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PRESERVING GROWTH MOMENTUM

A Politically Viable Framework For Fiscal Prudence

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The Advocacy Paper titled 'Preserving Growth Momentum: A Politically Viable Framework for Fiscal Prudence' undertakes an examination of the current state of public finances in India, the imminent dangers to the country's future and aims to devise institutional mechanisms within the Indian Constitutional framework to incentivise fiscal prudence and safeguard the long-term interests of the country. This Paper is enriched because of the valuable insights and feedback of some of the leading experts in the fields of public finances and economics. We would like to extend our heartfelt gratitude to the following for their guidance and support:

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EXECUTIVE SUMMARY

The most important faultline emerging in our electoral politics in recent times is the choice of prioritising between long-term growth and short-term political gains. While much of the globe is facing headwinds, India is poised to grow at about 7% on a long-term basis. This is the result of astute fiscal management and pragmatic policies implemented over the years, and favourable global climate encouraging investments in India to diversify supply chains – both these factors establishing a solid foundation for sustained high growth for the next 20-30 years. Preserving this growth momentum requires a continued focus on economic reforms, fiscal discipline, and investments in critical sectors that facilitate growth, enhance incomes and create opportunities. It is essential to strike a balance between short-term individual gains and the long-term public good to ensure lasting economic growth and prosperity for all citizens.

In a country with large numbers of poor, individual short-term welfare (ISW) has a strong political appeal. Even in wealthy, mature democracies voters are attracted to ISW. However, the challenge is to balance ISW with pro-growth expenditure in a manner that the public finances remain healthy and economic growth prospects are not hindered. A frontal clash between ISW and growth will be counterproductive.

The recent reversal of policy in several States to switch to unfunded, index-linked, defined benefit-based Old Pension Scheme (OPS) from defined contribution-based National Pension System (NPS) will spell disaster to public finances in the long run. In their quest to appease the vocal, influential, well-organised government employees, some States are tempted to take a short-term approach at the cost of future generations. OPS is unfunded and has no contributory element in it. Future generations are asked to pay for past services rendered. With index-linked pensions and increasing average life span, the pension burden on governments will be unsustainable, crippling public finances and leading to economic stagnation. Such a fiscal collapse will mean condemning hundreds of millions to perpetual poverty.

There are, however, significant qualitative differences between other forms of ISW and OPS. Other forms of ISW benefit the bulk of the poor and lower middle classes; in some States about 60-70% of the households are covered by free food grains, old age pensions, and other forms of short-term palliatives to mitigate the pain of poverty. The per capita expenditure on ISW is relatively low – accounting for about ₹ 5,000 to ₹ 15,000 per capita per annum. These ISWs are not legally mandated, and can be withdrawn as poverty levels come down, or when political priorities change. Even MGNREGA, which is legally mandated, is self-limiting; it is only applicable to the able bodied poor in distress who are willing to work for paltry wages, and as poverty levels decline, fewer people will work for such subsistence wages. In any case, all ISW expenditure is fully funded and accounted in the budgets.

There is no index linkage in most ISWs, and therefore if significant new programmes are not launched, the share of ISWs in public expenditure will fall steeply as the economy grows and tax revenue increases. But in case of OPS, the benefits flow only to 3.2% of the workforce comprising government employees. The average OPS burden is of the order of ₹ 400,000 – ₹ 500,000 per recipient per annum. Once a government switches over to OPS, it becomes a long-term, permanent legal liability from which the government cannot escape. Successive governments and future tax payers are burdened with the expenditure committed by the current government. And this commitment is incurred voluntarily by some States despite the fact that all employees since 2004 have been recruited on the basis of NPS; in effect, the governments have unilaterally moved to OPS against the contractual provisions, to the detriment of all taxpayers and future generations.

It is therefore imperative to preserve growth momentum by building an acceptable framework for politically viable fiscal prudence. Any effort to scrutinize individual welfare programmes is futile because there will never be agreement on the merits or demerits of those programmes. Micro-management of a State's welfare programmes and budget priorities is neither constitutionally feasible nor politically viable. In a federal polity with fierce political competition and high degree of polarisation, the fiscal framework should be pragmatic and effective without encroaching on the State's role or relying on subjective, partisan assessments.

Indian families irrespective of caste, creed and region practise thrift and do not borrow for current consumption needs. But our governments are profligate with public money, and are habitually borrowing to meet current expenditure without creating assets or enhancing productivity. Clearly, the government – at the Union or State level – should be free to decide how to spend money from its revenues, but borrowed money cannot be used to finance current expenditure. Unfunded, unproductive long-term liabilities, and profligate current expenditure forcing governments to borrow without creating assets or enhancing productivity pose the gravest and most immediate threats to India's economic stability and long-term growth prospects.

This paper proposes a minimalist approach of bringing revenue deficits to zero in a finite period of three years in States. The Union may need a longer period of upto five years because of the structural deficit in Union finances resulting from large transfers to States. Revenue deficit grants to States need to end so that there is no incentive for profligacy. FRBM Act should incorporate mandatory nil revenue deficit norm, and impose the necessary conditions under Article 293(4) of the Constitution of India. As a principle, social security in old age is sound policy. The key issues are: is the burden sustainable; who are the beneficiaries, and at whose cost. If governments adopt generous pension schemes to a select group of people at the cost of future generations, that is both unjust and unsustainable. However, if the governments reflect the cost of future pensions in current budgets, then there is accurate accounting of expenditure, and the burden of pensions is borne by the current generation of taxpayers who are the recipients of the public services. As future pensions are drawn from a fully provided pension fund, there will be no burden on the exchequer in the future. Therefore, in order to mitigate the potential adverse effects of the OPS, the States opting to revert to the OPS should be mandated to account for future pension liabilities in the current budget, using appropriate discounted cash flow factors. This will ensure that the future generations are not burdened for services rendered in the past. Moreover, a provision requiring such accounting should be made mandatory as a condition to borrowing under Article 293(4) of the Constitution. This will ensure fiscal discipline, safeguarding the future of the citizens.

There should be an independent, credible institution – either a permanent Finance Commission or a Fiscal Council – to monitor public finances of the governments at Union and State levels, and exercise the function of consenting to State's loans under Article 293. An Office of Budget Responsibility (OBR) should be created to act as a fiscal watchdog and provide independent analysis of public finances of the Union and States, including forecasts, scrutiny of public policy costings and evaluation of performance against fiscal targets. The OBR can be a part of the Finance Commission or Fiscal Council.

In case of large capital expenditure, there should be a proper cost-benefit analysis and approval of loans should be contingent upon reasonable returns or benefits from investments, as per the conditions imposed under Article 293(4).

Subject to this broad boundary conditions to ensure sustainable expenditure and healthy public finances, the governments and legislatures at the Union and State levels should be completely free to frame policies, design programmes and implement welfare measures and capital projects as they deem fit as long as fiscal responsibility is practised and resources are available. The government's sovereignty with regard to public expenditure is integral to democratic governance. The elected government and the voters alone should decide how government spends public money, and not any other organ of state or agency.

Such a minimalist, pragmatic framework is vital to preserve the growth momentum of the economy. In order to ensure fiscal responsibility while respecting the sovereignty of the legislature and government, it would be desirable to rely on an objective, measurable, reasonable indicator. The concept of Revenue Deficit (RD) is well established in Indian budgetary system, and RD is a measurable, clearly defined, non-intrusive, broadly acceptable indicator that would be helpful in protecting the health of public finances. Restriction on RD has the merit of preserving the freedom of action of elected governments as long as fiscal responsibility is practised. If we institutionalise a practice of transparent accounting by fully funding in current budgets the irrevocable, long-term commitments like pensions, then the burden does not fall on succeeding generations, and the future health of the public finances will not be undermined. Independent, non-partisan, transparent mechanisms for monitoring and decision making in respect of fiscal rules will ensure broad acceptability and credibility of the process. Other appropriate safeguards to ensure that public money is productively and prudently utilised need to be devised. Such a balanced, transparent and minimalist approach will be broadly acceptable across the political spectrum. This measured approach would ensure a right balance between sustainable short-term individual welfare measures, and long-term growth and poverty eradication.

PRESERVING GROWTH MOMENTUM

A POLITICALLY VIABLE FRAMEWORK FOR FISCAL PRUDENCE

India's economic reforms project, which began in 1991, marked a turning point in the country's economic future. Since then, successive governments – Union and States – have taken several reform initiatives and implemented policies to remove fetters in investments and promote economic growth in the country. India is now a relatively fast-growing economy among large economies in the world. The accent on promoting investment, building digital and physical infrastructure, liberating the producers from unproductive regulatory burden, unleashing the animal spirits of entrepreneurs, creating a national market, cleaning up the bad loans in the banking sector and above all, emphasis on competent and effective delivery have all boosted confidence of the consumers and investors alike. The Union and States have worked together to create a conducive environment for businesses and investors to survive and thrive in the country. The creation of a strong, unifying market through the introduction of the Goods & Services Tax (GST), measures to improve ease of doing business through the Insolvency and Bankruptcy Code (IBC), and the accent on infrastructure creation through the National Infrastructure Pipeline have helped attract investments and promote growth in the country. State governments have made remarkable progress in improving the business climate, making them attractive destinations for investments. This has been demonstrated in various sectors such as the Information Technology (IT) industry, automobile industry, infrastructure and tourism sector across different States. As a result of the sustained efforts, India is poised to be the third largest economy in a decade. India has a unique opportunity to further improve its economic prospects in the coming years. However, India's growth story is not without its challenges. The political culture of the country and the design of the current electoral system often force political parties to prioritise short-term electoral gains over long-term public good, posing a significant challenge to the country's growth trajectory. The decision in some States to revert to the Old Pension Scheme (OPS) and electoral promises to implement the OPS pose a grave threat to India's growth prospects in the long run. Though the economic impact of this policy decision will not be felt immediately, the long-term effects will cripple public finances and severely undermine the growth prospects of the country.

1. FRBM and NPS – Acts of Foresight

The Union Government exhibited great foresight in enacting the Fiscal Responsibility and Budget Management Act, 2003 (FRBM) and building a national consensus on fiscal responsibility. The Union government, following the recommendations of the Twelfth Finance Commission, implemented measures to incentivise States to adopt fiscal responsibility legislations at the State level. The recommendations included: first, permitting States to borrow directly from the market with the expectation that such mechanism would exert fiscal discipline on States; second, adopting a debt write-off scheme wherein repayments due from 2005-06 to 2009-10 on Union government loans contracted up to March 31, 2004, were made eligible for write-off. As a result, all States except Sikkim and West Bengal enacted Fiscal Responsibility Legislations (FRLs) to curb deficits and ensure broader macroeconomic stability. The Thirteenth Finance Commission provided similar incentives to the States of Sikkim and West Bengal to limit fiscal deficit and annual borrowing, leading to the two States adopting FRLs in the year 2010.[1]

An even more remarkable feat of the government was the introduction of the contributory pension scheme and the National Pension System (NPS) established in January 2004, based on defined contribution of the employee and employer for all new government employees recruited after 2004 in place of the Old Pension System (OPS) based on defined benefits without any contribution (refer Annexure 1 for details of bipartisan support for NPS). A national consensus was forged by the United Progressive Alliance (UPA) government under Dr. Manmohan Singh and all parties and States embraced the NPS for new recruits except the State of West Bengal[2].

The OPS is an unfunded pension system as no pension contribution accrues during an employee's active service. The pensioners receive 50% of the last drawn salary

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[1] Twelfth Finance Commission. (2004). Report of the Twelfth Finance Commission.
Thirteenth Finance Commission. (2009). Thirteenth Finance Commission Report.

[2] In 2009, the NPS was opened to workers outside government also.

linked to dearness allowance as pensions post their retirement. The burden of lifetime pension after retirement and family pension after death results in an open-ended liability on future generations for past services rendered and thereby undermines inter generational equity. The index-linked nature of pension together with the steep increase in salaries with successive pay revision commissions make the system under OPS unsustainable.

Government pension system in OPS is linked to both wage index and price index. Wage index refers to the substantial enhancement of salaries effected particularly in the last quarter century based on very generous wage revisions recommended by successive pay revision commissions at the Union and State levels. Price index refers to periodic increase in wages based on consumer price index. Price-index linkage is reasonable and sustainable; reasonable because the monthly pension should retain its value in purchasing power over time, and sustainable because the revenues of government normally increase faster than the rate of inflation. However, wage-indexation has played havoc with pension liabilities and public finances. As wages are increasing substantially with each pay revision, application of same scales in calculating the unfunded pension lead to enormous and unsustainable increase in the burden on exchequer.

The unsustainable nature of OPS is corroborated by the fact that the pension burden under OPS has sharply risen faster than the revenues of State governments over the years. The annual compound growth rate of pensions during the period 2004-05 to 2021-22 was 14.96%, resulting in the pension outgo surging from ₹ 37,378 crore in 2004-05 to ₹ 399,813 crore in 2021-22, an eleven-fold increase (see Figure 1a), while the State's own revenue grew at a compound annual rate of 12.60% (refer Annexure 3a).

Moreover, OPS disproportionately transfers already scarce resources to a small group of population, constituting just 1.2% of the population (or 3.2% of the workforce). The generous pension disbursements are several times the per capita income and account for 18.2% of total general government revenue. Such skewed expenditure in favour of a small section of the working population raises serious concerns about fairness in resource allocation (see Table 1).

Table 1: Burden of Pension Expenditure (FY 2020-21)

S.No.	Heads	Figures (Amounts in ₹ Crore)
a	Pension Expenditure of the Union	2,66,668
b	Pension Expenditure of all States and UTs	3,68,834
c	**Total Pension Expenditure (a+b)**	**6,35,502**
d	Union Government Revenue [1]	21,37,860
e	States' Own Revenue [2]	13,47,554
f	**Total Government Revenue (d+e)**	**34,85,414**
h	**Total Pension Expenditure as a Share of Revenue [c/f]**	**18.2%**

UTs: Union Territories with Legislature**; RE:** Revised Estimates

Note:
1. Union Government Revenue includes Gross Tax Revenue (before Devolution and Transfers to States) and Non-Tax Revenue (excluding Dividends and Profits).
2. States' Own Revenue includes Own Tax Revenue and Own Non-tax Revenue.

Source:
Pension Expenditure of all States Combined; States' Own Revenues
1. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India.
Pension Expenditure of the Union
2. Report of Comptroller and Auditor General of India for the year 2020-21 (More details in Annexure 2b);
Union's Gross Tax Revenues
3. Budget at a Glance, Union Budget Documents 2023-24.

Unfunded OPS runs counter to most social security systems in other countries. Worldover, the social security benefits are fully funded and the system does not impose an open-ended liability on successive generations or taxpayers. India is the only major economy that is adhering to an unfunded, defined-benefit OPS without any contributions to a pension fund while the employee is in active service.

The challenge of rising civil service pension burden and the consequent adverse effect on government finances has been a cause for concern in most countries for

[3] Reserve Bank of India. (2003). Report of the Group to Study the Pension Liabilities of the State Governments.

decades now. Significant efforts to reform the pension system began around the 1980s in several countries[3]. Although the pensions were traditionally provided through defined-benefit plans in most countries, there was some element of contribution by the employee, with any shortfall being met by government revenues. Realising the unsustainability of such plans, several countries had resorted to certain adjustments in the then existing schemes such as altering contribution structure, eligibility criteria, increasing retirement age, etc.

More importantly, most countries began to switch to some form of advance funding of pension liabilities by setting up separate pension funds. Despite significant variations in the civil service pension plans across countries, there is a common characteristic of providing for partial or full advance funding of pension obligations.

The NPS as a defined-contribution system offers a fiscally sustainable solution to address the social security needs of employees. Under NPS, both employees and employers contribute a share of employee's salary to individual pension accounts during active service[4]. These contributions along with investment returns constitute the pension corpus. This prudent approach limits the fiscal burden on the exchequer to the monthly contributions, and the government's liability ceases upon the employee's retirement. The system, thus, does not create an open-ended liability on successive generations or taxpayers. Conversely, under OPS, future budgets are stretched due to the large outflow as unfunded, index-linked pensions. In 2004, the Implicit Pension Debt (IPD) i.e., the Net Present Value (NPV) of future payments to the (civilian) government employees at the time was estimated to be ₹ 2,003,405 crore, equivalent to 64.51% of the GDP.[5] The IPD comprised of three components: pension and gratuity for Union government employees amounted to ₹ 463,464 crore (14.92% of GDP); pension and gratuity for State government totalled ₹ 1,517,920 (48.88% of GDP); and a funding gap of ₹ 22,021 crore (0.71 % of GDP) for the

[4] Monthly Contribution Rates under the National Pension System (NPS) –
For Union government employees: 10% by the employee and 14% by the government, calculated as a share of the employee's Salary (Basic Pay + Dearness Allowance).
For State government employees: 10% by the employee and 10% by the government, calculated as a share of the employee's Salary (Basic Pay + Dearness Allowance).

[5] Bhardwaj, G., & Dave, S. A. (2006). Towards Estimating India's Implicit Pension Debt. In The Balance Sheet of Social Security Pensions: Proceedings of the Second International Workshop, Organised by PIE and COE/RES, Hitotsubashi University.

Employees' Pension Scheme. These figures highlight the immense fiscal burden posed by pension commitments. Since then the pension burden has grown more than ten-fold (see section 'Rising Pension Burden), and therefore the IPD estimates also would have increased correspondingly in absolute terms.

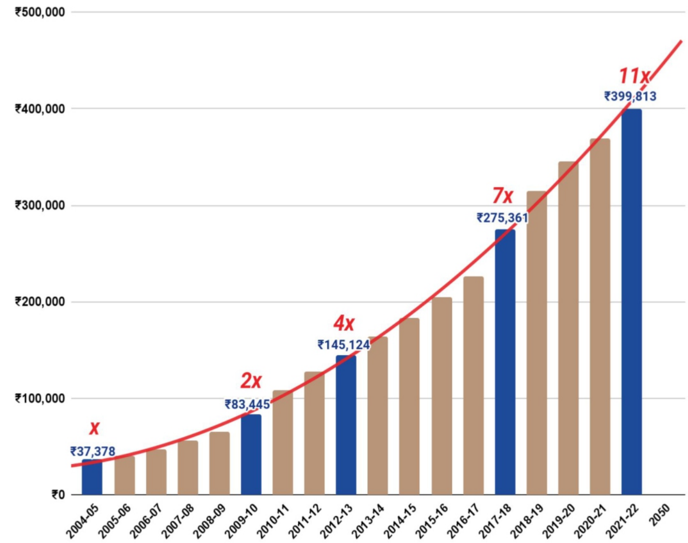
In addition to its fiscal benefits, the NPS secures social security for government employees. The individual pension corpus ensures that the pension benefits are secure irrespective of the government's fiscal situation. In case of an employee's demise, survivors are entitled to receive the accumulated corpus, providing financial security to the family (refer Annexure 4). In contrast, under OPS, pensions are drawn directly from the budgets, which raises the risk of governments deferring pension payments during times of fiscal constraints or being compelled to undertake measures to cut pensions cost as seen with the defence sector (see section 'Unfunded Pensions: Experience in the Defence Sector'). And if a Financial Emergency is ever imposed under Article 360 of the Constitution to protect the financial stability and credit of India, pensions of government employees under OPS may be significantly reduced. The finances of many States are already stretched to their limits, as seen in the subsequent sections of the paper. It is imperative to exercise fiscal prudence and simultaneously ensure a just and sustainable social security system for government employees.

2. Rising Pension Burden

The escalating pension burden on the exchequer poses a significant challenge to the state of public finances in India. Over the years, pension expenditure in government is rising exponentially (see Figures 1a and 1b). In just 17 years between 2004-05 and 2021-22, the pension expenditure in States increased eleven times – from ₹ 37,378 crore in 2004-05 to ₹ 399,813 crore in 2021-22, and almost trebled in nine years – from ₹ 145,124 crore in 2012-13 to ₹ 399,813 crore in 2021-22.

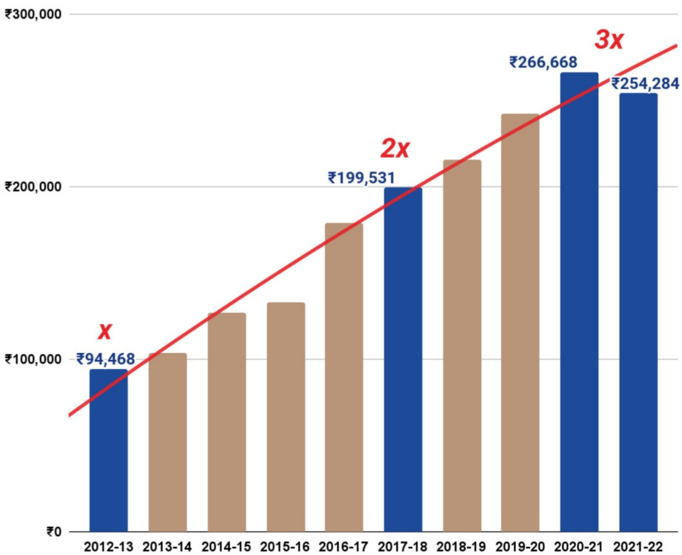
Similarly, the Union pension expenditure increased three-fold in nine years since 2012-13 – from ₹ 94,468 crore in 2012-13 to ₹ 254,284 crore in 2021-22. What is more alarming is, pension expenditure as a share of States' own revenues and of total

Figure 1a: Pension Outgo of all States and Union Territories (₹ Crore)



Data Source: *Handbook of Statistics on Indian States 2021-22, RBI; State Finances: A Study of Budgets 2022-23, RBI. More details in Annexure 2a.*
Chart: *Foundation for Democratic Reforms.*

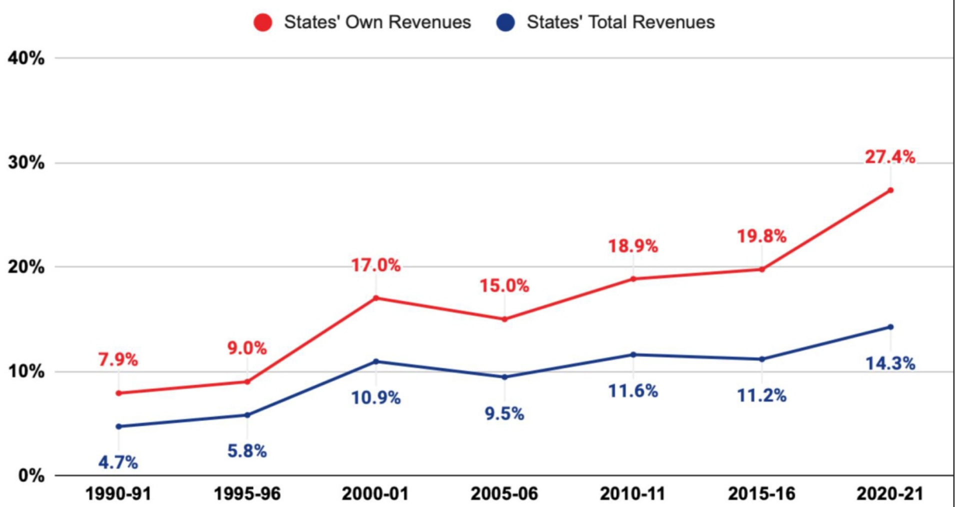
Figure 1b: Pension Outgo of the Union Government (₹ Crore)



Data Source: *C&AG Reports & Lok Sabha discussion. More details in Annexure 2b.*
Chart: *Foundation for Democratic Reforms.*

revenues is showing a steep increase. In 1990-91, the States incurred 7.9% of their revenues (excluding Union transfers) on pensions; whereas this ratio rose to 27.4% by 2020-21. Similarly, during the same period, the pension burden as a share of States' total revenues (including Union transfers) increased from 4.7% to 14.3% (see Figure 2).

