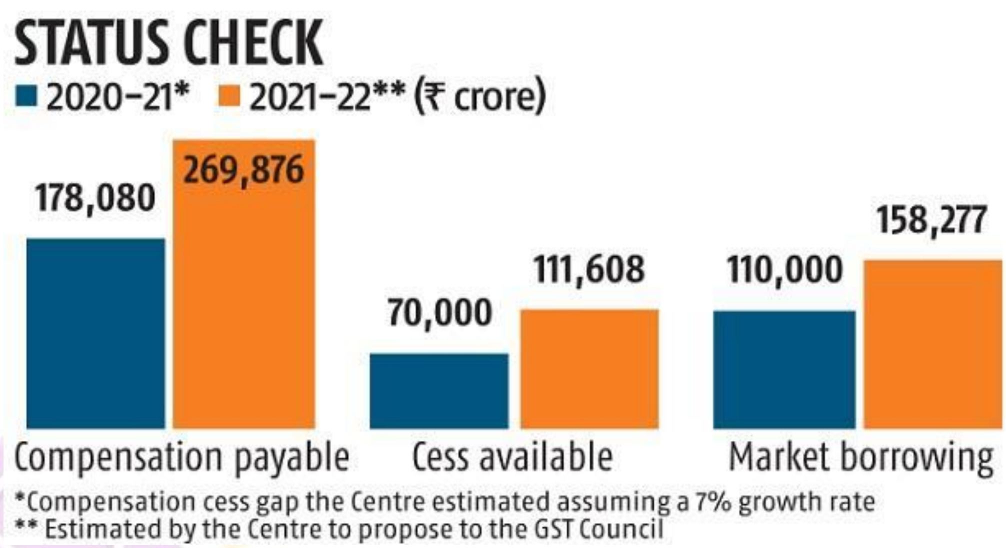
subsumed in GST, and remitted from a compensation cess fund backed by cess levied on
sin goods. Finance Ministry said that outstanding GST compensation due to the states
for 2021-22 is ₹78,704 crore, equivalent to four months.
Since July 2017, about ₹7.35 lakh crore has been
released as GST compensation to States.
During pandemic, govt has had to raise external money to compensate the states for GST.
Compensation cess was to stop from June 30 this year, but it has been
extended till March 202526 to use the receipts to repay these special loans. Several
States have urged the Centre to extend the GST compensation period beyond the five-
year promise.

STATES WITH MOST GST DUES PENDING (In ₹crore)

	Released	Shortfall loan released	Yet to be released
Maharashtra	17,834	13,782	11,563
UP	8,299	8,140	6,954
Tamil Nadu	6,697	8,095	6,733
Delhi	6,446	6,193	5,461
West Bengal	4,531	6,425	4,292
All states	**96,576**	**159,000**	**53,661**

Source: Finance Ministry reply tabled in Rajya Sabha



Centre yet to give Rs 78,704 crore GST compensation to states for FY22

This compensation cess is credited to the compensation fund and as per the Act, all compensation is paid out of the fund.

Written by FE Bureau
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Page 1. GS II (Polity)

President has no role to play in Perarivalan's plea, says SC

Governor had no authority to transfer mercy plea: Bench

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NEW DELHI

The Supreme Court on Wednesday disagreed with the Central government's suggestion that the court should wait till the President took a call on Rajiv Gandhi assassination case convict A.G. Perarivalan's mercy plea referred to him by the Tamil Nadu Governor for a decision.

A Bench of Justices L. Nageswara Rao and B.R. Gavai said the Centre had missed the obvious question posed by the court by a mile. The pertinent question was whether the Governor had, in the first place, the authority to refer the mercy plea to the President.

Under Article 161 of the Constitution, the Governor was bound by the aid and advice given by the Tamil Nadu Council of Ministers in September 2018 to the Governor to release Perarivalan, who has already served over 30 years of his life sentence. The Governor *prima facie* had no authority to transfer the mercy plea to the President. There was no role for the President here under the Constitution, the court told Additional Solicitor-General K.M. Nataraj, for the Centre.