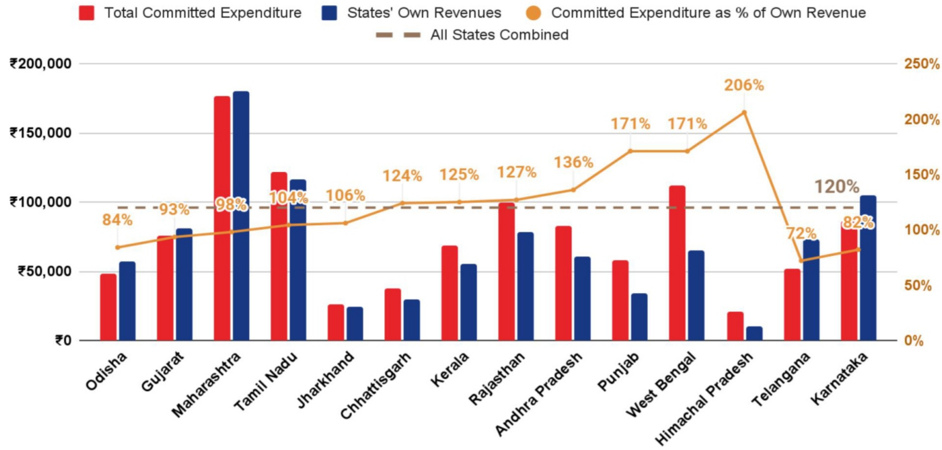
Figure 2: Pension Expenditure of All States as a Share of Revenues



Data Sources: *Calculated from data released by the Reserve Bank of India. More details in Annexure 3b.*
Chart: *Foundation for Democratic Reforms.*

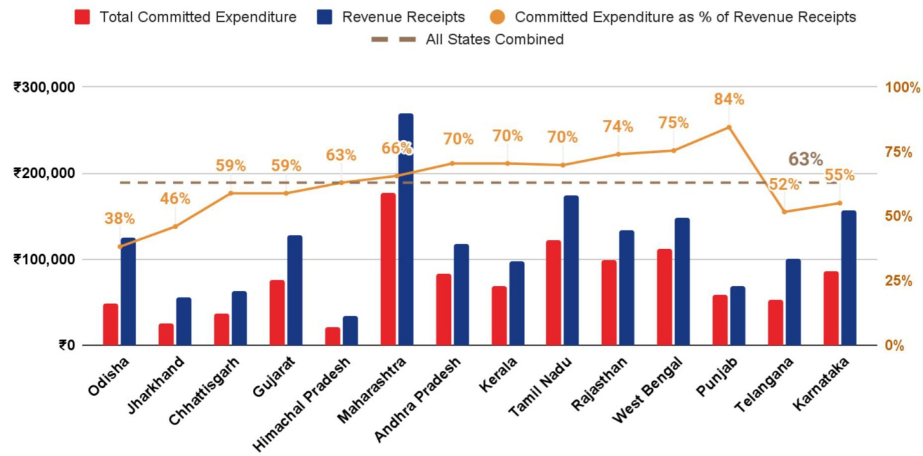
The country's public finances face enormous challenges on account of substantial burden of committed expenditure, comprising salaries, pensions and interest payments. The committed expenditure on an average accounts for 63% of the total revenues of States and a staggering 120% of the States' own revenue receipts, leaving little room for core governance functions (see Figures 3a and 3b). In some States, the share of committed expenditure in total revenues is remarkably high – e.g. Punjab – 84%; West Bengal – 75%; Rajasthan – 74%; Kerala – 70%; Tamil Nadu – 70%; Andhra Pradesh – 70%.

Figure 3a: Committed Expenditure vs. Own Revenues in Select States, FY 2020-21



Data Sources: *State Finances: A Study of Budgets of 2022-23, Reserve Bank of India. More details in Annexure 5.*
Chart: *Foundation for Democratic Reforms.*

Figure 3b: Committed Expenditure vs. Total Revenue in Select States, FY 2020-21



Data Sources: *State Finances: A Study of Budgets of 2022-23, Reserve Bank of India. More details in Annexure 5.*
Chart: *Foundation for Democratic Reforms.*

This is the context in which the Union government introduced NPS in 2004 by broad national consensus. After NPS introduction, the burden of OPS will continue to rise for several years, but there will be decreasing pension burden under NPS on the exchequer as employees recruited after 2004 will, after retirement, draw pension from the funds accrued under NPS. The future pension burden under NPS will decrease over time, and finally will become zero, as the government's pension contributions are made concurrently with the service of the employee, and pension will be drawn from the income from the pension fund in future. As and when the employees recruited after 2004 retire, the only OPS liability on the exchequer will be the pensions for the employees recruited before 2004. Over time, such pension burden on the exchequer will be zero, as all retired employees draw pension under NPS. NPS is not only fiscally prudent protecting the future; it is also morally imperative so that the next generation does not have to pay for the services rendered to earlier generations. Indian families of all castes, religions and regions sacrifice for the next generation, and even poor families practice thrift and build assets for their children. Governments borrowing heavily for current expenditure and transferring pension burden to future generations in the form of unfunded, index-linked defined benefit pension scheme is alien to Indian society's ethos and culture.

2.1. Regressive Switch to OPS

But now several States are unfortunately yielding to pressures from vocal, highly organised government employees and reversing the healthy trend of NPS established and running since 2004. In addition to West Bengal which persisted with unviable OPS, the States of Punjab, Rajasthan, Chhattisgarh, Jharkhand and Himachal Pradesh have either switched over to OPS, or announced their decision to do so in the near future. In several other poll-bound States, some of the major political parties have publicly announced their pledge to revert to OPS. Unfortunately, short-term political compulsions to attract the votes of government employees are trumping the considerations of long-term viability of OPS. The core functions of government, and resources needed to invest in the future and promote growth, incomes, employment and opportunities to the poor are ignored at the altar of instant electoral gain.

2.2. Perverse Incentives

There may even be a perverse incentive encouraging profligate governments to switch over to OPS. Paradoxically, a State government that switches over to OPS, while it is seriously undermining the State's fiscal health and future growth, may in the short-term get a bonanza of additional resources to squander. The earlier government and taxpayers have acted prudently since 2004 and funded the future pension liability under NPS through annual budgetary allocations. All that pension fund now constitutes Assets Under Management (AUM). The total NPS assets in AUM have risen by 23.45% (year-on-year) in FY22, and stands at ₹ 8.82 lakh crore, of which ₹ 6.94 lakh crore is contribution from the employees and governments towards future pension payments to government employees[6]. The Union government's directive under rules and statute governing the Pension Fund Regulatory and Development Authority (PFRDA) that the accumulated corpus from NPS cannot be transferred to State governments is welcome. If a State that switches over to OPS gets back earlier contributions of the government and employees now in AUM, they will actually have a one time bonanza to spend more, while the future burden of pensions on the next generation will rise exponentially. In the absence of restraint and concern for long-term sustainability, all short-term political and fiscal incentives are aligned in favour of profligacy at the cost of growth and inter-generational equity.

In addition, as governments do not make any budgetary allocation towards OPS contributions, once they switch from NPS to OPS, they will actually have reduced expenditure on pensions for some years. But the reduction of pension contribution burden will be at the cost of unviable, unsustainable burden on future governments towards actual payment of pensions from taxpayers' money.

[6] Ministry of Finance. (2023, March10). Release ID: 1905533.

These two perverse incentives for switching to OPS – one time bonanza of accumulated pension fund from past contributions being treated as revenue, and reduced burden of pension contributions for some years under unfunded OPS – should be removed so that governments are encouraged to take rational decisions and the cost of future pensions is reflected in current budgets.

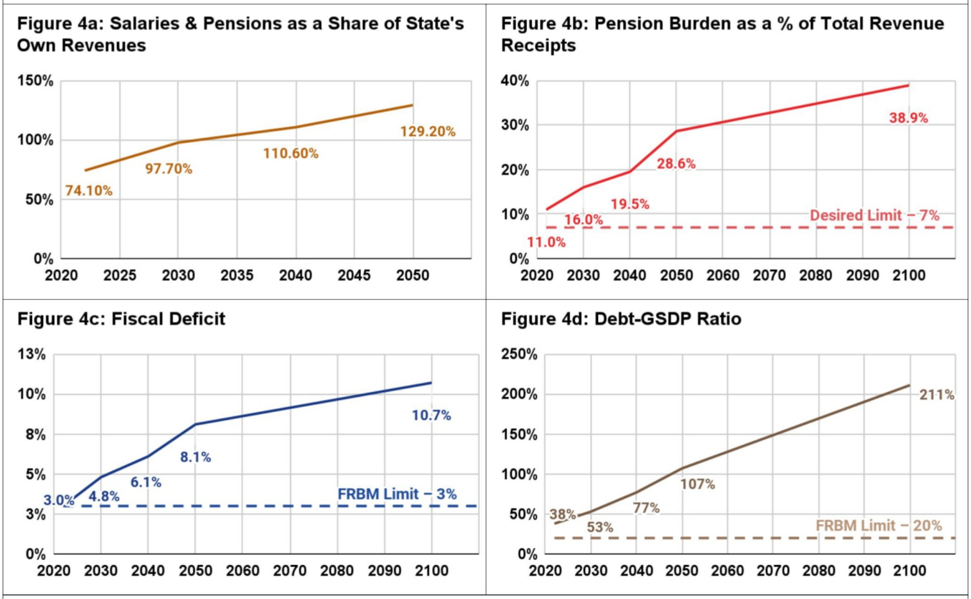
2.3. Horrendous Price with OPS

While short-sighted decisions to revert to OPS may give temporary political dividends, the price that will be paid later is horrendous. Andhra Pradesh (AP) government made detailed calculations and presented data to the public based on a rigorous financial model, developed with the help of experts and validated by actuaries. The results clearly establish the unsustainability of OPS. According to the study, if AP were to revert to OPS, within a span of seven years by 2030, the State's Own Revenues (SOR – excluding Union transfers) would only be sufficient to cover salaries and pensions, leaving no room for other committed or development expenditures.

The share of salaries and pensions as a portion of SOR would rise significantly, reaching 97.7% by 2030, 110.6% by 2040, and 129.2% by 2050 (see Figure 4a). The burden of pensions as a percentage of total revenues (including Union transfers) would exceed the sustainable range of 5-7%, increasing from the current level of 11% to 16% by 2030, 19.5% by 2040, 28.6% by 2050, and 38.9% by 2100 (see Figure 4b).

As a result, the State's fiscal deficit, currently at approximately 3% of GSDP, would grow exponentially. As most expenditure is beyond the control of the government, it would be mathematically impossible to meet FRBM targets. Fiscal deficit is projected to rise to 4.8% in 2030, 6.1% by 2040, 8.1% by 2050, and 10.7% by 2100 (see Figure 4c). As a consequence, the debt to GSDP ratio, on account of OPS alone, would increase from the current 38% to 53% by 2030, 77% by 2040, 107% by 2050, and a staggering 211% by 2100, in contrast to the FRBM norm of 20% of GSDP (refer to Figure 4d).

Figure 4(a-d): Andhra Pradesh – Projections of Key Fiscal Indicators upon Reverting to OPS



Data Source: *Government of Andhra Pradesh communication dated 28/08/2022. More details in Annexure 6.*
Chart: *Foundation for Democratic Reforms*

It must be noted that these are not absolute numbers; they are ratios taking into account increase in GSDP, revenues and Union transfers. The absolute increase in outflow of pensions under OPS will be astronomical, leading to fiscal collapse and Sri Lanka-like crises in all States that revert to OPS or continue with OPS. The misery citizens are going to endure with collapse of government finances and failure to deliver even basic services, the burden on the future generations in the form of mountains of debt and high taxes, the opportunity cost because of lost growth, incomes and employment, and the perpetuation and deepening of gruesome mass poverty crippling tens of millions of people in the coming generations are all too real outcomes that can be anticipated with certainty based on the realistic projections.

In reality, once States breach fiscal deficit norms, and as financial stability and credit of India are threatened, the Union will be forced to impose Financial Emergency under Article 360. That would mean that salaries as well as pensions of government employees will be severely reduced. Even now, in several States, the disbursement of salaries and pensions is often delayed, and payment of arrears of salaries and allowances deferred. Eventually, unsustainable OPS may mean no pension to retired employees, severely undermining their social security in old age.

The risks are further compounded by the demographic transition underway in the country, which is on a collision course with the sustainability of OPS. The pension costs under OPS would rise significantly, ultimately becoming unsustainable due to ageing population. This echoes the World Bank's warning about the illusory nature of pay-as-you-go schemes (PAYG)[7]. As highlighted in a SBI group research paper of March 2022 (see Table 2), "...the Ageing Index (adapted from Rakesh Mohan, 2004) for India defined as the number of persons 60 years old or over per hundred persons under the age of 15 years is likely to reach 76 by 2036 from the current value of 40. The old-age dependency ratio, defined as the number of persons 60 years and over per 100 persons 15 to 59 years old, will touch 23% by 2036 from the current 16%. By 2050, India's population will be 164 crore, out of which 32 crore will be of age 60 years and above. An increase in the old-age dependency ratio imposes heavier demands on the working-age population to maintain the intergenerational flow of benefits to the older people..."[8].

Table 2: Ageing Population Profile, India

Indicators	2011	2016	2021	2026	2031	2036
Ageing Index[1]	27%	33%	40%	49%	61%	76%
Old Age Dependency Ratio (60+)[2]	14%	15%	16%	18%	20%	23%

Note:
1. Ageing Index is defined as the number of persons 60 years old or over per hundred persons under the age of 15 years.
2. The Old Age Dependency ratio is the number of persons 60 years and over per one hundred persons 15 to 59 years.

Source:
1. SBI Research Ecowrap, Issue No. 67, FY22, dated 24 March, 2022.

[7] State Bank of India. (2022). Report on NPS Reforms vis-à-vis Old Pension Scheme (PAYG): Why Good Economics can also be Good Politics. SBI Research Ecowrap Issue No. 67.

[8] Ibid.

Thus continuance of OPS or reversion to it may only be pyrrhic victory – as parties may gain short-term, limited electoral gains and employees may feel they won a battle with collective bargaining power; but eventually it may come to naught as government finances collapse under the weight of OPS, and pensions and even wages may have to be reduced substantially.

2.4. Unfunded Pensions: Experience in the Defence Sector[9]

The demand for OPS is based on a misconception that a shift to OPS would not impact the number of employees receiving pensions. However, past experiences in India show that faced with fiscal unsustainability, governments may be compelled to replace pensioned employees with short-term, non-pensioned employees.

An illustrative example is India's defence sector, where between FY12 and FY21, while the total defence expenditure increased at a nominal annual rate of 9.5%, pension expenditure ballooned 14% year-on-year, and capital outlay spending rose only 8.4%. The approval of a wage-indexed, direct-benefit One-Rank-One-Pension (OROP) scheme in September 2015 was a major contributor to the pension burden, and the implicit pension debt due to OROP is estimated to be unsustainable in the future.

Though the government could not retract the OROP promise, it was forced to launch the Agnipath Tour of Duty scheme in 2023, aiming to reduce the pension burden over time. Agniveers recruited under this scheme would not be entitled to gratuity and pensionary benefits, saving a substantial amount, estimated to be over Rs. 34,500 crore per year, in pension expenditure[10].

The government's swift response in introducing Agnipath demonstrates the need to mitigate the fiscal implications of pension liabilities. Thus, it is plausible that OPS could force some State governments to gradually replace full-term employees with short-term recruits to manage the burden effectively. It is therefore necessary to

[9] The authorship of this section is credited to Pranay Kothasthane, Deputy Director, Takshashila Institution.

[10] Kotasthane, P. (2023, July 24). The Rs 34,500 Crore Argument: Rough Calculations on Agnipath's Pension-Saving Potential Show Why the Change Is Crucial. The Times of India. Accessed at: https://timesofindia.indiatimes.com/blogs/voices/the-rs-34500-crore-argument-rough-calculations-on-agnipaths-pension-saving-potential-show-why-the-change-is-crucial/

adopt sustainable pension models like the NPS to ensure financial prudence and equitable allocation of resources for both current and future generations.

2.5. Social Security: Cross-Country Comparison

The experience world over has been that pensions pose an enormous burden on a country's finances. With more and more State governments in India increasingly resorting to OPS and assuming an unfunded index-linked legal liability, the looming threat of fiscal collapse is real. The employees recruited after NPS came into effect in 2004 will start retiring from about 2034 onwards. NPS was made applicable only to new recruits who joined on the basis of contractual arrangement that they would be eligible for fully-funded, defined-contributory pension scheme (NPS) and not the unfunded, index-linked defined-benefit scheme (OPS). If States resort to OPS despite the binding contract on NPS, they are shifting the burden of future pension payments to the next generation taxpayers. The salaries in the public sector are growing with successive pay revision commissions; the increasing wages and index linkage of pensions are escalating the pension burden exponentially (see section 'Rising Pension Burden'). In many instances, the pension drawn by a retired employee is in multiples of the last salary drawn. As the number of retirees grows and the average life span increases, the burden on the exchequer to discharge an unfunded legal liability will be astronomical and unsustainable.

As discussed in the section 'FRBM and NPS – Acts of Foresight', countries worldover have now taken a more sustainable path to provide for future, anticipated, large expenditures such as social security benefits to their citizens. The current generation provides for their future benefits from their own resources, ensuring there is no open-ended, blanket liability on the future governments or successive generations. The pension fund drawn from social security taxes covers the pension liability. In the United States, for example, the employed and the self-employed, constituting 94% of the current US workforce[11], are covered under a near-universal social security program called the OASDI (Old Age, Survivor, and Disability

[11] Office of Retirement and Disability Policy, Office of Research, Evaluation, and Statistics. Annual Statistical Supplement to the Social Security Bulletin. (2022). Report No. 13-11700.

Insurance). Employee and employer each pays 6.2% of earnings as OASDI payroll taxes, and self-employed people pay an amount equal to the employer-employee contribution[12]. These taxes are paid on earnings upto a specified annual ceiling of USD 147,000 (in 2022). The taxes are allocated to two Trust Funds: the Old-Age and Survivors Insurance (OASI) Trust Fund and the Disability Insurance (DI) Trust Fund. According to the most recent data, over 65 million retired workers aged 65 and above and their families[13], received social security benefits of about USD 1,100 billion during calendar year 2021. This retirement benefit is roughly USD 16,920 per person per year, and is about 25% of the per capita income. During the year (2021), about 179 million employees and their employers, and self-employed workers[14] contributed about USD 981 billion towards OASDI at an average of USD 5,480 per worker. The Trust Fund has a healthy reserve of about USD 2,800 billlion, so that any deficit can be comfortably met from the fund without burdening the exchequer (see Table 3).

Table 3: Old Age Survivor and Disability Insurance (OASDI) Trust Fund Operations in the Year 2021 (in USD Billion)

Trust Fund Heads	Old Age Survivor Insurance (OASI)	Disability Insurance (DI)	Old Age Survivor and Disability Insurance (OASDI)
Reserves (end of 2020)	2,811.7	96.6	2,908.3
Income during 2021	942.9	145.5	1,088.4
of which net payroll tax contributions	838.2	142.4	980.6
Cost during 2021	1,001.9	142.6	1,144.5
of which net benefit payments	993.1	140.1	1,133.2
Reserves (end of 2021)	**2,752.6**	**99.4**	**2,852.0**

Source:
1. The 2022 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds, Social Security Administration, United States of America.

Similarly, under the contributory pension programme in the United Kingdom (UK) known as the New State Pension, over 12 million workers[15] received social security benefits of about £ 104 billion during the year 2020. This retirement benefit is

[12] The break-up of the scheduled payroll tax rates for 2022 and later: OASI – 10.6% and DI – 1.8% , shared equally between the employer and the employee. The self-employed pay an amount equal to the total contribution of the employer and the employee.

[13] Total beneficiaries under the OASDI program include: 50.1 million old-age beneficiaries (including 47.3 million current retired workers); 5.9 million survivors of deceased workers, and 9.2 million disabled workers and dependents of disabled workers.

[14] Supra note 11.

[15] National Statistics. (n.d). DWP Benefits Statistics: August 2022. Retrieved from https://www.gov.uk/

roughly £ 8,700 per person per year, accounting for approximately 23% of the country's per capita income. In 2020, the contributions to the pension fund were around £ 110 billion, and reserves showed a balance of approximately £37 billion to meet future requirements.

In mature democracies with funded pension systems, there is an accumulated, comfortable reserve fund from past surpluses. Despite contributory pension being in place for decades, the demographic changes are leading to deficit in pension funds. As more and more retired workers are drawing pension in an ageing society, the pension outflows are exceeding inflows of contributions from working population. The net result is underfunding of social security, and increase in unfunded liabilities. For example, in six major States in the US – California, Florida, Illinois, New York, Ohio and Texas – the unfunded liabilities of States and local governments are mounting (as seen in Figure 5(a-f)). The total unfunded pension liabilities in these six States are for the order of USD 2,037 billion[16].

A 2022 analysis on state fiscal health in the US shows that the States in the US owed a total of USD 1.25 trillion in unfunded pension benefits in fiscal 2019[17]. This amount is equivalent to 6.8% of all States personal income, up from 3.0% in fiscal 2007.[18]

Unfunded pension liabilities in a defined-benefit system without contributions, or even in an underfunded contributory pension scheme, can drive even otherwise successful giant corporates into crisis. Corporate pension plans are rare in the US outside the payroll taxes and government social security. In 2021, only 13% of private sector employees had pension plans, which are being replaced by the popular 401(k) and other defined contribution plans[19]. General Motors, (GM) an automobile

[16] Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/

[17] The unfunded liabilities of State and local governments in six States is high as seen in Figure 5(a-f), because local governments are larger than State governments in terms of total employment and expenditure. The total unfunded pension liabilities of all States excludes local governments, and is therefore USD 1.25 trillion.

[18] Biernacka-Lievestro, J., & Fleming, J. (2022, July 7). States' Unfunded Pension Liabilities Persist as Major Long-Term Challenge. State Fiscal Health.

[19] Congressional Research Service. Worker Participation in Employer-Sponsored Benefits Plans: A Fact Sheet (2021).

Figure 5(a-c): Unfunded Pension Liabilities of Select States and Local Governments in the US

Assets   Liabilities

Figure 5a: California

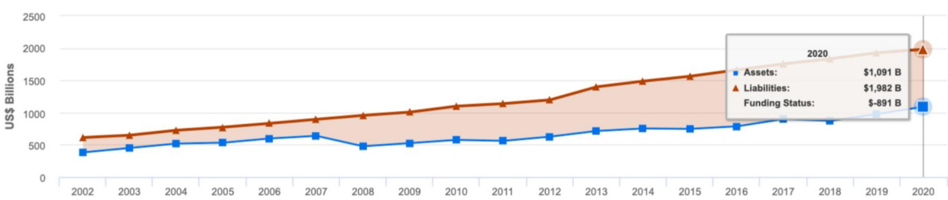


Figure 5b: Florida

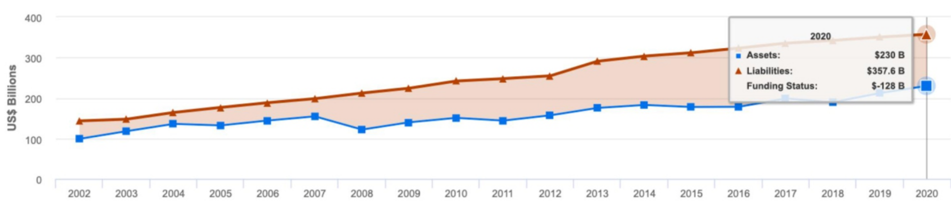
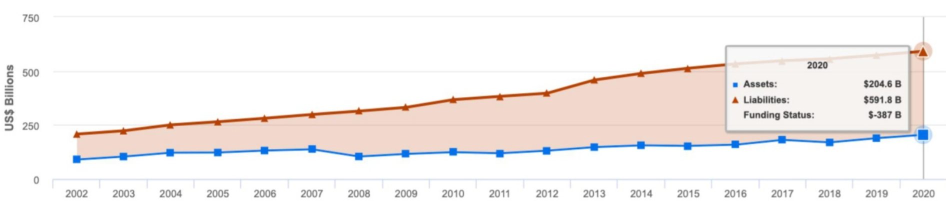


Figure 5c: Illinois



Data Source: *Financial Accounts of United States, Census Bureau and Bureaus of Economic Analysis. More details in Annexure 7.*
Chart: *The Federal Reserve System, United States of America*

Figure 5(d-f): Unfunded Pension Liabilities of Select States and Local Governments in the US

Assets   Liabilities

Figure 5d: New York

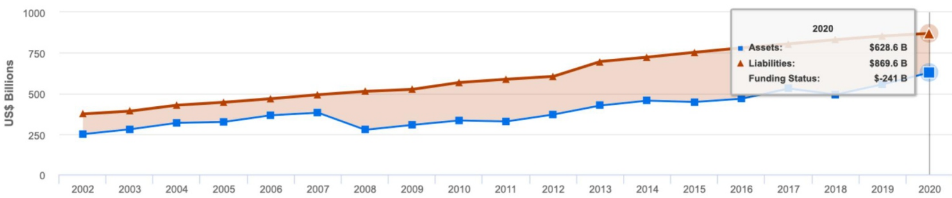


Figure 5e: Ohio

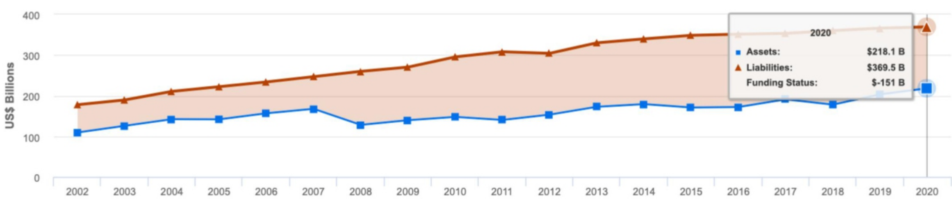
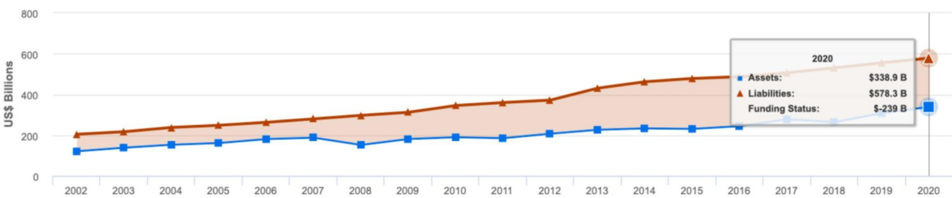


Figure 5f: Texas



Data Source: *Financial Accounts of United States, Census Bureau and Bureaus of Economic Analysis. More details in Annexure 7.*
Chart: *The Federal Reserve System, United States of America*

giant, earlier had pension plans which were not fully funded. As a result, there was a shortfall of USD 20 billion in the pension funds relative to obligations, and the company went into crisis in 2009[20]. Subsequent restructuring of pension plan and generous government support during the Great Recession after 2008 helped GM overcome the crisis. Similarly United Airlines (2002), Eastman Kodak (2012) and Delphi Corporation (2005) faced crises on account of unfunded pension liabilities at varying periods of time.[21]

It is disconcerting that in an impoverished society like India, governments are resorting to reckless populism without any concern for the finances and future of the children. India is the only large country that had earlier committed to providing unfunded, open-ended, index-linked, long-term legal liability as pensions exclusively for the government employees. As previously noted, the average annual social security benefit for retired employee or family in the US is about 25% of the per capita income. However, in India, the average annual pension payments to retired employees are multiples of per capita income. For instance, in Andhra Pradesh State, 3.80 lakh retired employees and their families were paid a total of ₹ 20,327 crore as pension in 2021-22[22]. Thus, the average pension disbursement is ₹ 534,000 against the State's per capita income of ₹ 192,587[23] in 2021-22, or 277% of the per capita income (see Figure 6).

This pattern with minor variations is repeated in respect of all States and the Union. In a scenario where nearly 89% of the workforce is eking out a precarious livelihood with no assured monthly income, the provision of such generous, unfunded, index-linked pension to benefit a tiny, privileged group – 3.2% of the workforce – is immoral and unjust (See Figure 7). Continuation of OPS will drive all governments into fiscal collapse and bankruptcy.

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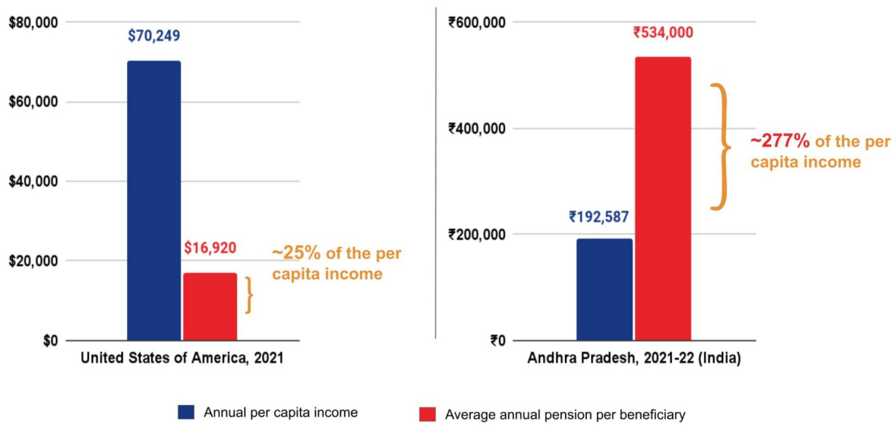
[20] Elliott, D. J. (2009, May 29). What Happens to the GM Pensions in Bankruptcy? Brookings. Accessed at: https://www.brookings.edu/articles/what-happens-to-the-gm-pensions-in-bankruptcy/

[21] Pension Benefit Guaranty Corporation archives. Accessed at: https://www.pbgc.gov/

[22] Finance Department, Government of Andhra Pradesh. (2023). Fiscal Policy Strategy Statement.

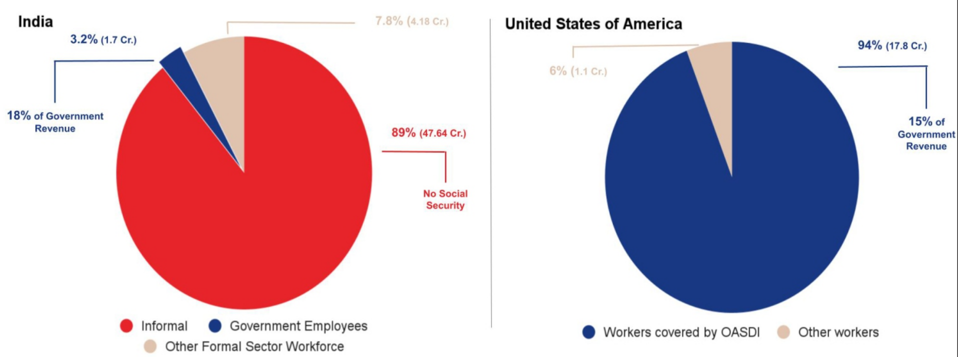
[23] Planning Department, Government of Andhra Pradesh. (2023, March 15). Highlights of Socio Economic Survey 2022-23.

Figure 6: Per Capita Income vs. Pension per Beneficiary, USA & Andhra Pradesh



Data Source: *For USA – Per Capita Income: World Bank Open Data Portal; Pensioners and Pension Amount: OASI & DI Trust Funds 2022 Annual Report. For Andhra Pradesh – Per Capita Income: Socio Economic Survey 2022-23; Pensioners and Pension Amount: Fiscal Policy Strategy Statement 2023, Government of Andhra Pradesh.*
Chart: *Foundation for Democratic Reforms*

Figure 7: Workforce and Social Security Expenditure, India & USA



OASDI: Old-age, Survivors and Disability Insurance

Data Sources: *For India – Total and Informal Workforce: Economic Survey 2021-22,Government of India; Public Sector Workforce: see Annexure 8; Government pension burden: see Table 1. For USA – Annual Statistical Supplement to the Social Security Bulletin, 2022.*
Chart: *Foundation for Democratic Reforms.*

The growing burden of the unfunded pension liability will fall disproportionately on the future generations and the remaining workforce that have no such social security cushion. In contrast, the US with a per capita income 10 times India's (in PPP) has a funded pension program. On the OASDI program, benefiting 94% of all the workers[24], including the private sector, the government spends about 15% of total general government revenues (see Table 4); and the pension/social security payments are fully financed from the Trust Fund derived from contributions from the workers and employers in the form of payroll taxes. Similarly, the other OECD countries have a pension fund drawn from the employee and employer to meet future liabilities. Recent data from other countries indicate that pension (or social security) outflow as a share of general government revenues for nearly 100% of the workforce is: United Kingdom – 12.60%; France – 22.70%; Sweden – 13.10% (see Table 4). Despite the funded nature of pension programs and more frugal pension benefits, many countries are concerned about the pension funds getting depleted in the future, as pension payments for a growing, aged population exceed contributions to the pension fund. The lawmakers are debating policy options to fund long-term shortfalls and ensure continuity in benefits. That is why the retirement age has been progressively increased in most rich countries, and now stands at 65 years or more (refer Annexure 9). In sharp contrast, India, despite a large informal workforce with no social security net, spends 18% of general government revenues towards a generous package for privileged few – the government employees constituting 1.2% of the population (or 3.2% of the workforce). With unfunded OPS, the burden on the exchequer will be astronomical in the future.

Governments reverting to OPS are simply shifting liabilities to future generations. Most States even now are unable to cover their current expenditures with revenue; shifting to unfunded OPS only means that the debt burden of future generations will be unsustainable. Governments today are dealing with massive debts and deficits, as illustrated in the following section of the paper. By committing to unfunded, long-term expenditures, governments are ensuring that mountains of debt will accumulate for incurring unproductive current expenditure, devastating the lives of millions of Indians.

[24] Supra note 11.

3. Living Beyond the Means

Several States and the Union are already spending well beyond their means. As a result governments are incurring revenue deficits, which means that the current day-to-day expenditure is in excess of total revenue receipts (own revenues and all Union transfers), and therefore the States are forced to borrow even to meet current expenditures (see Table 5).

3.1. Unsustainable Debts

As a result, fiscal deficits (borrowings resulting from excess of expenditure over income) are mounting (see Table 5), and the Debt to GSDP ratio is growing to unsustainable levels (see Table 6). The FRBM Act prescribes that the Debt to GSDP ratio should be at 40% for the Union and 20% for the States[25]. However, the Union debt is at 57% of GDP (2022-23 RE)[26], has already exceeded the FRBM limit by 17% of GDP. States' cumulative debt as per 2021-22 RE was already at 28.7% of GDP and budgeted at 29.5% for 2022-23[27]. Some States have much higher debt ratios – eg: Punjab: 48%, Himachal Pradesh: 44%, Rajasthan: 40%, Kerala: 39%, West Bengal: 34% (see Table 6). These debt figures do not include off-budget loans of many States, which do not come under legislative oversight. And yet the Special Purpose Vehicles (SPVs) or other entities which borrowed the money with government guarantees, sometimes with future government revenues directly flowing into an escrow account for debt repayment, have no revenue stream. The money is spent by the government or at the government's behest, and the government has to repay the amount. These SPVs have clearly been created only to be able to borrow in a non-transparent manner bypassing the FRBM scrutiny at least for some time. Often such loans carry a very high interest burden of 10-12% per annum. While exact figures are not clear, a rough estimate indicates that they constitute about 3.5 to 4% of GDP[28]. If we add the fiscal deficit of about 2.5% GDP in States in 2022-23, and the off-budget loans of about 3.5% GDP, the real debt-GDP ratio of States is of the order of 34% by end of fiscal year 2022-23 (see Table 6).

[25] The Fiscal Responsibility and Budget Management Act, 2003, § 4.
[26] Ministry of Finance. (2023). Medium Term Fiscal Policy cum Fiscal Policy Strategy Statement. Union Budget 2023-24.
[27] Reserve Bank of India. (2023). State Finances: A Study of Budgets of 2022-23.
[28] As seen in Table 6, the Outstanding Government Guarantees of major States are ₹8,25,000 crore. Assuming that the combined Outstanding Government Guarantees of all States are ₹10,00,000 crore, it is estimated that the Outstanding

Table 4: Overview of Contributory Pensions Programmes in Select OECD Countries and Comparison with India

Country	Name of the program	Nature of Pension Liability	Coverage as a share of Workforce	Pension Expenditure as a Share of General Government Revenues	Annual Inflow of Contributions to the Fund (Billions)	Annual Outflow of Benefits from the Fund (Billions)	Annual Surplus/Deficit of the Fund (Billions)	Accumulated Reserves at the end of the year (Billions)
United States (2021)	Old Age, Survivors and Disability Insurance	Funded	94%	14.79%	\$980.60	\$1,133.20	-\$152.60	\$2,852.00
United Kingdom (2020)[1]	New State Pension	Funded	~100%	12.60%	£110.64	£104.35	£6.39	£36.93
France (2021)	Basic Scheme and Compulsory Complementary Scheme	Funded	~100%	22.70%	€299.40	€298.50	€0.90	€163.00
Sweden (2020)	Income Pension (Inkomstpension)	Funded	~100%	13.10%	295.499 SEK	326.27 SEK	-30.771 SEK	5.2 years[2]
India (2021)[3]	Old Pension Scheme (OPS)	Unfunded	1.84%	18.2%[6]	Nil	NA[4]	Nil	NA
	National Pension System (NPS)	Funded	1.36%[5]		₹729.04	NA	NA	₹4731.70[7]

NA: Not Applicable

Note:
1. The Annual Inflows consist of contributions received from the New State Pension programme, while the Annual Outflows comprise benefit payments for the New State Pension programme and other allowances. The accumulated reserves at the end of the year are related to the New State Pensions programme and other allowances.
2. The size of the buffer fund is expressed in terms of fund strength i.e., Fund capital at year-end divided by pension disbursements for the year. At the end of 2020, the fund strength is 5.2 years.
3. For India, the pensioners include only the government workforce; unlike the OECD countries, India does not provide a universal, funded social security net.
4. There is no pension fund. The pension expenditure on retired government employees was ₹ 6,35,502 crore in 2020-21.
5. Percentage of the workforce covered under the National Pension System (NPS) is calculated as a share of Union and State government sector subscribers (0.73 crore) in the total workforce (53.53 crore) in the country.
6. For India, pension expenditure includes annual inflow of contributions (₹729.04 Billion) under the National Pension System (NPS).
7. For India, accumulated reserves under the NPS correspond to Assets Under Management (AUM) of the Government Sector.

Source:
Coverage as a Share of the Workforce
1. United States: Annual Statistical Supplement to the Social Security Bulletin, 2022 (Report No. 13-11700), Social Security Administration; pg. 8.
2. India:
- *Old Pension Scheme (OPS) – FDR's calculations; for details see Annexure 8.*
- *National Pension System (NPS) – Official Website of NPS Trust. Retrieved from: https://npstrust.org.in/assets-under-management-and-subsribers*

Pension Expenditure as a Share of General Government Revenues
a) General Government Revenues
3. United States; United Kingdom; France; Sweden: OECD Database.
4. India: FDR's calculations; for details see Table 1.

b) Pension expenditure (or Annual Outlfows) in absolute terms:
5. United States: Status of the Social Security and Medicare Programs: A summary of the 2022 Annual Reports, Social Security Administration, pg.4
6. United Kingdom: Great Britain National Insurance Fund Account, March 2021, HM Revenues & Customs, Government of UK, pg. 23.
7. France: 'CONSEIL D'ORIENTATION DES RETRAITIES-Annual report', September 2022, pg.62.
8. Sweden: 'Orange Report 2020- Annual report of the Swedish pension system', 2020, pg.10.
9. India: FDR's calculations; for details see Table 1.

Annual Inflows; Annual Outflows; Annual Surplus/Deficit; Accumulated Reserves
10. United States: Status of the Social Security and Medicare Programs: A summary of the 2022 Annual Reports, Social Security Administration, pg. 4
11. United Kingdom: Great Britain National Insurance Fund Account for the Year ended 31 March 2021, Corporate Report.
12. France: CONSEIL D'ORIENTATION DES RETRAITIES-Annual report, September 2022, pg.11,62,82.
13. Sweden: Orange Report 2020- Annual report of the Swedish pension system,2020, pg.10,65.
14. India: Official Website of NPS Trust. Retrieved from: https://npstrust.org.in/assets-under-management-and-subsribers

Table 5: Revenue and Fiscal Balance of Select States (% of GSDP)						
States	Revenue Deficit (-) / Revenue Surplus (+)[1]			Fiscal Deficit (-) / Fiscal Surplus (+)[2]		
	2019-20	2020-21	2021-22[3]	2019-20	2020-21	2021-22[3]
Andhra Pradesh	-2.74	-3.5	-0.72	-4.11	-5.44	-2.08
Telangana	-0.66	-2.3	0.38	-3.35	-5.06	-3.88
Tamil Nadu	-2.06	-3.45	-2.25	-3.45	-5.2	-3.96
Punjab	-2.66	-3.25	-3.16	-3.13	-4.24	-4.77
Rajasthan	-3.64	-4.34	-2.98	-3.77	-5.86	-5.18
Kerala	-1.76	-3.23	-3.54	-2.89	-5.12	0.06
Uttar Pradesh	3.95	-0.12	1.26	0.65	-2.81	-4.27
Madhya Pradesh	-0.30	-1.88	-0.49	-3.51	-5.11	-3.7
West Bengal	-1.63	-2.27	-2.15	-3.05	-3.43	-3.47
Jharkhand	0.61	-0.98	0.14	-2.5	-3.65	-2.59
Chattisgarh	-2.79	-1.96	-0.26	-5.21	-4.52	-3.81
Himachal Pradesh	0.01	-0.06	0.64	-3.52	-3.64	-2.99
All States	-0.6	-1.9	-0.9	-2.6	-4.1	-3.7

Note:
1. Revenue Deficits – Instances of States' revenue deficit exceeding 1% of GSDP have been highlighted in red, to indicate the extent of crisis. The threshold is purely illustrative.
2. Fiscal Deficits – Instances of States exceeding fiscal deficit limit have been highlighted in red. The maximum net borrowing ceilings set by the Union Ministry of Finance for 2019-20, 2020-21 and 2021-22 were 3.5%, 5% and 4.5% GSDP respectively.
3. For FY 2021-22 – The figures indicate Actuals for four States – Andhra Pradesh, Tamil Nadu, Punjab and Himachal Pradesh, and Revised Estimates for all other States.