> The question whether the Governor was right in referring the State Cabinet's wish to the President, instead of exercising his duty under Article 161, has to be decided by the court
>
> JUSTICE L. NAGESWARA RAO
> SUPREME COURT

"We cannot shut our eyes to something that is happening against the Constitution. We have to follow our Bible – the Constitution of India," Justice Rao addressed the Centre.

Justice Gavai said no authority, however high, could put a spoke in the working of the Constitution.

Mr. Nataraj urged the court, "The file has been referred by the Governor to the President. If the President refers it (mercy plea) back to the Governor, there is no need to discuss this issue at all... The President himself will decide if the Governor could have referred the file to him or not. Leave it to the President to take a call on whether to pardon or reject or send the file back to the Governor...".

Justice Rao shot back, "We thought it was our duty to interpret the law and not the President's... The question whether the Governor was right in referring the State Cabinet's wish to the President, instead of exercising his duty under Article 161, has to be decided by the court".

Justice Gavai said there had been ample time for the Centre to return the mercy plea file to the Governor.

Mr. Nataraj said, "No, it was only recently the file came to us".

Justice Gavai told Mr. Nataraj, "The Governor decided to send the file to the President on January 27, 2021... It is May 5, 2022 today... And you are saying it came to you only 'recently'? This is a matter concerning personal liberty".

Mr. Nataraj persisted, "The man is out on bail".

Justice Rao reminded the Centre, "But he has a Damocles' sword hanging over him". The court said Perarivalan was not interested in these "finer questions of law".

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SC disagreed with the Central government's suggestion that the court should wait till the President took call on Rajiv Gandhi assassination case convict A.G. Perarivalan's mercy plea referred to him by the Tamil Nadu Governor for a decision.

SC - Pertinent question was whether the Governor had the authority to refer the mercy plea to the President. Under Article 161 of the Constitution, the Governor was bound by the aid and advice given by the Tamil Nadu Council of Ministers - to release Perarivalan, who has already served over 30 years of his life sentence. The Governor prima facie had no authority to transfer the mercy plea to the President. There was no role for the President here under the Constitution – SC.

SC - There had been ample time for the Centre to return the mercy plea file to the Governor. The court also asked why the Centre had to speak for the Governor. Tamil Nadu CoM had recommended Perarivalan's release way back in September 9, 2018.

President and Governor exercised two distinct powers of mercy under Articles 72 and 161, respectively.

Beyond the Writeup: Governor's power to pardon overrides Section 433A of IPC

Recently, the Supreme Court (SC) held that the Governor's power to pardon overrides Section 433A of Code of Criminal Procedure (CrPC). SC held that the Governor of a State can pardon prisoners, even before they have served a minimum 14 years of prison sentence. The Governor's power to pardon overrides a provision in the CrPC Section 433A which mandates that a prisoner's sentence can be remitted only after 14 years of jail.

Section 433A states that where a sentence of imprisonment for life is imposed on conviction of a person for an offence for which death is one of the punishments provided by law, or where a sentence of death imposed on a person has been commuted under section 433 into one of imprisonment for life, such person shall not be released from prison unless he had served at least fourteen years of imprisonment.

The court noted that the sovereign power of a Governor to pardon a prisoner under Article 161 is actually exercised by the State government and not the Governor on his own. The advice of the appropriate government binds the Head of the State. The state government can frame a policy of grant of remissions either under Section 432 of the CrPC or under Article 161 of the Constitution. If a prisoner has undergone more than 14 years of actual imprisonment, the state government, as an appropriate Government, is competent to pass an order of premature release. Section 432 of the Code of Criminal Procedure empowers the Government to remit sentence.

Mains Practice Questions

1. Write a short note on the pardoning powers of the Governor of a state in India and draw comparison with the pardoning powers given to the President of India.

(250 words; 15 marks)

2. What is GST compensation cess? Does the demand by the state governments to extend GST compensation by 5 more years have merit?

(250 words; 15 marks)

Q1 – GS II (Polity)
Q2 – GS III (Economic Development)