Source:
FYs 2019-20, 2020-21 and 2021-22 (RE)
1. Sacchidananda Mukherjee, Analysis of State Budgets of Major States 2022-23 in India, NIPFP Working Paper Series No. 386, National Institute of Public Finance and Policy.
FY 2021-22 (Actuals) for Andhra Pradesh, Tamil Nadu, Punjab and Himachal Pradesh
2. States' Finances Audit Reports of the Comptroller and Auditor General of India for the year ending 31 March 2022.

Table 6: Debt Burden of Select States					
State	Outstanding Liabilities (2023) (₹ Crore)	Outstanding Government Guarantees (₹ Crore)[1]	GSDP at Nominal prices (2023) (₹ Crore)	Outstanding Liabilities to GSDP (exclusive of Government guarantees) (in %)[2]	Total Liabilities to GSDP (inclusive of Government Guarantees) (in %)
Andhra Pradesh	442,442	138,875	1,317,728	33.58	44.11
Telangana	366,306	129,244	1,293,469	28.32	38.31
Tamil Nadu	753,860	91,975	2,349,143	32.09	36.00
Punjab	305,047	31,282	638,023	47.81	52.71
Rajasthan	537,012	102,810	1,413,620	37.99	45.26
Kerala	390,859	36,601	999,643	39.10	42.76
Uttar Pradesh	710,210	171,705	2,048,234	34.67	43.06
Madhya Pradesh	378,616	39,775	1,322,821	28.62	31.63
Odisha	113,856	6,141	765,963	14.86	15.66
Himachal Pradesh	80,816	1,885	195,404	41.36	42.32
Chhattisgarh	118,166	20,689	457,608	28.54	30.34
Jharkhand	129,467	4,822	381,125	34.32	35.23
West Bengal	608,313	13,156	1,554,992	34.41	39.97
Karnataka	535157	36,657	2,241,368	23.88	25.51

GSDP: Gross State Domestic Product

Note:
1. Government Guarantees for states are for the latest years as available:
   - Telangana, Punjab, Himachal Pradesh, Jharkhand, Odisha – FY 2022-23
   - Rajasthan, Madhya Pradesh, Chhattisgarh – as of December 2022
   - Andhra Pradesh, Tamil Nadu, Uttar Pradesh, West Bengal, Karnataka – FY 2021-22
   - Kerala – FY 2020-21
2. Ratios of Outstanding Liabilities to GSDP calculated here vary slightly from the figures in *State Finances: A Study of Budgets of 2022-23*, Reserve Bank of India.

Source:
Outstanding Liabilities
1. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India
Outstanding Government Guarantees
2. Odisha, Jharkhand: State Finances: A Study of Budgets of 2022-23, Reserve Bank of India;
3. Chhattisgarh, Karnataka: State Budget Documents;
4. Tamil Nadu, Kerala: C&AG Audit Reports;
5. Andhra Pradesh, Telangana, Punjab, Rajasthan, Uttar Pradesh, Madhya Pradesh, Himachal Pradesh, West Bengal: PRS Analysis of State Budgets
GSDP at Nominal Prices
6. State Domestic Product and other aggregates (2011-12 series), National Accounts Data, Ministry of Statistics and Programme Implementation, Government of India.

Several reports indicate that the actual liabilities of State governments may be higher than the reported figures due to repeated deferrals and postponements of bills. These unpaid obligations could amount to tens or thousands of crores, encompassing payments to contractors, public procurement expenses, and deferred allowances to employees, among others. It is evident that the finances of States are facing significant strain, and adopting OPS will markedly worsen the state of public finances in an irreversible manner.

The high ratio of debt to meet current expenditure needs is largely because of committed expenditure and individual short-term welfare (ISW) measures that will only meet current desires and needs without promoting growth or future incomes to people. As a result, no matter how many ISW measures are in place, they only provide temporary relief from the burden of poverty, and there is no prospect of rising incomes in the future. Poverty therefore is perpetuated, and the poor will continue to remain poor without the opportunities for skills, employment and higher incomes in future.

Moreover, the decision to revert to unfunded, legally binding, irrevocable, index-linked liabilities, in the form of OPS, would significantly increase future debt requirements of States to meet their obligations. The additional borrowing would add to debt servicing costs associated with committed unproductive expenditure (or current expenditure) without creating assets or promoting investments and growth. Without adequate investments that promote productivity and growth or enhance future revenues, the mounting burden of interest and debt repayment obligations would ensnare the governments in a debt spiral, making it impossible for them to discharge their obligations to the taxpayers in the future.

4. Short-term Incentives vs. Long-term Public Good

All democracies have a fundamental political challenge. The candidates, leaders and parties have to make difficult and painful choices in the face of limited resources and unlimited wants. When the candidate or a party goes to the people, they have to offer temporary relief from the burden of poverty and high cost of living, and long-term hope of economic growth, rising incomes and escape from poverty and entry into the middle classes. Often there is a clash between the short-term political incentives, and the long-term public good they have to pursue. World over, even in rich countries, voters are attracted to short-term relief. Even in the USA, the massive cash transfers made by the Biden administration toward Covid relief, and the student debt waiver were very popular. In France, another wealthy country, the workers resisted President Macron's proposal to increase the retirement age from 62 years to 64 or 65 years in order to reduce the pension burden on future generations; this despite the fact that in most of Western Europe and the USA the retirement age is about 65 years (refer Annexure 9).

In a poor, developing country like India, it is particularly important to invest in infrastructure, basic amenities, rule of law, service delivery, and quality education and healthcare in order to boost investment and growth, enhance productivity and promote prosperity. As of today, India ranks in the bottom five among 50 large economies in terms of most infrastructure and socio-economic development indicators (refer Annexure 10). If the public finances continue to be neglected, it will become harder to improve education, healthcare, infrastructure and rule of law. This will perpetuate poverty and significantly impede economic progress, making it impossible to catch up with more prosperous countries, thus stunting the future of our children.

4.1. Curb Borrowings for Current Expenditure

If we take the committed expenditure, it broadly is composed of salaries, pensions and interest payments on past debt incurred. Of these, salaries and interest payments are inevitable expenditure; however with NPS, over the long-term the pension outflow from the exchequer can be reduced to zero. When it comes to ISW, it is neither fair nor prudent to withdraw various welfare schemes which are being implemented by the Union and States. But ISWs can be restructured to reduce wastage and corruption, and a reasonable restraint can be exercised to ensure that

ISW expenditure is either frozen for some years, or its growth is less than the growth in revenues. Both NPS implementation and restraint on ISW will eliminate revenue deficits within a few years. At the very least we should make sure that we do not spend borrowed money for committed expenditure and ISW.

4.2. Zero Revenue Deficit

In a democracy, elected governments and legislatures have a right and duty to decide how to spend public money and what programmes to design and implement; that is the essence of sovereignty. Therefore any external effort to identify each ISW programme, assess its merits and demerits, and approve or reject it is simply neither feasible nor desirable. In a politically polarized and surcharged atmosphere, such an evaluation and value judgment of each ISW measure will not be acceptable, and will lead to further polarization and fruitless polemics. In addition, some states have opted to revert to OPS. Such a short-sighted decision to appease a small section (3.2%) of the workforce constituting government employees will lead to economic devastation and collapse of public finances in about a decade's time.

Unfortunately, apart from the appeasement of a small, powerful, vocal section of government employees, there are potentially two perverse incentives for governments reverting to OPS. First, they hope to get a draw from the accumulated pension fund under NPS; such a drawal will give more resources to the offending governments for current expenditure. Second, there will be no outflow towards pension contributions of the government under NPS. But the burden of index linked, defined-benefit pensions in future will be humungous and unaffordable, and will be at the cost of government's core functions. Such large pension commitments tied to future revenues will leave less fiscal room for other expenditures, leading to increase in deficits and debts. Given this context, it is crucial to implement measures that protect the country's finances while also allowing the elected governments to exercise their policy preferences and options. A broadly acceptable, measurable indicator should be applied to monitor and regulate public expenditure. Given our social norm of thrift and protecting income and assets of future generations, a simple norm of not applying borrowed money for committed expenditure and ISW, and limiting all current or revenue expenditure to current revenues with no revenue deficit would be the most pragmatic and effective method of improving public finances.

Therefore measures need to be taken to provide in current budgets future committed expenditure, and remove the perverse incentives of actually benefiting in the short term while shifting the burden on future taxpayers.

4.3. Power Sector Challenges

Curbing revenue deficits and improving public finances acquire great urgency in the context of two present and impending developments which will further weaken public finances. For long, electricity has been supplied to various groups of customers at a heavily subsidised cost or free. This not only put the utilities in financial crisis, but use of unmetered power has precluded proper energy audit and stymied systematic attempts to reduce distribution losses. Because of failure to recover costs from consumers and inefficient power grid, the annual losses accruing to all power distribution companies taken together is of the order of ₹ 62,000 crore (taken as a five-year average),[29] and the losses have not reduced despite years of effort and various rescue programmes (see Figure 8 and Table 7).

Figure 8: Total Borrowings of Distribution Utilities since FY12

Data Source: Report on Performance of Power Utilities 2020-21, Power Finance Corporation. ***Chart:*** *Foundation for Democratic Reforms.*

[29] Power Finance Corporation Ltd. (2023). Report on Performance of Power Utilities 2021-22.
Power Finance Corporation Ltd. (2022). Report on Performance of Power Utilities 2020-21.
Power Finance Corporation Ltd. (2021). Report on Performance of Power Utilities 2019-20.

Table 7: States with the Most Financially Distressed Distribution Utilities		
State	**Annual Loss (FY22) (₹ Crore)**	**Outstanding Debt (as of FY22) (₹ Crore)**
Tamil Nadu	-16,518	153,909
Uttar Pradesh	-6,492	82,228
Rajasthan	2,374	65,945
Madhya Pradesh	-2,159	52,474
Maharashtra	684	44,026
Andhra Pradesh	-2,595	36,428
Telangana	-831	29,197
Karnataka	4,719	29,564
West Bengal	1,045	16,616

FY: Fiscal Year

Source:
1. Report on Performance of Power Utilities 2020-21, Power Finance Coporation.

These deficits in the power sector will inevitably grow over the next two or three decades on account of the necessary and inevitable transition to renewable energy. On the one hand, high paying customers will switch to rooftop solar and other renewable power sources with net metering system. On the other hand, the utilities will still have to service agriculture and low-end customers whose tariffs will not recover the cost of supply. At the same time, the utilities will have to maintain the base load stations for all customers to meet the night time needs of consumers who switched over to solar power. The utilities will also have to honour the Power Purchase Agreements (PPAs) with Independent Power Producers (IPPs) and generation companies (GENCOs) as their power plants are installed at enormous capital cost. This additional burden of energy transition has to be borne either by the consumers through tariffs, or by the exchequer through taxes. Consumers are already heavily subsidised, and there is a limit beyond which taxes cannot be raised. High taxes will not only be politically painful, but are impractical. There is a relationship between GDP per capita and tax-to-GDP ratio of a nation. India's tax-to-GDP ratio is about 18-19% for the Union and States put together (refer Annexure 11), and this ratio is comparable to other economies with similar GDP per capita (Table 8).

Table 8: Tax-to-GDP Ratio and Per Capita Income of Select Countries				
Country	**Tax-to-GDP Ratio (%)**		**Per Capita Income (Nominal, in USD)**	
	2018	**2020**	**2018**	**2020**
India	19.5	19	1,974	1,910
China	17.4	20.1	11,074	10,409
Vietnam	23.2	22.7	3,267	3,586
Malasiya	12.5	11.4	11,074	10,161
Indonesia	11.9	10.1	3,903	3,894
United States	24.9	25.8	62,823	63,531
United Kingdom	32.4	32.1	43,306	40,319

Source:
Tax-GDP Ratio
1. For China, Indonesia, Malaysia,Vietnam – Revenue Statistics in Asia and the Pacific 2022: Strengthening Tax Revenues in Developing Asia, OECD, 2022.
2. For United Kingdom, United States – Revenue Statistics 2022: The Impact of Covid-19 on OECD Tax Revenues.
3. For India – FDR's calculations. See Annexure 11 for more details.
Per Capita Income
4. World Bank Open Data Portal.

While more efficient tax collection may raise the tax-to-GDP ratio marginally, raising that ratio significantly is not a realistic proposition because of poverty and relatively poor delivery of services. These challenges of energy transition will have to be faced by all countries. For India, the pre-existing crises in power sector finances and public finances will make it twice as hard. It requires a detailed study to estimate the resource needs for energy transition. Some global studies indicate that about $15 Trillion may be the additional global cost of energy transition, and it is reasonable to assume India will probably have to spend about 6-7% of it, or $1 Trillion, or about ₹ 80 lakh crore over 20 or 30 years.

4.4. Perils of Non-recovery of Costs

Increasingly, there is a tendency on the part of political parties and elected governments to offer free power, water and other services and commodities. What started as free, unmetered power to farmers has spread to other services like water. In Punjab, with free power up to a consumption of 300 units per month, it is reported that almost 90% of households are covered by free power.[30] In an already stressed sector like electricity, free power is further deepening the financial crisis, with losses and debt burden mounting. But the loss to society is greater than the financial loss to the utilities. Free supply of power, water or other services weakens consumer voice and accountability. Over time, the quality of services will decline on account of inadequate resources to maintain the system properly, and the loss of consumer voice and accountability. This leads to a downward spiral and a vicious cycle of inadequate resources, weak consumer voice and accountability, decline in quality of services, erosion of assets over time and eventual collapse of the service.

Increasingly many paying customers are reducing dependence on public service delivery and opting for privately funded models like gated communities with all amenities, and they are isolating themselves from the rest of society and polity. The net result is increasing decay of public systems and infrastructure, greater class division and ghettoisation, and potential rise in crime, violence and disorder, further depressing growth, and deepening the fiscal crisis.

5. Union's Structural Revenue Deficit

The foregoing data and analysis clearly show that there is an urgent and vital need to improve the health of public finances in States. The problem is not limited to States. The Union finances have been managed more prudently by successive governments since 1991. However, the Union has a structural revenue deficit[31].

[30] Department of Finance, Government of Punjab. (2023). Budget Speech 2023-24.

[31] The advocacy paper uses the concept of structural revenue deficit as a measure to evaluate the net resources available to the Union. It is crucial to note that not all revenue raised by the Union is at its disposal. Over 56% of the resources raised by the Union are shared with the States for various purposes (see Table 9). This includes constitutionally mandated devolution of taxes, resource transfer for Centrally Sponsored Schemes, and other grants, loans or transfers to States. Additionally, the Union has committed expenditure obligations, including salaries, pensions and interest payments. By taking into account all these transfers and obligations, the measure provides a more realistic assessment of the actual funds available to the Union for developmental initiatives or address other priorities outlined by the government or the legislature.

As Table 9 shows, after transfers to States (including for centrally sponsored schemes, and capital investment support), interest payments, salaries and pensions, the Union is saddled with a structural deficit of over ₹ 2.57 lakh crore.

The Union has no control over this expenditure. Sudden cessation of Centrally Sponsored Schemes, MGNREGA etc will create havoc. Even though a part of transfers to States are for capital expenditure, the fact of the matter is the Union has a revenue deficit of ₹ 8.69 lakh crore in FY 2023-24 even after accounting for this capital spend. In any case, the Union too is starved of resources for investment for future growth or to assist the States in case of a fiscal crisis. The reversal to the unfunded OPS in some States poses a significant threat to the sound fiscal health of the country. There is a widespread misconception in the country that the Union

Table 9: Structural Deficit of the Union Government (₹ Crore)[1]

	Heads	2019-20	2020-21	2021-22	2022-23 RE	2023-24 BE
A	Gross Revenue of the Union Government[2]	2,151,083	2,137,859	2,913,780	3,220,865	3,571,508
B	Resources Transferred to States and UTs with Legislatures	1,282,648	1,355,293	1,778,224	1,852,702	2,010,785
	Devolution of States share in Taxes	650,678	594,997	898,392	948,406	1,021,448
	Other Transfers including Finance Commission Grants and Centrally Sponsored Schemes[3]	631,970	760,296	879,832	904,296	989,337
C	Salaries and Pensions (including Defence)	618,935	673,919	634,725	724,364	737,930
D	Interest Payments	612,070	679,868	805,499	940,651	1,079,971
E	**Net Resources available with the Union (A-B-C-D) / Structural Revenue Deficit of the Union**	**-362,570**	**-571,221**	**-304,668**	**-296,852**	**-257,178**
F	Revenue Deficit (-)[4]	-666,545	-1,449,599	-1,031,021	-1,110,546	-869,855
G	*Revenue Deficit as a percentage of GDP*	*3.3*	*7.3*	*4.4*	*4.1*	*2.9*

BE: Budget Estimates; **RE:** Revised Estimates; **GDP:** Gross Domestic Product

Note:
1. **Structural Revenue Deficit of the Union Government** = [Gross Tax Revenue + Non-Tax Revenue excluding Dividends and Profits] - [Devolution of States share in Taxes + Other Transfers to States + Salaries and Pensions + Interest Payments]
2. Gross Revenue of the Union Government includes Gross Tax Revenue (before Devolution and Transfers to States) and Non-Tax Revenue (excluding Dividends and Profits).
3. Other Transfers include Centrally Sponsored Schemes, Finance Commission Grants, and Other Grants/ Loans/ Transfers.
4. The significant difference between Structural Revenue Deficit and Revenue Deficit is seen on account of the Union Government's expenditure on Central Sector Schemes. The Revenue Expenditure on Central Sector Schemes (in crore) is ₹ 446086, ₹ 968811, ₹ 741888, Rs. 832870, and ₹ 695454 for FY 2019-20, 2020-21, 2021-22, 2022-23, and 2023-24 (BE) respectively.

Sources:
Gross Revenue; Interest Payments; Revenue Deficit; Revenue Deficit as a Percentage of GDP
1. Budget at a Glance, Union Budget Documents of 2021-22, 2022-23, 2023-24.
Transfer of Resources
2. Budget at a Glance (Full), Union Budget Documents of 2021-22, 2022-23, 2023-24, pg. 8.
Salaries
3. Expenditure Full Profile, Union Budget Documents of 2021-22, 2022-23, 2023-24.
Pensions
4. FY 2019-20 & 2020-21 - Comptroller and Auditor General of India, "Report No. 31 of 2022 - Financial Audit of the Accounts of Union Government", pg. 22 (2022).
5. FY 2021-22 - Lok Sabha reply, unstarred question no. 2961, dated 03.08.2022.
6. FY 2022-23 & 2023-24 - Expenditure Full Profile, Union Budget Documents of 2023-24.

government has unlimited funds at its disposal, and can come to the rescue of States whenever needed. The truth is that Union finances are precarious too, and there is very little room to assist the States.

Non-discretionary expenditure of the Union in the form of interest payments, wages and pensions cannot be reduced in the short-term. Only long-term prudent fiscal management will reduce the debt-GDP ratio, and therefore interest burden as a share of public expenditure. Wages are unlikely to be reduced as a share of expenditure even in long-term. Pension payments as a share of total expenditure will reduce gradually after another decade as employees recruited after 2004 and eligible for NPS start retiring. Even then, it will take decades for the pension burden on the exchequer to cease.

The discretionary expenditure of the Union that should be reduced is largely in two baskets. First, the large subsidies mostly on food, fertilizer and fuel accounting for over 2% of GDP[32]; and second the Union share of Centrally Sponsored Schemes and statutory programmes like employment guarantee. Given the nature of our political economy and federalism, food fertilizer and fuel subsidies will take a long time to be reduced or eliminated. Centrally Sponsored Schemes need to be rationalized and integrated further, but sudden cessation of these programs may undermine development goals.

As noted in section 'Union Oversight of State Debt', the States account for nearly two-thirds of the total government expenditure, and the Union's share is only a little over a third. Also, as discussed, the Union is the ultimate guarantor of the fiscal health of India, and individual States cannot go bankrupt without jeopardising the Union and the rest of the country. Therefore, concerted efforts are needed to address revenue deficits both at the State and the Union level. It is realistic that all States can meet a zero revenue deficit target within 1-3 years; but the Union may need up to five years to restructure its finances and meet a revenue deficit target of zero even as the

[32] Budget Division, Ministry of Finance. (2023). Budget At a Glance (Full). Retrieved from https://www.indiabudget.gov.in/

transfers to States are not affected significantly. In the long run however, with the NPS firmly in place, the Union will be well placed to manage the public finances provided no future government reverts to OPS. Such a switch to OPS will spell a disaster to future public finances and growth prospects of the country, and will severely undermine India's credibility in the world, and seriously dampen investments and erode our credit-worthiness.

6. Union Oversight of State Debt

There is a need to judiciously and equitably apply the powers conferred on the Union government under Article 293, clauses (3) & (4) of the Constitution of India, particularly in the context of the Indian fiscal framework. Article 293 (excerpt given below) gives the Union the authority to monitor and regulate the fiscal health of States –

(3) A State may not without the consent of the Government of India raise any loan if there is still outstanding any part of a loan which has been made to the State by the Government of India or by its predecessor Government, or in respect of which a guarantee has been given by the Government of India or by its predecessor Government.

(4) A consent under clause (3) may be granted subject to such conditions, if any, as the Government of India may think fit to impose.

Article 293 clearly is not aimed at restricting the political choices or policies of a State. However, the financial stability of a State is regarded as vital, and should be protected by the Union. The mechanism that the Constitution envisages in normal times to enforce fiscal discipline in States is the requirement of prior consent of the Union to incur any debt burden in States. Article 293(4) goes beyond a debt limit, and empowers the Union to impose such conditions as deemed fit to protect the financial stability and fiscal future of the State.

Given India's political economy, the Union's authority to regulate State borrowings is liable to be questioned on the premise that such a power amounts to excessive Union intervention and control over States' autonomy. That States in a federation ought to be able to manage their revenue generation and expenditure as they see fit according to their local needs and conditions is a valid argument. However, in India the Union is the ultimate guarantor of fiscal and financial stability, and States cannot go bankrupt. In the final analysis, all public debt is general government debt, and there is an implicit Union guarantee of all public debt. That is why Article 360 (excerpt given below) provides for proclamation of financial emergency, and transfers the fiscal responsibility to the Union –

> *(1) If the President is satisfied that a situation has arisen whereby the financial stability or credit of India or of any part of the territory thereof is threatened, he may by a Proclamation make a declaration to that effect.*
>
> ...
>
> *(3) During the period any such Proclamation as is mentioned in clause (1) is in operation, the executive authority of the Union shall extend to the giving of directions to any State to observe such canons of financial propriety as may be specified in the directions, and to the giving of such other directions as the President may deem necessary and adequate for the purpose.*
>
> *(4) Notwithstanding anything in this Constitution –*
>
> *(a) any such direction may include –*
>
> *(i) a provision requiring the reduction of salaries and allowances of all or any class of persons serving in connection with the affairs of a State;*
>
> *(ii) a provision requiring all Money Bills or other Bills to which the provisions of article 207 apply to be reserved for the consideration of the President after they are passed by the Legislature of the State;*

> *(b) it shall be competent for the President during the period any Proclamation issued under this article is in operation to issue directions for the reduction of salaries and allowances of all or any class of persons serving in connection with the affairs of the Union including the Judges of the Supreme Court and the High Courts.*

From the explicit wording of Article 360, it is clear that the constitution-makers recognised that the a threat to the financial stability of any part of the territory of India is a threat to the financial stability and credit of India. The explicit powers of the Union to deal with such a threat include giving "directions to any State to observe such canons of financial propriety as may be specified", directing reduction of salaries of all or any class of public servants, and a direction requiring all Money Billls to be reserved for the consideration of the President after they are passed by the State Legislature. Clearly, the Constitution does not envisage a State or a constituent unit of the Indian Union going bankrupt and left to its own devices. The Union is the guarantor of the financial stability and credit of India across all tiers of government. Similarly, Article 293 is essentially a framework to ensure that States have the total autonomy as per the local economic needs and political judgement subject to the boundaries fixed by the needs of protecting the financial stability and credit of India, sustainability and intergenerational equity. Therefore, given the nature of the Indian federation, both in terms of the broad constitutional framework and the subsequent evolution in Union-State relations with respect to fiscal matters, Union has a vital role in regulating States' debt. Transparency, fairness and credibility of the process can be ensured if the exercise of such control is based on the advise of an independent non-partisan authority whose recommendations apply equally to the Union and the States.

6.1. A Case for Control of Subnational Debt[33]

It is now a well established principle that macroeconomic management in our federal system including redistribution and stabilisation is a Union government function as it serves national interests and has significant spillover effects across subnational units.[34] Fiscal policy, and therefore financing of government expenditure, is a critical component of macroeconomic management. Owing to their proximity to the people, provincial or State governments are generally responsible for providing a wide range of public goods and services, while the Union is assigned taxes with a wider base as a matter of administrative efficiency. Consequently, federal systems resort to fiscal transfers, both vertical and horizontal, to equalise the imbalances in revenues and expenditure requirements.[35]

In most federal countries, including India, subnational governments enjoy great autonomy in financial matters – contracting debt, giving guarantees and undertaking large-scale infrastructure projects.[36] However, excessive debt and unsustainable finances at the State level pose great risks for the macroeconomic stability of the country as a whole. Although the public finances in a federal system are inextricably intertwined, subnational interests may not always align with the overall need for macroeconomic stability, as narrow provincial and short-term considerations take precedence. The risk is particularly high in an electoral democracy. Further, a system of intergovernmental transfers designed to fill any gap between the spending and revenue generation responsibilities of the subnational units increases the risk of moral hazard, disincentivising fiscal discipline which is politically unpopular in the short-term (Revenue Deficit Grants in India).

In an efficient financial system, "expenditure responsibilities would be matched with revenue resources, revenue capacities matched with political accountability, and

[33] This section of the paper is written with contributions from Pranay Kothasthane, Deputy Director, Takshahila Institution.
[34] Shah, A. (Ed.). (2008). Federalism and Macroeconomic Performance. In Macro Federalism and Local Finance. World Bank.
[35] Ter-Minassian, T. (1997). Decentralisation and Macroeconomic Management. International Monetary Fund; Singh, N.K. (2020). Fiscal Federalism in India. In Local Public Finance and Capacity Building in Asia: Issues and Challenges. OECD.
[36] Saxena, S. (2022). How to Manage Fiscal Risks from Subnational Governments. International Monetary Fund.

benefit areas matched with financing areas".[37] In other words, there should be a high degree of overlap between those who decide, those who benefit, and those who pay. However, when it comes to OPS, this alignment is lacking. The beneficiaries of OPS tend to be a small portion of the overall tax-paying population in a state. On the other hand, given the financial unsustainability of the measure, the economic burden of a state's OPS will also be borne by future citizens from other states. Such a system creates an unfair liability for individuals who do not influence decision-making.

This mismatch between the beneficiaries and payees is another reason why an intervention of the Union government is warranted. In his analysis of competitive federalism, Albert Breton identifies cost-benefit appropriability as a necessary pre-condition for competitive federalism to deliver results. He writes, "In competing to attract businesses to its jurisdiction, either by supplying particularly attractive local public goods, such as theatre, concerts, or dance, by offering tax advantages, or by buying part of the output of the sought-after enterprises, the government of a province should not be able to shift the burden of the offered amenities to the citizens of other jurisdictions."[38]

Maintaining cost-benefit appropriability is the *dharma* of the Union government in a federal structure. Hence, disincentivising states from shifting their burden to other states is necessary for healthy federalism.

It is important to note that India's general government (Union and States) expenditure in the pre-pandemic years was around 27% of the GDP (see Table 10); of this almost a third was funded by borrowings. Of the nearly ₹ 54.1 lakh crore spent by the governments in 2019-20, only about 35% was spent by the Union (about ₹ 19 lakh crore), and the States spent about 65% (about ₹ 35 lakh crore including Union transfers to States). The expenditure pattern indicates that States are playing a vital role in delivering services to the citizens. The Union is starved of resources on account of large transfers to States, leaving little to no scope for the Union to assist

[37] Bird, Richard M., and Enid Slack, eds. 2014. Local Taxes and Local Expenditures in Developing Countries: Strengthening the Wicksellian Connection. Public Administration and Development.

[38] Breton, A., Galeotti, G., Salmon, P., & Wimrobe, R. (Eds.). (1987). Towards a Theory of Competitive Federalism. European Journal of Political Economy, Special Issue, Vol. 3.

the States in case of fiscal distress (see section 'Union's Structural Revenue Deficit'). Thus, the expenditure pattern and debt burden of both the Union government and the State governments are important in determining the health of public finances, the sustainability and viability of public expenditure and fulfilling their basic obligations to the taxpayers.

Table 10: General Government Expenditure in India

Year	Level of Government	Expenditure[1]		
		Amount (₹ Crore)	As a share of GDP (%)	As a share of General Government Expenditure (%)
2015-16	**General Government**	**3,760,611**	**27.31**	
	State Government	2,360,229	17.14	62.76
	Union Government	1,400,382	10.17	37.24
2016-17	**General Government**	**4,265,969**	**27.72**	
	State Government	2,708,215	17.60	63.48
	Union Government	1,557,754	10.12	36.52
2017-18	**General Government**	**4,515,946**	**26.42**	
	State Government	2,924,599	17.11	64.76
	Union Government	1,591,347	9.31	35.24
2018-19	**General Government**	**5,040,747**	**26.67**	
	State Government	3,337,713	17.66	66.21
	Union Government	1,703,034	9.01	33.79
2019-20	**General Government**	**5,410,887**	**26.92**	
	State Government	3,495,003	17.38	64.59
	Union Government	1,915,884	9.53	35.41

RE: Revised Estimates

Note:
1. Union Government Expenditure here is calculated by subtracting State governments' expenditure from General Government Expenditure. Figures for Union Government Expenditure as a percentage of GDP are approximately 0.2 to 0.7% lower than the figures if calculated based on the expenditure amounts taken from Union Government's Budget documents (Union's expenditure after Transfers to States).
2. The figures for 2020-21 and 2021-22 have not been considered as they would be skewed because of the sudden surge in the Union government expenditure to cope with the COVID pandemic.

Source:
1. Economic Survey 2022-23, Statistical Appendix – Table 2.6.

Box 1: Sub-national Debt Regulation in Brazil

Similar to India, Subnational government spending in Brazil accounts for more than half of the total public spending in the country.[39] However, the process of fiscal decentralization in Brazil that began in the 1980s is also marked by federal bailouts of subnational governments on account of repeated episodes of fiscal distress. The major bailouts in 1993 and 1997 cost the federal government around 7.24% and 11.65% of the GDP, respectively.[40]

Consequently, the federal government introduced various constitutional and statutory measures to effectively regulate subnational debt and limit excessive expenditures at all levels of the government. Specific important fiscal rules in the Federal Constitution (1988) and the Brazilian Fiscal Responsibility Law, 2000 are given in the Table below –

Table I: Provisions Related to Subnational Fiscal Control in Brazil

Fiscal Rule	Description of the Rule	Relevant provision in the Constitution or Statute	Effective for
Golden Rule	Forbids credit transactions which exceed the amount of capital expenditure	Constitution[1]- Art.167, III; FRL[2]- Art.32, §3	All levels of government
Consolidated Debt Limit	The Senate sets limits on the consolidated debt by a resolution (as proposed by the President)	Constitution - Art.52, VI; FRL - Art.30, I; Federal Senate Resolution No. 40/2001	Sub-national governments
Social Security Expenses	No social welfare benefit or service may be created, increased or extended without corresponding source of funding	Constitution - Art. 195, §5	All levels of government

Note:
1. **Constitution** – Constitution of the Federative Republic of Brazil 1988.
2. **FRL** – The Brazilian Fiscal Responsibility Law 2000 (Lei de Responsabilidade Fiscal).

Along with the constitutional and statutory provisions, the federal government uses administrative controls to regulate States' debt. States that breach any one of the fiscal rules are penalized by forbidding further credit operations and curtailing

[39] Medas, P., et al. (2020). Brazil Technical Assistance Report - Strengthening Fiscal Responsibility at the Subnational Level (IMF Country Report No. 20/227) (p. 10). International Monetary Fund.
[40] Bevilaqua, A. S. (2002). State Government Bailouts in Brazil (Research Network Working Paper #R - 441)(pp. 20, 33). Inter-American Development Bank.

new voluntary transfers from the federal government.[41] In addition, the National Monetary Council (CMN),[42] comprising the Minister of Finance, the Minister of Planning, and the Governor of the Central Bank of Brazil, sets rules limiting the supply of domestic bank credit to the States.[43]

6.2. Indian Constitutional Framework Warrants Union Control over State Debt

The fundamental principle that informed the constitution-makers in determining the fiscal relations between the Union and the States is that India is one indivisible economic unit. Shri K.M. Munshi (being a member of the Drafting Committee and the Union Powers Committee) forcefully made the point during the discussion on the article relating to Financial Emergency (Article 360; Article 280A in the Draft Constitution):

> *"...This article in the Constitution is the realisation of one supreme fact that the economic structure of the country is one and indivisible. If a province breaks financially, it will affect the finances of the Centre: if the Centre suffers, all the provinces will break. Therefore the interdependence of the provinces and the Centre is so great that the whole financial integrity of the country is one..."*

Such an interdependence between the Union and the States, and the States inter se is evident from the provisions relating to division of revenue heads and those relating to revenue sharing, not just vertically but also horizontally to ensure equity. Most taxing powers are assigned exclusively to either the Union or States with little overlap. Most of the broadbased and progressive tax handles are assigned to the Union (for instance – personal income tax, corporation income tax, central excise, customs), while States are assigned taxing powers relating to land (stamp duties and

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[41] According to Art.25 of the Fiscal Responsibility Law, voluntary transfers are the transfer of current or capital resources to another Member of the Federation, which does not arise from Brazilian constitutional or legal determination. As per Art.25, §3, Voluntary transfers relating to education, health, and social assistance actions will not be used to apply the sanctions.

[42] Banco Central do Brasil. (n.d). About the CMN (National Monetary Council). Retrieved May 11, 2023, from https://www.bcb.gov.br/en/about/cmnen

[43] Medas, P., et al. (2020). Brazil Technical Assistance Report - Strengthening Fiscal Responsibility at the Subnational Level (IMF Country Report No. 20/227) (p. 12). International Monetary Fund.

registration fees), sales tax/value added tax, excise on alcoholic products, taxes on motor vehicles and transportation. Introduction of GST in lieu of sales tax has furthered the economic integration of the country. Recognising the resulting imbalance between the revenue generation capacity of the States and their expenditure obligations, the Constitution provided for transfer of a share of Union revenues in the forms of tax devolutions and grants-in-aid.[44]

It is also noteworthy that the Constitution does not provide for bankruptcy of States. In times of grave crisis, the Constitution provides for Union government intervention to restore financial stability.[45] While it may be a sound principle that each subnational unit must be left to face the consequences of its fiscal decisions, it is not desirable in practice. First, bankruptcy of one State will adversely affect the rest of the country. Second, the people of the State should not be punished for the mismanagement of the government.

As seen in the earlier section on the Structural Deficit of the Union Government, transfers to States, as recommended by the Finance Commission, including grants to fill State revenue deficits, place a huge burden on the Union finances. Poor financial health of a State undoubtedly has several grave and long-lasting ramifications within its territory – diminished quality of public services, curtailed expenditure on productive long-term investments and lower growth prospects. Additionally, a fiscal crisis in one or more States will also severely affect the Union and all other regions in the country. It would mean a vicious cycle of strained Union resources (collected from across the country), more borrowing at the Union level to bail out the States in distress, lower available revenue for distribution between other States, reduced productive capital expenditure and therefore, significantly lower growth prospects.

In an effort to strike a right balance between fiscal autonomy of States and debt sustainability of the general government (Union and States), Article 293 was incorporated in the Constitution of India. As noted earlier, Article 293(3) confers on

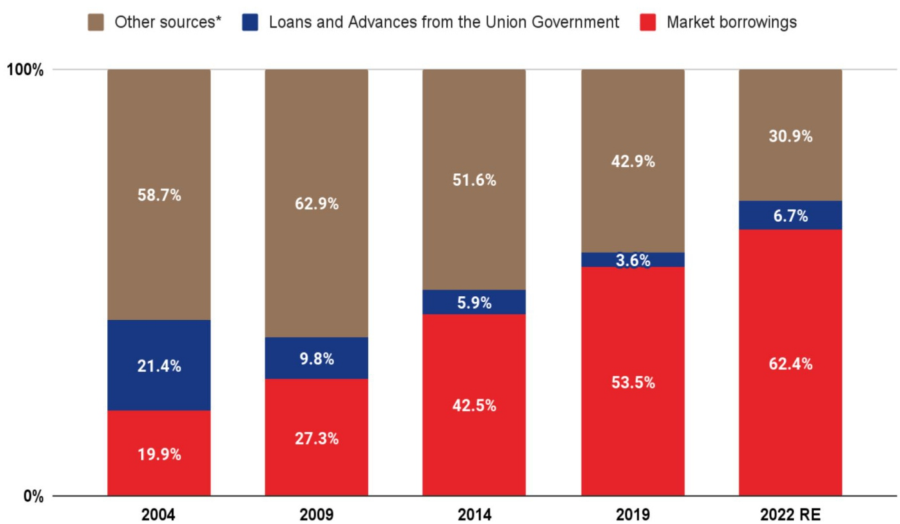
[44] Rao, M. G. (2007). Republic of India. In A. Shah (Ed.), The Practice of Fiscal Federalism: Comparative Perspectives (Vol. IV, pp. 160-162). A Global Dialogue on Federalism. Forum of Federations and the International Association of Centers for Federal Studies.

[45] The Constitution of India. (n.d.). Article 360.

the Union control over borrowing by States, the condition being that the State be previously indebted to the Union, and the mechanism being that such State shall require the prior consent of the Union for further borrowing. While all States still meet a part of their borrowing requirements by taking loans from the Union, their share in the total outstanding liabilities of States has been steadily decreasing (see Figure 9).

Figure 9: Composition of Outstanding Liabilities of States and UTs (in %)

Outstanding Liabilities do not include Off-budget Borrowings/Government Guarantees



UT: Union Territory with Legislature

**Other sources of financing of the GFD include cash drawdown balance, special securities issued to NSSF, loans from Banks and FIs (NABARD, LIC, NCDC, SBI etc.), state provident funds, reserve funds, deposits and advances, other public account transactions etc. The figures are on a 'net' basis.*

Data Source: *'State Finances: A Study of Budgets' reports, RBI. More details in Annexure 12.*
Chart: *Foundation for Democratic Reforms.*

The quantum of market borrowings of States has increased 23 times between FY04 and FY22 (RE) whereas it only doubled in case of loans and advances from the Union government, indicating greater reliance of States on the market for financing needs. As of FY22 (RE), State governments' total outstanding liabilities (excluding off-budget borrowings) are at ₹ 6,793,770 crore, with 62% (₹ 4,235,944 crore) borrowed from the market and 6% (₹ 457,434 crore) from the Union government.

This is a significant change from FY04 when market borrowings accounted for 19% (₹ 179,917 crore) of total outstanding liabilities, and loans and advances from the Union government accounted for 21% (₹ 192,981 crore).

In light of these changes, the Fourteenth Finance Commission (2015-20) recognised the potential for States to no longer be indebted to the Union in the future.[46] As the Commission noted, several States with strong economies may reach this point within a decade. In such a scenario, as States repay debts to the Union fully, there will be no constitutional constraint on market borrowings by States. Fiscal profligacy at any level can severely undermine the fiscal health and credibility and creditworthiness of the Union of India. States cannot go bankrupt in our constitutional scheme of things, and the Union is the ultimate guarantor of all public debt, and custodian of our economy. Therefore there is a need to create mechanisms to ensure that the Union can invoke powers under Article 293 in a fair and prudent manner, so that fiscal profligacy at all levels is curbed.

6.3. Implicit Sovereign Guarantee Renders Market Forces Ineffective

Vesting the Union with the authority to regulate State debt is perfectly legitimate in light of the current practice of raising market borrowings in India (see section 'Indian Constitutional Framework Warrants Control Over States' Debt'). Mandating a proportion of bank deposits to be invested in State Development Loans and the implicit guarantee offered by the Union government to such borrowings necessitates Union oversight.[47] These twin features distort incentives and render market forces ineffective in disciplining State governments. They lead to softening of budget constraints or give rise to expectations, both in State governments and the markets, that overshooting budget constraints is not a cause for concern. Therefore, the terms of borrowings of States do not reflect their individual creditworthiness.[48]

[46] Fourteenth Finance Commission. (2014). Chapter 14. In Fourteenth Finance Commission Report (p. 200).

[47] Rangarajan, C., & Prasad, A. (2013). Managing State Debt and Ensuring Solvency: The Indian Experience. In Till Debt Do Us Part. The World Bank.

[48] McCarten, W. J. (2003). The Challenge of Fiscal Discipline in the Indian States. In J. Rodden, G.S. Eskeland, & J. Litvack (Eds.), Fiscal Decentralisation and the Challenge of Hard Budget Constraints (Chapter 8). Massachusetts Institute of Technology.

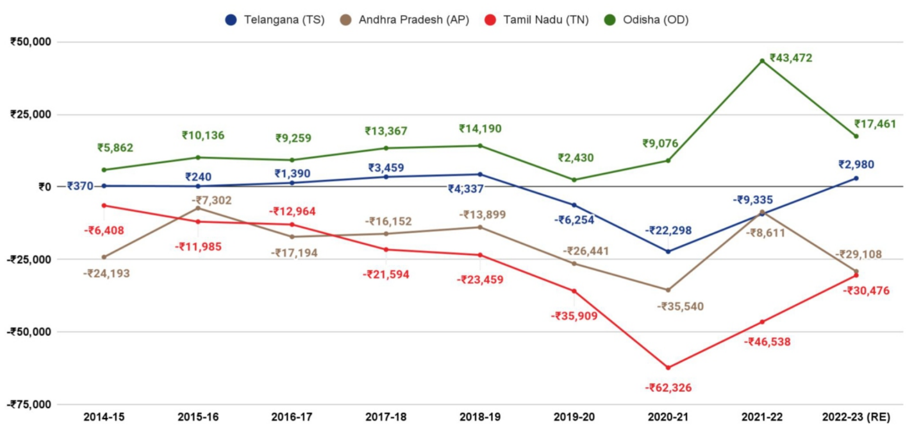
The burgeoning debt and the resultant fiscal crisis seen across major States in India during the late 1990s and early 2000s illustrates the risks in the Indian fiscal system. With greater State autonomy in financial matters post-1991, but inadequate market safeguards, fiscal profligacy in pursuit of populism could not be constrained.[49]

Therefore, given the specific features of the Indian financial system as envisaged by the Constitution as well as the subsequent evolution of Union-State relations, Union oversight and control of State debt is indispensable.

7. A Case Study: Telangana, Andhra Pradesh, Tamil Nadu & Odisha

An analysis of public finances of select States reveals that even States which have great advantage because of high industrialisation, high per capita income and big cities as engines of rapid growth can incur huge revenue deficits if they are lax about the health of public finances. Similarly, even the States with low per capita income and no advantage of big cities can manage their finances well and show healthy revenue surpluses. What is more, political stability, electoral viability and healthy public finances can go together. Figure 10 and Table 11 show the comparison between Telangana State, Andhra Pradesh, Tamil Nadu and Odisha.

Figure 10: Revenue Balance over the Years of Select States – TS, AP, TN & OD (₹ Crore)



Data Sources: *RBI Handbook of Statistics on Indian States 2021-22, State Budget documents & PRS State Budget Analyses.*
Chart: *Foundation for Democratic Reforms.*

[49] Ibid; Supra note 47.

The Telangana State was projected to have the highest surplus resources, post-devolution, of about ₹ 1,18,000 crore between 2014-15 and 2019-20, as reported by the Fourteenth Finance Commission.[50] However, fiscal profligacy in the form of ISWs, significant increase in wages of government employees, and vast expenditure on unviable capital projects have created fiscal stress. The State should have sustained a consistently healthy revenue surplus owing to a the booming economy of a big metropolis (Hyderabad) accounting for nearly 30% population of the small state; however, Telangana recorded a revenue deficit in 2019-20, which increased substantially to over ₹ 22,000 crore by 2020-21.[51] Though the State has improved it revenue balance, recording a revenue surplus in 2022-23 (RE), the substantial ISWs, investments in unviable large capital projects, and the long-term burden of high-cost maintenance of those projects are still a threat to the healthy state of public finances.

Andhra Pradesh, which had suffered on account of loss of revenue from a big metropolis (Hyderabad) with the division of the State, started with a huge revenue deficit. Because the State increased wages substantially and opted for multiple ISW programmes at high cost, the revenue deficit has mounted despite significant support of the Union government in view of division of the State and loss of revenues. The power sector losses are relatively high because of ISW in the form of free power.

Tamil Nadu is a relatively prosperous State with a high degree of urbanisation and industrialisation, a big metropolis as a growth engine and high per capita income. Despite that, fiscal profligacy in the form of ISWs and relatively low revenue mobilisation meant that revenue deficits are very high. Even more striking, Tamil Nadu, which has a relatively small agricultural economy, is incurring huge annual losses of power distribution companies, and the DISCOMs are weighed down by a mountain of debt.

When you compare these States with Odisha, the contrast cannot be more glaring. Odisha is relatively a less developed State with low per capita income and low

[50] Fourteenth Finance Commission. (2014). Chapter 11. Fourteenth Finance Commission Report (p. 149).
[51] Finance Department, Government of Telangana. (2022). Telangana Budget in Brief 2022-23 (p. 4).

urbanisation. And yet, Odisha has consistently generated healthy revenue surpluses, and the power utilities are well-managed and outstanding debt of DISCOMs is very low (see Table 11).

Table 11: Per Capita Income & Losses of Distribution Utilities of Select States

Parameter	Telangana	Andhra Pradesh	Tamil Nadu	Odisha
Population (Crore)	3.85	5.39	7.78	4.63
Per Capita Net State Domestic Product (₹)	275,443	192,587	241,131	124,669
Annual Losses of DISCOMs (₹ Crore)	-831	-2,595	-16,518	940
Outstanding Debt of DISCOMs (₹ Crore)	29,197	36,428	1,53,909	1,368

Note:
1. Population figures here are the State's projected population in 2020, as given by UIDAI.
2. Annual Losses and Outstanding Debt of DISCOMs are for 2021-22.

Source:
Population
1. Projections 2020, State-wise Aadhar Saturation by UIDAI
Per Capita Net State Domestic Product
2. Andhra Pradesh - Socio Economic Survey 2022-23, Planning Department, Government of Andhra Pradesh.
3. Telangana, Tamil Nadu, Odisha - Table 1.11A, Per Capita Net State Domestic Product at Current Prices (2011-12 Series) as on 01.08.2022, Statistical Appendix, Economic Survey 2022-23.
Annual Losses and Outstanding Debt of DISCOMs
4. Report on Performance of Power Utilities 2021-22, Power Finance Corporation.

Sound Fiscal policies and good health of public finances are not necessarily politically costly. The government in Odisha has been politically stable and popular, and the governing party is consistently winning elections since 2000. The Odisha story illustrates that balancing ISWs with growth, and fiscal prudence with political viability is eminently feasible.

8. Requirements of a Politically Viable Framework

What then is a realistic framework for promoting fiscal health in a politically viable manner? First, we should identify the minimum requirements of an effective model that will achieve the desired objective. A set of these requirements is listed here for wide public debate and careful consideration. The requirements are in consonance with the three-pillar approach as laid down by the Fifteenth Finance Commission for the twenty-first century fiscal architecture. The approach includes: first, fiscal rules across all levels of government which set the institutional and budgetary framework for fiscal sustainability; second, a public financial management system which provides complete, consistent, reliable and timely reporting of the fiscal indicators that are part of the first pillar; and third, an independent assessment mechanism so as to provide assurance and advice on the working of the other two pillars.[52]

The requirements of a viable framework are:

- i The model should be acceptable across the society and the political spectrum.
- ii. It should enable the Union and States to work in harmony with a common purpose, not at cross purposes.
- iii. The indicators identified should be measurable, reasonable, and widely understood and accepted.
- iv. The goals set should be realistic and achievable in a reasonable timeframe with reasonable restraint and prudence.
- v. The norms should be applied uniformly for all States in a non-partisan manner.
- vi. The norms should apply to the Union as well in an impartial and transparent manner, giving due allowance to the structural deficit imposed on the Union.
- vii. The sovereignty of elected legislatures and governments should be respected, and there should be enough flexibility of political choices and resource deployment without micro-management from outside.

[52] Fifteenth Finance Commission. (2020). Chapter 13. In Fifteenth Finance Commission Report (p. 379)

viii. The perverse and paradoxical short-term incentive to revert to OPS should be eliminated, and any governmental decision regarding such policies must not violate the principle of inter-generational equity.

ix. The employees should have the choice of pension fund management under NPS based on their risk appetite, provided that pension payments are fully supported by past contributions to the fund, thereby ensuring no burden on future taxpayers.

x. The perverse incentive of revenue deficit grants to States under Finance Commission awards should be eliminated, so that the burden of fiscal profligacy in States is not transferred to the Union.

xi. There should be reasonable safeguards to ensure that revenue expenditure is not misclassified as capital expenditure, and the capital deployed meets reasonable standards of cost-benefit analysis without external micro-management.

9. Outlines of a Politically Viable Framework

9.1. Key Features

Based on the above requirements, the following could be the key features of a viable framework for ensuring fiscal prudence in the Union and States.

9.1.1. Bring Revenue Deficit of States Down to Zero

Along with the existing norms of FRBM Act, viz: Fiscal Deficit (FD) and Debt-GSDP ratio, Revenue Deficit targets should be reinstated for both the Union and the States (in the Finance Act 2018, the Revenue Deficit target was deleted from the Union government's FRBM framework).[53] An adherence to zero revenue deficit would be the only politically viable, practically feasible, and widely acceptable norm to ensure fiscal health of the Union and States. In respect of States, a maximum period of three years may be allowed to reach the target, subject to the condition that revenue deficit should show a steady and significant decline annually during this period. The States that already have no revenue deficits should be required to show steady increase in revenue surpluses during the period.

9.1.2. Bring Revenue Deficit of the Union Down to Zero

The Union has a structural deficit on account of huge transfers to States which cannot be reduced. At present the Union's Revenue Deficit as per 2022-23 RE and 2023-24 BE is ₹ 11.1 lakh crore (4.1% GDP) and ₹ 8.6 lakh crore (2.9% GDP) respectively (see Table 9). The Union may be given a period of five years if needed as per expert analysis, to meet the zero revenue deficit target. Corresponding amendments may be made in FRBM Act.

9.1.3. Uniform and Transparent Application of Provisions under Article 293(4)

The importance of the Union government's control over the debt of States cannot be overemphasised. Articles 293(3) and 293(4) of the Constitution establish the legal

[53] Fiscal Responsibility and Budget Management (Amendment) Acts, 2018, Part XV, s. 212.

framework for the Union to monitor and impose fiscal discipline on States (see section 'Union Oversight of State Debt'). Under Article 293(3), the Union's consent is needed for a State to borrow funds, and under Article 293(4), the Union may impose conditions for granting consent to States to borrow. States should be required to meet and maintain zero revenue deficit targets and subsequently revenue surplus targets under 293(4) as a condition for consent to borrow. Additionally, in respect of NPS, if any government wishes to opt out of it, the public finances of the State should be subjected to rigorous scrutiny and analysis, and such an option should be discouraged under FRBM Act provisions and the conditions that may be imposed under Article 293(4). If a State insists on unilaterally reverting to OPS, or continuing with OPS, then under Article 293(4) the State should be required to make annual allocation in current budgets the necessary amount for fulfilling future pension liabilities, calculated on discounted cash flow basis. In any case, the accumulated contribution to the pension fund under NPS should never be transferred upon reverting to OPS. Such a transfer of past savings under NPS to a State reverting unilaterally to an unsustainable, fiscally ruinous OPS will reward fiscal profligacy and create a dangerous perverse incentive. The accumulated fund in AUM pertaining to the State should be retained with AUM, and only the yields and income generated should be transferred annually to the State towards future pension payment. Appropriate provisions should be made in FRBM Act and other statutes relevant to long-term health of public finances.

9.1.4. Safeguarding the Future of the States that Revert to OPS

As noted earlier, five States have so far committed to restoring the OPS, with West Bengal never having opted for NPS. Narrow, short-term political considerations have outweighed considerations of long-term wellbeing of the people in those States. The ominous projections made by the Andhra Pradesh government (see section 'Horrendous Price with OPS') give a glimpse of the crisis that looms over the six States that have opted for the unfunded, index-linked, defined-benefit pension that imposes a future legal liability. A similar study in respect of all States by the

Economic Times (dated 6 March 2023) suggests that if all States revert to OPS, 40.5% of their own tax revenues will go into funding only the pensions by the year 2046-47. In respect of the five States that have now reverted to the OPS regime, the share of pensions in their own tax revenues would be 64.1%, as the average annual growth rate in pensions in those States was higher than the national average (the five States – 12.8%, national average – 11.9%) between 2013-14 and 2021-22, but the growth in own tax revenues was lower than the national average (the five States – 9.5%, national average – 10%).[54]

While the imminent danger is undeniable, there is a need to institutionalise a mechanism to prevent future fiscal disaster without impinging on the sovereign rights of the elected governments. As previously noted (see section 'Union Oversight of State Debt'), there is a compelling case for the Union to impose conditions under Article 293(4) to regulate borrowings by State governments. Considering how reverting to OPS alone throws the States into a debt-spiral in the future, it is incumbent upon the Union to prevent such a crisis to safeguard the interests of the people of the respective States as well as the whole country. Fiscal crisis or near-bankruptcy of one State has ripple effects on the financial prospects of all other States. Apart from future fiscal crisis, unfunded OPS imposes unjust and unsustainable burden on the future generations of taxpayers. Therefore the Union has the duty to protect these States and future generations by discharging the responsibilities entrusted to it under Article 293.

It is true that the choice of the pension scheme is a matter of policy that should be negotiated and decided between the people and the elected political leaders. However, our constitutional framework envisages certain limits or boundaries to be imposed in fiscal matters in order to preserve and protect the country's future.

Therefore, the following pre-condition may be imposed by the Union (or the independent institution exercising that authority) under Article 293(4) in order to permit borrowing by a State government in respect of States reverting to OPS:

[54] Gera, I. (2023, March 6). Reverting to old pension scheme to cost states dear, hit spending. The Economic Times. Accessed at: https://economictimes.indiatimes.com/news/economy/finance/reverting-to-old-pension-scheme-to-cost-states-dear-hit-spending/articleshow/98459825.cms?from=mdr

> Funds equivalent to the current value of the entire future pension outflow, calculated with the appropriate discount factor, to be allocated in the budgets concurrent to the years that the beneficiary employees are in service.

This condition is predicated on principles of fairness and justice. The voters and the elected governments are free to opt for a pension scheme where the future liability is funded in the current budget, so that there is no unjust burden on the future generation of taxpayers for the services rendered to the current generation.

A similar stand was taken by the Group to Study the Pension Liabilities of the State Governments (Reserve Bank of India, 2003), recognising that pre-funding would sensitise both the Governments and the employees of the actual burden of unfunded pension liability. It recommended setting up of a dedicated Pension Fund to meet the pension burden of the existing employees, in addition to a prospective introduction of a contributory element to civil service pensions in States.[55]

If the electorate and the legislature are willing to curtail the rest of the public expenditure and accept poor infrastructure and inadequate public services at the cost of quality of life and economic growth, that is an unfortunate choice they will make. But the consequences of the reckless populism should be borne immediately by the taxpayers, so that there is a more informed decision making, fully assessing costs and benefits; in any case the immoral and unjust practice of transferring the burden of current profligacy to the next generation should come to a complete stop. The principle of intergenerational equity cannot be violated. It is unjust for the voters and political leaders today to irrevocably bind the revenues generated by future taxpayers, without creating assets. Considering the fact that a lion's share of the future revenues will have to be diverted for outlay on unfunded, index-linked pensions, justice and fairness demand that long-term policy commitments, especially those incurring unproductive expenditure, be funded in the current budgets. The elected governments should be required to choose between disproportionate, unfunded future pensions to government employees and the socio-

[55] Reserve Bank of India. (2003). Report of the Group to Study the Pension Liabilities of the State Governments. (p. 83)

economic development of the State. Within these boundaries, that is a choice best left to the people and the elected governments in the State.

9.1.5. Centrally Sponsored Schemes: Restructuring for Better Fiscal Management

With States' reliance on Union borrowings reducing, it is critical to include provisions that allow the Union to exercise its powers under Article 293(3) rigorously and transparently. One such mechanism of ensuring application of Article 293(3) to all States is restructuring the transfers under Centrally Sponsored Schemes (CSS). The CSS exhibit the collective sense of national priorities set by the Parliament – provision of quality education and healthcare; basic service provisioning like sanitation and drinking water; strengthening agriculture, infrastructure etc. The Union, therefore, has an obligation to ensure that the money is utilised for the stated objectives. As per 2022-23 RE, over ₹ 4.5 lakh crore[56] are transferred by the Union to States towards CSS, constituting about 24% of transfers from the Union to States.[57] It is desirable to convert transfers under CSS as long-term, interest-free loans from the Union to States. Such an approach would serve two important purposes. First, it would ensure that the powers of the Union under Article 293(3) are further strengthened. The powers of the Union to approve State borrowings under Article 293 apply only when the State owes money to the Union. There is a potential danger of better-off States discharging all the debt to the Union, and then claiming sovereign power to borrow from the market without any restraint. Such a course will pave way for reckless borrowing, fiscal profligacy and eventual fiscal collapse. Fair and uniform application of provisions under Article 293(3) without any discretion is necessary for a sound fiscal edifice. While States' financial autonomy is important, it must not come at the expense of the country's overall fiscal health and cohesion. The exercise of powers under Article 293(3) must not be viewed as an infringement of States' rights, but rather as a safeguard to avert fiscal

[56] Budget Division, Ministry of Finance. (2023). Budget At a Glance. Retrieved from https://www.indiabudget.gov.in/doc/Budget_at_Glance/budget_at_a_glance.pdf

[57] The amount transferred towards Centrally Sponsored Schemes as per 2022-23 RE is ₹ 451901 crore, while the total transfers to States, including devolution, amount to ₹ 1852702 crore. Budget Division, Ministry of Finance. (2023). Budget At a Glance.

collapse, which is the path many States' political economies are taking. Second, extending funds as loans would aid in reducing the revenue deficit of the Union. As discussed previously (see section‘Union’s structural revenu Deficit’), the Union has a structural revenue deficit; CSS transfers totaling ₹ 4.5 lakh crore (2022-23 RE) are shown as the Union's revenue expenditure. Transferring the Union share of the CSS as interest-free loans would bring down the revenue expenditure of the Union and thus the revenue deficit. There is a strong case for transferring Union's share of the CSS to States as interest-free loans. Any asset created, be it by the Union or the States, is legitimate capital expenditure. The transfer of funds as interest-free loans would also put a greater obligation on the Union to ensure that resources are utilised for their intended purpose, that there is better control and monitoring, and that wasteful spending is avoided.

The following factors must be taken into account while providing for such interest-free resource transfer:

I The States must not be burdened with interest payment obligations on such loans; therefore, there will be no cash flow problems. The Union would have the discretion to waive loan repayment depending on the fiscal situation that evolves in future.

ii. Transfers for programmes backed by statute, such as the National Rural Employment Guarantee Scheme (NREGS), would continue as grants.

iii. The loans disbursed under CSS would be outside the ambit of FRBM limits and State borrowing ceilings, so that there is no sudden fiscal contraction.

iv. The Accountant General's (AG) office in each State must be strengthened to monitor resource utilisation. Banks, both public and private, must be required to provide the AG's office with information on all data related to public debt.

9.1.6. Transparent Accounting – Off-Budget Borrowings and Deferred Expenditure to be Fully Reflected in Budgets

As discussed in section 'Living Beyond Means', many States are resorting to off-budget borrowings, presumably to conceal the actual debt burden. Such a practice allows States to bypass fiscal responsibility norms with impunity. Therefore, all off-budget borrowings through SPVs, and government guarantees as loans to public entities should be required to be fully disclosed in the budget, as well as to the Union government. There are reports of Scheduled Commercial Banks, including Public Sector Banks refusing to disclose lendings to State governments even to Comptroller and Auditor General (C&AG). While client confidentiality is an important principle of running businesses, borrowings by governments cannot be covered by such privilege in a democratic society. Therefore statutory provisions should be made mandating full disclosure by banking institutions of all lendings to States and public entities.

There are reports that many State governments are simply postponing non-discretionary expenditure in order to conceal the real state of public finances. Delaying or deferring payments of dues to contractors and suppliers of public goods and services, deferring arrears on salaries and allowances to employees, and postponing other payments which are due are some of the tactics deployed to show compliance of FRBM norms. However, such deferment merely postpones the burden and makes the task of fiscal management much more difficult in succeeding years. Therefore it is vital that deferred, non-discretionary expenditure is transparently accounted for in full. Appropriate rules should be framed in the application of Article 293(3) and in respect of conditions imposed under Article 293(4). In respect of the Union government also such transparent accounting should be mandated and monitored by an appropriate authority like the Fiscal Council or Public Accounts Committee of Parliament.

9.1.7. Independent Exercise of Functions under Article 293

There should be an independent, credible institution to exercise the functions under Article 293, subject to any law or laws made by Parliament. Given the political sensitivity of the issue in a robust federal democracy, and the fierce political competition and intense polarization in the country, if the Union bureaucracy under direct political control exercises these functions, it will not carry conviction.

It will be best to insulate monitoring and decisions from the appearance of partisan politics, and entrust them to a professionally competent, independent, credible authority. One relatively easy and widely acceptable approach would be to entrust it to the Finance Commission (FC) established under Article 280 (refer Annexure 13). The FC has the competence, credibility and expertise, and has gained wide acceptance across the political spectrum over the decades. The FC needs to be made a permanent body like the Election Commission of India (ECI). Now it is an ad hoc body constituted every five years. Article 280 of the Constitution mandates that *"The President shall, ...at the expiration of every fifth year or at such earlier time as the President considers necessary, by order constitute a Finance Commission ...to be appointed by the President…"*. There are strong legal arguments that suggest that the FC can be made a permanent body within the existing provisions of Article 280, and a set of new Chairman and members may be appointed every five years. Utilising this provision, the FC may be made permanent body, and if deemed necessary, appropriate amendment to Article 280 may be carried out. Parliament may make a law entrusting the monitoring of the fiscal health of the Union and States and exercising the functions under Article 293 to such a permanent FC.

Alternatively a Fiscal Council may be constituted as per the recommendations of the FRBM Review Committee headed by Shri NK Singh. In either case, the FC or Fiscal Council should specifically be entrusted with the task of exercising the functions of Article 293 as explained above. The Permanent Finance Commission or the Fiscal Council should be empowered to monitor the fiscal health of both the Union and States, and the grant of consent for State borrowings should be subject to zero revenue deficit/revenue surplus targets, and such other conditions as may be imposed under Article 293 (4).

9.1.8. Phase out Revenue Deficit Grants to States

Special grants are now being provided to States to meet the Revenue Deficit. Such grants create a perverse incentive for States to overspend on revenue items and depend on GoI grants without any consequences. Therefore the Revenue Deficit grants to all States including special category States should be phased out with the end of the 15th Finance Commission period. Zero Revenue Deficit norm and future revenue surplus norms should be applicable to all States equally on a permanent basis.

9.1.9. Independent Analysis of Budgetary Proposals

In the UK, the Office for Budget Responsibility (OBR) was created in 2010, and given statutory status as a non-departmental public body under the Budget Responsibility and National Audit Act 2011.[58] The OBR is a central part of the UK's fiscal framework, with a main duty to examine and report on the sustainability of the public finances. Its primary role is to carry out independent and authoritative analysis of the UK's public finances. Its core functions include forecasts of the economy and public finances, evaluation of the government's performance against its fiscal targets, scrutiny of government's policy costings, assessment of the long-term sustainability of the public finances, and welfare spending analysis. OBR does not take any position on the policies or welfare programmes proposed, and does not make any policy recommendations. Its role is limited to independent and authoritative analysis, forecasts and costing. Similarly, the United States created the Congressional Budget Office (CBO) in 1974 as a nonpartisan body to produce independent analysis of budgetary and economic issues to support the Congressional budget process. With similar functions, and on the same lines, institutions exist in other countries, e.g. Parliamentary Budget Office in Australia, and Fiscal Council in several OECD countries.

[58] Office for Budget Responsibility. (2019). Office for Budget Responsibility and HM Treasury: framework document.

Independent, accurate and credible analysis, forecasts and costings of programmes are vital for a viable framework for fiscal prudence. Therefore an equivalent of Office for Budget Responsibility should be created in the Office of the permanent Finance Commission or the proposed Fiscal Council with similar functions as the OBR in the UK.

The Parliament may empower and strengthen the OBR by law to make it mandatory to subject all public finances and major expenditure proposals and welfare programmes to OBR's analysis, costing and forecasts. Such a process will inform the governments and legislatures of the Union and States of the long-term implications of their policy proposals and the sustainability of public finances. A healthy public debate based on verified facts and analysis will also promote public awareness and strengthen the framework for long-term health of public finances.

9.1.10. Cost-Benefit Analysis of Large Infrastructure Projects

Once the zero-revenue deficit norm is implemented fairly and uniformly, fiscal profligacy will give way to fiscal prudence. However governments sometimes do take up unviable, large vanity projects, investment in which cannot be justified by any meaningful cost-benefit analysis. The iron law of economics is that wants always outstrip resources, and there are always trade-offs in deployment of resources. If a private individual spends lavishly for unproductive purposes, their family alone suffers. If a private enterprise does not exercise prudence and sound judgement in expenditure and investments, the market will punish the company, and they will lose market share or become insolvent. But the government enjoys a monopoly in its functions, and there is no competition. A profligate government bankrupts the whole society and undermines the future of the succeeding generations by imprudent expenditure. And the government has coercive power to silence the people if there are no safeguards and checks and balances. There are increasing instances of governments incurring huge, unsustainable debts for unviable projects. The fact that such lavish expenditure is incurred under capital account does not promote the health of the public finances if the benefits are marginal, public finances are strained, debt burden is unsustainable, and the returns on investment are paltry or negative. Therefore very large public projects proposed by governments should be subjected to cost-benefit analysis by the OBR-like organisation proposed above. The authority to monitor fiscal health and accord approval for borrowing under Article 293 should have the power to withhold consent for such loans if the cost-benefit analysis shows that it will adversely affect the long-term health of public finances.

9.1.11. Measures to Secure Maximum Returns under NPS

Until 2019, the NPS funds of Union government employees were invested in a predefined pattern: upto 15% invested in equity investments and the balance invested in debt-related instruments. Since 2019, Union government employees have the option of choosing a pension fund manager and asset mix depending on their rik appetite. There are three options available to employees based on the cap on equity investments – upto 50% invested in equity instruments; upto 25% invested in equity instruments; and 100% invested in government bonds. In the first two schemes involving equity investments, with retirement approaching, exposure to equity comes down, and share of investments in bonds is correspondingly increased. However, the employees of State governments have no such flexibility in most cases. It is desirable that States give employees similar freedom of investment depending on their risk appetite, and multiple schemes may be offered enabling the employees to make informed choices. Also the States should be free to readjust the employee and employer contributions, provided the pension liability is fully funded through monthly contributions, and there will be no future burden on taxpayer towards pension payments. Union and States may also opt for greater flexibility in fund management in consultation with the employees. However, three basic principles should be followed:

i. The employee should have the choice of fund management depending on risk appetite.

ii. The pension fund should not be subjected to excessive risks, so that the employee's social security needs after retirement are met.

iii. The pension payments will be fully met from past contributions and growth of the fund, and there will be no burden on future taxpayers.

There are also many apprehensions in the minds of government employees about NPS. For instance, that OPS is replaced by fully-funded, contributory pension scheme is not widely understood. There is spread of misinformation that employees would not get pension after retirement. If the States face fiscal crisis on account of OPS, and if financial emergency becomes inevitable, employees may get no pension. Such a danger to future security of employees with OPS is not widely understood. An assured pension that is fully funded and kept separate from the general revenue of the government provides greater security in old age, rather than transferring the pension liability to the increasingly stressed exchequer. Similarly, OPS merely assures monthly pension, and the employee's successors do not get any lumpsum. But with NPS, part of the accumulated pension fund is transferred to the successors as a lumpsum, in addition to receiving pension until the end of life. And with capital gains in a growing economy, NPS could give significant pension benefits to employees. These merits of NPS vis-à-vis OPS need to be widely publicised among government employees through an imaginative campaign with credible brand ambassadors. A fixed share of AUM needs to be utilised for mass campaigns to promote NPS.

State governments opposed to a pure defined contribution-based pension system like the NPS because of social security concerns, may consider adopting a hybrid defined contribution-defined benefit model. This is one of the recommended models of the 2003 RBI Group[59] mentioned above (see section 'Safeguarding the Future of the States that Revert to OPS'). The State governments would guarantee a certain level of pension, which could be fixed at a certain percentage of average pay (say, 50% of the last 36 months pay). The employees would contribute a certain percentage (say, 10%) of their basic pay and dearness allowance, with matching contributions by the State governments.

[59] Reserve Bank of India. (2003). Report of the Group to Study the Pension Liabilities of the State Governments. (p. 78)

The actual rate of contribution by the employees and the State governments should be determined based on actuarial calculations to ensure that the contribution amount would be adequate to pay for the guaranteed level of pension. The other relevant factors for consideration would be assumptions regarding growth rate of salaries, return on investment etc. Any shortfall in returns to meet the pension requirement has to be met by the State governments. As recommended by the 2003 RBI Group, the contingent liabilities of the government can be minimised by a periodic adjustment of benefit and contribution rate based on a triennial actuarial review of the system.

The question of indexation of pensions is critical in a system where the benefits are defined. The benefits under the hybrid system should be price-indexed and not wage-indexed (see section 'FRBM and NPS – Acts of Foresight'). As noted in the report of the 2003 RBI Group, there is no justification for wage-indexation of State pensions in a country where government employees are financially more secure than the majority of other workforce. The report states, "The pension benefits of State Government employees are generally indexed to wages as well as prices. Studies have shown that, on an average, about 90 per cent of Government employees in India (mainly in Group 'D' and 'C' categories) earn more than their counterparts in the private sector. Such Government employees are in a better position to save for their future when compared to the average employees in a large number of private organisations, specially those working in informal/ tiny sector, Small and Medium Enterprises/ service sector organisations, etc. Hence, it would be quite fair and equitable to sanction to the Government employees an earnings related pension, which is price indexed, but not wage indexed. Furthermore, in a number of countries, the trend is to move from wage indexation to price indexation. The Group after examining the various issues, feels that there is no justification for providing the benefits of both wage and price indexation to the State Government pensioners, especially in view of the current fiscal stress faced by the State Governments. The Group recommends continuation of the present practice of price indexation (subject to the recommendation in the following paragraph), while doing away with wage indexation facility (i.e., increasing basic pension as and when salary structure is raised upward consequent on Pay Commission's award), wherever it exists". The fiscal situation and budgetary constraints of State governments make wage-indexation unviable.[60]

9.1.12. Progressively Increasing the Retirement Age

The changing demographic landscape and the need to address the fiscal burden on the exchequer necessitate a critical and continuous review of the retirement age of government employees in India. The retirement age of government employees, which stood at 55 years in 1950, still remains at 60 years in many States and in the Union government, despite the average life span rising from about 35 years in 1950 to about 70 years now[61]. The age of recruitment has been increasing over the years and individuals are entering the workforce at a later stage in life; however, the retirement age still remains low compared to the average life expectancy. The twin challenges of shorter career in government, and longer post-retirement lifespans need to be addressed so that the efficacy of delivery of services is enhanced, and fiscal burden on account of pension is sustainable.

The country is experiencing significant demographic changes that underscore the urgency to raise the retirement age. India's Total Fertility Rate (TFR – average number of children a woman bears in her reproductive life) is now below replacement level, and stands at 2.0[62]. While some of the large States have higher fertility rates, there is a secular trend of rapid decline in fertility rates in all States and all social groups. The working-age population is projected to start declining from 2036 as a result of decelerating population growth. The population growth rate has reduced from 2.2% in 1971 to 1.1% in 2021 and is projected to further decline to 0.7% by 2031[63]. This demographic transition will lead to a fall in the population between the age of 0-14 years, from 30.9% (384 million) of the total population in 2011 to 22% (336 million) by 2031. Although the share of working-age population

[60] Reserve Bank of India. (2003). Report of the Group to Study the Pension Liabilities of the State Governments. (p. 81)
[61] Department of Economic and Social Affairs, United Nations. (2013). World Population Prospects (2012 Revision).
[62] Ministry of Health and Family Welfare. (2022, December 13). Press Information Bureau. Release ID: 1883140.
[63] Ministry of Statistics and Programme Implementation. (2022). Women & Men in India 2022: Table 1.1. Retrieved from https://mospi.gov.in/publication/women-men-india-2022.

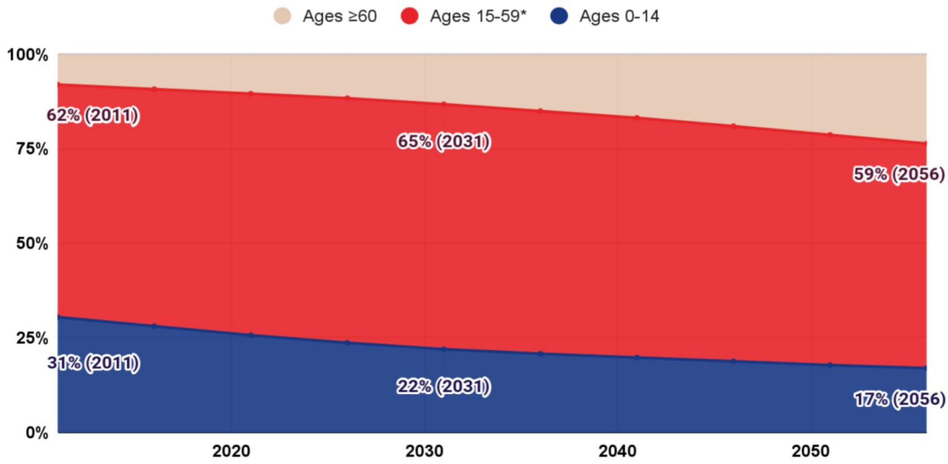
(15-59 years) is projected to increase to 64.8% by 2031 from 61.5% in 2011, this proportion will gradually decline afterwards as fewer children are born (see Figure 11). These demographic changes will create a significant skill shortage in the future as fewer workers join the workforce. To address this impending skill shortage, it is essential to tap into the existing skill set of experienced government employees. By progressively increasing the retirement age over the next 10-15 years, India can efficiently utilise the knowledge, understanding and expertise of the experienced workforce. The move would bridge the future skill shortage and ensure the country leverages the contributions of the experienced employees.

In addition to addressing the skill shortage, extending the retirement age of government employees would have significant fiscal benefits. By progressively increasing the retirement age, keeping in line with the increasing life expectancy, the burden on the exchequer in terms of future pension outflow would be reduced. Many developed countries have already recognised the need to sustain future pension liabilities and have progressively increased the retirement age to 65 years or more. India must adopt such global best practices to limit pension liability and ensure a healthy state of public finances.

The changing demographic landscape, coupled with the future pension liabilities emphasise the urgency for this policy change. By aligning the retirement age with increased life expectancy, bridging the skill gap, and adopting global best practices, India can ensure a healthy state of public finances in the country.[64]

[64] The proposition of increasing the retirement age was endorsed in the Economic Survey 2019-20, echoing the rationale outlined in this advocacy paper.
Ministry of Finance, Government of India. (2020). Economic Survey 2019-20: Volume 1.

Figure 11: Trends in Age Composition of Population, India



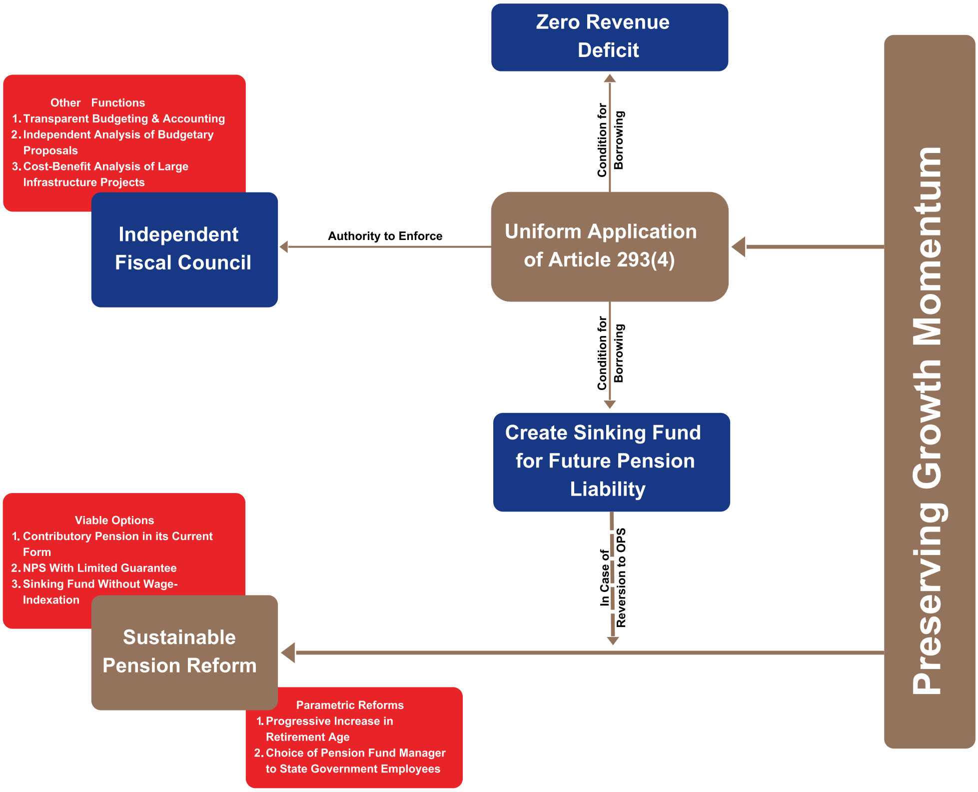
**The proportion of population aged 15-59 indicates the working age population in the country.*

Data Source: *World Population Prospects 2022, United Nations.*
Chart: *Foundation for Democratic Reforms.*

9.2. Minimalist Framework

The above framework is minimalist in nature focusing on eliminating revenue deficits, subjecting public finances to independent analysis and costing while respecting the sovereignty and powers and functions of elected government and legislatures. Such an approach will eliminate the clash between short-term unsustainable populism and long-term economic growth, and will harmonise both welfare and growth. There is a need to address the immediate concerns and needs of the people, even as we protect the long-term health of public finances and promote growth, prosperity and opportunity for all while ensuring intergenerational equity. Such a framework is likely to build a consensus across the political spectrum and between the Union and States.

Figure 12: Overview of Recommendations



10. Conclusion

The most important faultline emerging in our electoral politics in recent times is between long-term growth and short term fiscal profligacy without increasing assets and growth momentum. In such polarised elections in a poor country short term populism will win hands down most of the time. World over, even in rich countries, voters prefer ISW. The recent reversal of course in some States reverting to OPS from the fiscally sound NPS is a danger signal to public finances. Fiscal profligacy in the form of short-term populism and OPS pose the greatest and most proximate danger to India's growth prospects. The great challenge of democracy is reconciling short term political profit with long-term public good. There is increasing temptation to risk the future of youth for temporary political gains. We need to build a fresh consensus on long-term fiscal health if we are to enjoy long-term, sustained high growth and prosperity. If we allow elections to be a clash of economic populism vs. growth, while also allowing governments to cater to the demands of powerful, vocal sections for OPS without instituting necessary safeguards, the prospects of high growth over the next two or three decades will vanish. India would have squandered a priceless opportunity to grow the economy rapidly, end poverty and give opportunity for all in a generation. We need to build an acceptable framework to balance short term populism with growth, and simultaneously ensure that the reversal to OPS does not unfairly burden the future generations. This paper is a modest attempt to analyse the relevant issues, raise awareness, promote healthy debate on our public finances, and help build a consensus.

10.1. Why Growth Matters

The compounding effect of growth in a developing economy is significant and cannot be overemphasised. As Poonam Gupta and Arvind Panagriya pointed out,[65] the difference between sustained 7% growth rate versus 8% growth rate over ten years for an economy of India's size would mean a difference in GDP of $600 billion or about ₹ 50,00,000 crore of GDP lost per year after 10 years. Our tax-to-GDP ratio is about 18-19% (see Annexure 11). Loss of ₹ 50 lakh crore GDP means that the Union and States lose over ₹ 9 lakh crore revenue every year, which could have been deployed for more ISW promoting welfare, and better infrastructure to promote further higher growth and employment. Even during the next 10 years, a loss of 1% annual growth means the revenues lost to governments will be of the order of ₹ 50,000 crore in the first year, and ₹ 2,88,000 crore at the end of five years.

Despite prevailing global uncertainties, India has immense untapped potential, and successive governments since 1991 have laid foundations for sustained high growth of 7-8% over the next 20-30 years. We are at the point of inflexion that marks a critical juncture in the country's development, making long-term high growth a realisable goal with the potential to significantly improve the lives of millions of Indians. It is imperative that the country seizes this opportunity and exercises fiscal

[65] Panagariya, A., & Gupta, P. (2022, October 6). Freeing the white elephants: Why privatisation of public banks can only be good. The Economic Times.

prudence. By directing investments towards critical sectors such as quality education and healthcare, infrastructure, and rule of law, the country can preserve the growth momentum, enhance skills and productivity, stimulate employment and income, and ultimately eradicate poverty.

10.2. Poor Suffer When Core Functions are Neglected

The neglect of public finances leads to scarcity of resources available for governments to fulfill their core functions. Access to good quality roads, water supply, sewerage, storm water drainage, school education, and healthcare are critical for the poor who lead precarious lives. Failure of these basic services for want of resources will have a disproportionately adverse impact on the lives of the poor. If there is no investment to promote future growth, poverty will be perpetuated, and employment and incomes will not rise. There is a strong case for focusing on labour-intensive growth and strategies for promoting employment and formalisation of the large unorganised, informal workforce.

Even more important, if governments fail to improve rule of law and if rights of all citizens irrespective of wealth and power are not protected, then the poor will suffer the most. When rule of law fails, might becomes right and society will descend into new feudalism or jungle raj with armed marauders controlling the streets. When public order collapses, rights are not enforced equitably, crimes are not punished swiftly and surely, and disputes are not settled speedily and fairly, the poor will be the worst sufferers. Already, in our jails, over 70% are undertrial prisoners[66] who, because of poverty, could not afford a lawyer or post bail. Most of the convicts in criminal cases are the poor, and the wealthy escape conviction by strong legal representation and other tactics in a dysfunctional system.

There is no rational or realistic case to argue against robust economic growth in order to eliminate poverty. Moreover, the revenue foregone due to lost GDP growth will severely impact fiscal health and set off a vicious cycle. If revenues fail to grow while

[66] National Crime Records Bureau. (2020). Prison Statistics India 2019.

spending on unproductive purposes continues to increase, debts will soar, dragging the economy into the abyss, condemning millions to Indians to perpetual poverty, and leading to break down of order in society.

10.3. Can Public Finances be Restored to Health?

One question we have to address is, can public finances be restored to sound health with the minimal measures proposed in this paper. There is every reason to be optimistic. India is a developing country with a fast growing economy. With 7% growth and inflation of 4-6%, the nominal growth will be about 12% per annum. This will increase government revenues by about 12% per annum. If the NPS commitment is not diluted, and ISWs are frozen at current level, or their growth in expenditure terms is kept at a moderate level well below the nominal growth rate, over a relatively short period of three to five years the share of committed expenditure and ISWs in revenues will fall significantly. Revenue deficits will soon disappear. With NPS, the pension burden on future taxpayers will progressively decline from about 2035, and finally will be eliminated as all retired employees will draw pensions from AUM under NPS. But if governments yield to the pressures to revert to OPS, all the gains will be lost, and there will be irreversible decline in fiscal health, undermining the Indian economy and the well-being of future generations.

Table 12 shows the significant increase of revenues of the Union government since 1998-99. While the revenues of the Union government stood at ₹ 2,54,369 crore in 1998-99, by 2022-23, the revenue estimates shot up by 12 times to ₹ 30,43,067 crore.

Similarly, the erstwhile State of Andhra Pradesh (comprising present day AP and Telangana) had a revenue of ₹ 20,361 crore in 1998-99; the combined revenue estimates of Andhra Pradesh and Telangana in 2022-23 are ₹ 3,52,250 crore, a 17 fold increase.

Table 12: Growth in Government Revenues – Union and erstwhile Andhra Pradesh						
Years	Union Government		Andhra Pradesh		Telangana	
	Total Expenditure (₹ Crore)	Revenue Receipts (₹ Crore)	Total Expenditure (₹ Crore)	Revenue Receipts (₹ Crore)	Total Expenditure (₹ Crore)	Revenue Receipts (₹ Crore)
1998-99	372,250	254,369	20,361	14,260	Not Applicable	Not Applicable
2011-12	1,304,365	889,176	115,882	93,554	Not Applicable	Not Applicable
2022-23[1]	4,187,232	3,043,067	240,509	176,448	237,611	175,802

Note:
1. Figures for FY 2022-23 are Revised Estimates

Sources:
1.1998-99 figures – C&AG Archives
2.2011-12 figures – respective State Budget documents for 2013-14, Union Budget 2013-14
3.2022-23 figures – respective State Budget documents for 2023-24, Union Budget 2023-24

If reasonable steps are taken to freeze ISW or allow moderate growth in expenditure below nominal growth rate and ensure commitments under NPS are upheld, the compounding effect of nominal growth rate in a growing economy will quickly restore the health of public finances.

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ANNEXURE

Annexure 1: Statements Indicating Political Endorsement of NPS

Statements Indicating Political Endorsement of NPS			
FY	**Union Budget Statements**	**Political Party Heading the Government**	**Name of the Finance Minister**
2001-2002	*"While economic reforms have placed the country on a much more secure and sustainaed growth path,we still have some serious concerns and cannot afford to be complacent... The pension liability of the Government is becoming onerous."* *"The Central Government pension liability has reached unstainable proportions: as a percentage of GDP, it has risen from about 0.5 per cent in 1993-94 to 1 per cent in 2000-2001. As such it is envisaged that those who enter central government services after October 1, 2001 would receive pension through a new pension programme based on defined contributions. In order to review the existing pension system and to provide a roadmap for the next steps to be taken by the Government, I propose to constitute a High Level Expect Group, which would give its recommendations within 3 months."*	National Democratic Alliance	Yashwant Sinha
2002-2003	*"The present pension scheme for Government employees casts an open-ended financial burden on the Government. I had announced the appointment of a High Level Expert Group to develop a new pension scheme, based on defined contributions, for new recruits entering government service. The Expert Group has submitted its report to the Government. It has proposed a hybrid scheme that combines contributions from employees and the Union Government on matching basis, on the one hand, while committing to the employees a defined benefit as pension. The report is being considered by the Government and the new pension scheme for new recruits will be announced and implemented by June 1, 2002."*	National Democratic Alliance	Yashwant Sinha
2003-2004	*"My Predecessor in office had, in 2001, announced a road map for a restructured pension scheme for new Central Government employees, and a scheme for the general public. This scheme is now ready. It will apply only to new entrants to Government service, except to the armed forces, and upon finalisation, offer a basket of pension choices. It will also be available, on a voluntary basis, to all employers for their employees, as well as to the self-employed."* *"This new pension system, when introduced, will be based on defined contribution, shared equally in the case of Government employees between the Government and the employees. There will, of course, be no contribution from the Government in respect of individuals who are not Government employees. The new pension scheme will be portable, allowing transfer of the benefits in case of a change of employment, and will go into 'individual pension accounts' with Pension Funds. The Ministry of Finance will oversee and supervise the Pension Funds through a new and independent Pension Fund Regulatory and Development Authority."*	National Democratic Alliance	Jaswant Singh
2004-2005	*" A 'defined contribution' pension scheme has been introduced with effect from January 1, 2004 for the Central Government employees recruited on or after that date. A suitable legislation to provide a regulatory framework for the scheme will be introduced in Parliament."* *"A new 'defined contribution ' pension scheme for new entrants into Central Government service has come into effect from January 1, 2004. The tax treatment of contributions made to the scheme had engaged the attention of Govenrment. I propose to adopt the universally accepted formula of EET: that is, the contributions will be excluded from income for tax purposes; the accruals will also be exempt from tax; and only the terminal benifits will be taxed at the applicable rate in the year of receipt."*	United Progressive Alliance	P.Chidambaram

Annexure 1: Statements Indicating Political Endorsement of NPS

Statements Indicating Political Endorsement of NPS			
FY	**Union Budget Statements**	**Political Party Heading the Government**	**Name of the Finance Minister**
2005-2006	*"With increasing longevity, the problem of old-age income security can no longer be ignored. Government had announced a defined contribution pension scheme for newly recruited Central Government employees which would also be extended to the unorganized sector. I am happy to inform the House that seven State Govenrments- Andhra Pradesh, Chhattisgarh, Himachal Praesh, Jharkhand, Manipur, Rajasthan and Tamilnadu- have introduced similar schemes for their employees. Other States have also evinced interest. An Ordinance was promulgated on December 29, 2004 to set up a pension Fund Regulatory and Development Authority(PFRDA). I propose to introduce a Bill to replace the Ordinnce during this session."* *"Through the new scheme, it is proposed to offer a menu of investment choices to the subscribers and to provide a strong regulatory mechanism to ensure that the interests of subscribers are protected. I appeal to workers all over the country to join the new pension system."*	United Progressive Alliance	P.Chidambaram
2009-2010	*" The New Pension System (NPS) is an important milestone in the development of a sustainable, efficient, voluntary and defined contribution pension system in India . While the NPS will continue to be subjected to the Exempt-Exempt-Taxed (EET) method of tax treatment of savings, it is proposed to provide necessary fiscal support to the NPS for the establishment of this much needed social security system. Accordingly, I propose to exempt the income of the NPS Trust from income tax and any dividend paid to this Trust from Dividend Distribution Tax. Similarly, all purchase and sale of equity shares and derivatives by the NPS Trust will also be exempt from the Securities Transaction Tax. I also propose to enable self employed persons to participate in the NPS and avail of the tax benefits available thereto."*	United Progressive Alliance	Pranab Mukherjee
2011-2012	*"The financial sector reforms initiated during the early 1990s have borne good results for the Indian economy. The UPA Government is committed to take this process further. Accordingly, I propose to move the following legislation in the financial sector:* *(i) The Insurance Laws (Amendment) Bill, 2008;* *(ii) The Life Insurance Corporation (Amendment) Bill, 2009;* ***(iii) The revised Pension Fund Regulatory and Development Authority Bill, first introduced in 2005****;* *(iv) Banking Laws Amendment Bill, 2011;* *(v) Bill on Factoring and Assignment of Receivables;* *(vi) The State Bank of India (Subsidiary Banks Laws) Amendment Bill, 2009; and* *(vii) Bill to amend RDBFI Act 1993 and SARFAESI Act 2002."*	United Progressive Alliance	Pranab Mukherjee
2015-2016	*"To provide a social safety net and the facility of pension to individuals, an additional deduction of ` 50,000 is proposed to be provided for contribution to the New Pension Scheme under Section 80CCD. This will enable India to become a pensioned society instead of a pensionless society."*	National Democratic Alliance	Arun Jaitley
2016-2017	*"Pension schemes offer financial protection to senior citizens. I believe that the tax treatment should be uniform for defined benefit and defined contribution pension plans. I propose to make withdrawal up to 40% of the corpus at the time of retirement tax exempt in the case of National Pension Scheme."*	National Democratic Alliance	Arun Jaitley

Annexure 1: Statements Indicating Political Endorsement of NPS

Statements Indicating Political Endorsement of NPS			
FY	**Union Budget Statements**	**Political Party Heading the Government**	**Name of the Finance Minister**
2019-2020	*"After submission of the 7th Central Pay Commission Report, the recommendations were implemented immediately. The New Pension Scheme (NPS) has been liberalized. Keeping the contribution of the employee at 10%, we have increased the Government contribution by 4% making it 14%... "* *"In order to give effect to the cabinet decision already taken to incentivise NPS, it is proposed to,-* *(i) increase the limit of exemption from current 40% to 60% of payment on final withdrawal from NPS;* *(ii) allow deduction for employer's contribution upto 14% of salary from current 10%, in case of Central Government employee;* *(iii) allow deduction under section 80C for contribution made to Tier II NPS account by Central Government employees."*	National Democratic Alliance	Piyush Goyal
2022-2023	*"At present, the Central Government contributes 14 per cent of the salary of its employee to the National Pension System (NPS) Tier-I. This is allowed as a deduction in computing the income of the employee. However, such deduction is allowed only to the extent of 10 per cent of the salary in case of employees of the State government. To provide equal treatment to both Central and State government employees, I propose to increase the tax deduction limit from 10 per cent to 14 per cent on employer's contribution to the NPS account of State Government employees as well. This would help in enhancing the social security benefits of the state government employees and bring them at par with central government employees."*	National Democratic Alliance	Nirmala Sitharaman

Source:
1. Union Budget Speeches from FY 2002 to FY 2023.

Annexure 2: Pension Expenditure of the State and Union Governments

Annexure 2a: Combined Pension Expenditure of All States and Uts

Combined Pension Expenditure of All States and UTs	
Year	**Pension Outgo (in ₹ Crore)**
2004-05	37,378
2005-06	40,733
2006-07	46,965
2007-08	56,218
2008-09	65,606
2009-10	83,445
2010-11	108,514
2011-12	128,099
2012-13	145,124
2013-14	163,474
2014-15	183,499
2015-16	204,686
2016-17	226,772
2017-18	275,361
2018-19	314,865
2019-20	345,505
2020-21	368,834
RE 2021-22	399,813

UTs: Union Territory with Legislature.

Data from this table has been used to generate Figure 1a.

Source:
For the years 2004-05 to 2020-21
1. Handbook of Statistics on Indian States 2021-22, Reserve Bank of India.
For 2021-22 (RE)
2. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India.

Annexure 2b: Pension Expenditure of the Union (in ₹ Crore)

Pension Expenditure of the Union (in ₹ Crore)					
FY	**Defence**	**Civil**	**Railways**	**Post**	**Total**
2012-13	43,368	26,111	21,021	3,968	94,468
2013-14	45,499	29,397	24,761	4,443	104,100
2014-15	60,450	33,161	28,642	5,034	127,287
2015-16	60,238	36,533	30,701	5,408	132,880
2016-17	87,826	43,575	40,463	7,547	179,411
2017-18	92,000	53,745	45,275	8,511	199,531
2018-19	101,775	58,437	46,718	8,706	215,636
2019-20	117,810	66,144	49,188	9,419	242,561
2020-21	128,066	80,407	48,435	9,760	266,668
2021-22	121,984	79,579	51,935	786	254,284

FY: Fiscal Year

Note:
For FY 2021-22, the employees of the Department of Telecom are included under the civilian head.

Data from this table has been used to generate Figure 1b.

Source:
For FY 2012-13 to 2015-16
1. Report of Comptroller and Auditor General of India for the year 2016-17;
For FY 2016-17 to 2020-21
2. Report of Comptroller and Auditor General of India for the year 2020-21;
For FY 2021-22
3. Lok Sabha reply, unstarred question no. 2961, dated 03.08.2022.

Annexure 3:
Pension Expenditure vis-a-vis Revenues of States and UTs, Over the Years

Annexure 3a: Compound Annual Growth Rate of Pensions vis-à-vis Own Revenues of States

Compound Annual Growth Rate of Pensions vis-à-vis Own Revenues of States		
Year	**Pension Expenditure (in ₹ Crore)[1]**	**States' Own Revenues (in ₹ Crore)[2]**
2004-05	37,378	236,670
2005-06	40,740	271,580
2006-07	46,960	328,550
2007-08	56,220	378,610
2008-09	65,610	419,520
2009-10	83,450	470,580
2010-11	108,510	575,270
2011-12	128,100	678,700
2012-13	145,120	797,910
2013-14	163,474	874,630
2014-15	183,499	953,473
2015-16	204,686	1,034,936
2016-17	226,772	1,117,616
2017-18	275,361	1,310,098
2018-19	314,865	1,433,590
2019-20	345,505	1,484,884
2020-21	368,834	1,347,554
2021-22 (RE)	399,813	1,778,996
CAGR (2004-05 to 2021-22)	**14.96%**	**12.60%**

RE: Revised Estimates; **CAGR:** Compound Annual Growth Rate

Note:

1. Pension Expenditure is for States and Union Territories with Legislature.
2. States' Own Revenues include Own Tax Revenue and Own Non-tax Revenue.

Source:

Pension Expenditure; States' Own Revenue

1. Handbook of Statistics on Indian States 2021-22, Reserve Bank of India.

For 2021-22 (RE)

2. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India.

Annexure 3b:
Pension Expenditure as a Share of Revenues of States and UTs, Over the Years

Pension Expenditure as a Share of Revenues of States and UTs, Over the Years					
Year	Pension Expenditure (in ₹ Crore)	States' Own Revenues (in ₹ Crore)[1]	States' Total Revenues (in ₹ Crore)[2]	Pension Expenditure of all States as a Share of	
				States' Own Revenues (%)	States' Total Revenues (%)
1990-91	3,130	39,590	66,467	7.9	4.7
1995-96	7,810	86,750	134,507	9.0	5.8
2000-01	25,450	149,440	232,509	17.0	10.9
2005-06	40,740	271,575	431,021	15.0	9.5
2010-11	108,510	575,268	935,347	18.9	11.6
2015-16	204,686	1,034,936	1,832,885	19.8	11.2
2016-17	226,772	1,117,616	2,046,401	20.3	11.1
2017-18	275,361	1,310,098	2,321,241	21.0	11.9
2018-19	314,865	1,433,590	2,620,353	22.0	12.0
2019-20	345,505	1,484,884	2,670,138	23.3	12.9
2020-21	368,834	1,347,554	2,586,622	27.4	14.3

UTs: Union Territories with Legislature**; RE:** Revised Estimates

Note:
1. States' Own Revenues include Own Tax Revenue and Own Non-tax Revenue.
2. States' Total Revenues include Own Tax Revenue, Own Non-tax Revenue, and Devolution and Transfers from the Union.

Data from this table has been used to generate Figure 2.

Source:
Pension Expenditure; States' Own Revenue; States' Total Revenue
1. FY 1990-91 to 2019-20 – Handbook of Statistics on Indian States, Reserve Bank of India;
2. FY 2020-21 – State Finances: A Study of Budgets of 2022-23, Reserve Bank of India.

Annexure 4: Survivor Benefits under NPS

Annexure 4a: Overview of Survivor Benefits under NPS

Circumstance	Overview of Survivor Benefit[1]
Unfortunate Death (before normal exit/ 60 years or Superannuation)	a) Complete (100%) withdrawal for the corpus to nominees/legal heirs if the corpus is less than or equal to ₹ 5 Lakh. However, the nominees can opt for an annuity if desired. b) If the corpus is higher than ₹ 5 Lakh, at least 80% of the accumulated pension wealth of the Subscriber has to be utilized for the purchase of default Annuity by dependents, and the balance 20% is paid as a lump sum to the nominee/legal heir. c) If none of the dependent family members (spouse, mother & father) are alive, the corpus, i.e., 80 %, has to be returned to the surviving children of the Subscriber and, in the absence of children, to the legal heirs.
In case of death after 60 years/Superannuation)	60% lump sum will be paid to the nominees and 40% for default annuity by dependents
Option of Family Pension for Government sector Subscribers provided by the employer	Suppose the Subscriber or the family members of the deceased Subscriber, upon his death, avails the option of additional relief on death or disability provided by the Government. In that case, the Subscriber has to transfer the NPS corpus to the Nodal Office. The Subscriber or family members of the Subscriber availing such benefit shall specifically and unconditionally agree and undertake to transfer the entire accumulated pension wealth to the Government.

Note:
1. Applicable to survivors of government employees.

Source:
1. National Pension System Trust. (n.d.). NPS exit withdrawal. Retrieved from: https://npscra.nsdl.co.in/nps-exit/

Annexure 4b: Details of Survivor Benefits under NPS; Ministry of Personnel, Public Grievances and Pensions (No. - 57/03/2022-P&PW(B)/8361 (1)

No. - 57/03/2022-P&PW(B)/8361 (1)
Government of India
Ministry of Personnel, Public Grievances and Pensions
Department of Pension and Pensioners' Welfare
***

3rd Floor, Lok Nayak Bhavan, Khan Market,
New Delhi, Dated the 28th October, 2022

OFFICE MEMORANDUM

Subject: Entitlement for family on death of a Central Government servant covered under National Pension System -reg.

The undersigned is directed to say that Department of Pension and Pensioners' Welfare has notified the Central Civil Services (Implementation of National Pension System) Rules, 2021 and Central Civil Services (Payment of Gratuity under National Pension System) Rules, 2021 which are applicable from the date of its publication in the Official Gazette, to govern service related matters and for grant of gratuity respectively to Central Government civil employees covered under National Pension System.

2. Rule 20 of the Central Civil Services (Implementation of NPS) Rules, 2021 provides for the entitlement of family members on death of a Central Government covered under National Pension System. As per rule 20, on death of a Subscriber, who had exercised option or in whose case the default option under rule 10 of the CCS(Implementation of NPS) Rules, 2021 is for availing benefits under the Central Civil Services (Pension) Rules, 1972 or Central Civil Services (Extraordinary Pension) Rules , further action will be taken by the Head of Office for disbursement of benefits in accordance with the Central Civil Services (Pension) Rules. However, if the death is attributable to Government service, further action will be taken by the Head of Office for disbursement of benefits in accordance with the Central Civil Services (Extraordinary Pension) Rules subject to fulfillment of all the conditions for grant of benefits under those rules.

3. If on death of the Subscriber, benefits are payable to the family under the Central Civil Services (Extraordinary Pension) Rules or the Central Civil Services (Pension) Rules, the Government contribution and returns thereon in the accumulated pension corpus of the Subscriber shall be transferred to Government account. The remaining accumulated pension corpus shall be paid in lump sum to the person(s) in whose favour a nomination has been made under the Pension Fund Regulatory and Development Authority (Exits and Withdrawals under National Pension System) Regulations, 2015. If there is no such nomination or if the nomination made does not subsist, the amount of remaining accumulated pension corpus shall be paid to the legal heir(s).

Contd.

Annexure 4b: Details of Survivor Benefits under NPS; Ministry of Personnel, Public Grievances and Pensions (No. - 57/03/2022-P&PW(B)/8361 (1)

4. In the case of death of a Subscriber who had exercised option or in whose case the default option under rule 10 of the CCS(Implementation of NPS) Rules, 2021 is for availing benefits under the National Pension System, such benefits may be granted in accordance with the Pension Fund Regulatory and Development Authority (Exits and Withdrawals under National Pension System) Regulations, 2015.

5. In the event of death of Government employees covered under NPS during service, and in whose case benefits from accumulated pension corpus under NPS have been availed, family member of such deceased Government employee would also be eligible for death gratuity in accordance with rule 22 of the Central Civil Services (Payment of Gratuity under NPS) Rules, 2021. The rates provided in the rules for death gratuity is as under:

Sl. No.	Length of qualifying service	Rate of death gratuity
(i)	Less than one year	Two times of emoluments.
(ii)	One year or more but less than five years	Six times of emoluments
(iii)	Five years or more but less than eleven years	Twelve times of emoluments
(iv)	Eleven years or more but less than twenty years	Twenty times of emoluments
(v)	Twenty years or more	Half of emoluments for every completed six monthly period of qualifying service subject to a maximum of thirty three times of emoluments:

The maximum amount of death gratuity payable under this rule shall in no case exceed twenty lakh rupees.

6. All Ministries/Departments are requested that the above provisions regarding entitlement in respect to Central Government employees covered under National Pension System may be brought to the notice of the Government servants covered under NPS and personnel dealing with the pensionary benefits in the Ministry/Department and attached/subordinate offices thereunder, for strict implementation.

(S. Chakrabarti)
Under Secretary to the Government of India

To

All Ministries/Departments/Organisations,
(As per standard list)

Annexure 4c: Benefits Available in case of Death of a Union Government Employee covered under NPS during service; Pensioners' Portal, Ministry of Personnel, Public Grievances and Pensions

Benefits available in the case of death of a Central Government Employee covered under National Pension System during service

- Central Government employees covered under National Pension System have been given option under rule 10 of CCS(Implementation of NPS) Rules, 2021 to choose benefits either from old pension scheme or accumulated pension corpus under NPS in the event of their death. Family of deceased Government employee cannot exercise this option.

- In the case, the Central Government employees could not furnish his option in this regard, there is default option of benefit under old pension scheme for first 15 years of service and thereafter, default option would be benefits under NPS. At present default option of old pension scheme is in vogue till March, 2024 in accordance with these rules even if Government Employee has completed 15 years of service.

- Following benefits are available in the event of in-service death of a Central Government Employee covered under NPS:

  (i) Family pension under CCS(Pension) Rules, 1972 as per option exercised by Government servant or default option

  or

  In case, Government servant has opted for benefits under NPS, family would get benefits from his accumulated pension wealth under NPS.

  (ii) Death Gratuity
  (iii) Leave Encashment
  (iv) Benefits from CGEGIS,
  (v) CGHS facilities

- As per rule 20 of CCS (Implementation of NPS) Rules, 2021, if the Government servant had opted for benefits under old pension scheme (or if no option was exercised, then default option applicable in his case) the concerned office would take action to sanction family pension to eligible member(s) of the family of the deceased Government servant, as done for Government servants covered under old pension scheme (i.e. as applicable to those joined service before 01.01.2004).

Annexure 4c: Benefits Available in case of Death of a Union Government Employee covered under NPS during service; Pensioners' Portal, Ministry of Personnel, Public Grievances and Pensions

- Simultaneously, they would start process to close PRAN under NPS of the Government servant and Government contribution (and return thereon) would be transferred into the Government account. Remaining amount would be paid to the nominee or legal heir as per PFRDA regulations in lump sum.

- However, those Government servants who had opted for benefits from NPS in the event of their death or if no option exercised, then in whose case default option is benefits under NPS, concerned office would take action to close PRAN under NPS of the deceased Government servant and grant benefits of lump sum (maximum of 20% of accumulated pension wealth) and annuity from the remaining pension wealth to eligible member from annuity service provider registered with PFRDA in accordance with PFRDA (Exits and Withdrawals under NPS) Regulations, 2015.

- Other benefits viz. Death gratuity, leave encashment, CGEGIS and CGHS would be available in both the cases.

--- *End* ---

Annexure 5: Burden of Committed Expenditure on States Resources for Select States (FY 2020-21)

Burden of Committed Expenditure on States Resources for Select States (FY 2020-21)*					
States	**Committed Expenditure (in ₹ Crore)**	**States' Own Revenues (in ₹ Crore)**	**States' Revenue Receipts (in ₹ Crore)**	**Committed Expenditure as % of States' Own Revenues**	**Committed Expenditure as % of States' Revenue Receipts**
Maharashtra	176,849	180,230	269,467	98%	66%
Gujarat	75,453	80,759	128,155	93%	59%
Tamil Nadu	121,529	116,574	174,076	104%	70%
Odisha	47,989	57,018	125,600	84%	38%
Kerala	68,771	54,988	97,617	125%	70%
Andhra Pradesh	82,517	60,804	117,136	136%	70%
Rajasthan	99,406	77,982	134,307	127%	74%
Chhattisgarh	37,208	30,026	63,176	124%	59%
West Bengal	111,934	65,486	148,393	171%	75%
Punjab	58,327	34,205	69,048	171%	84%
Telangana	52,142	72,752	100,914	72%	52%
Karnataka	86,326	104,946	156,716	82%	55%
Himachal Pradesh	21,204	10,271	33,438	206%	63%
Jharkhand	25,895	24,444	56,150	106%	46%
All States Combined	**1,617,120**	**1,347,554**	**2,586,621**	**120%**	**63%**

*Committed Expenditure includes expenditure on salaries, pensions, and interest payments.

Data from this table has been used to generate Figures 3a & 3b.

Source:
1. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India.

Annexure 6: Andhra Pradesh: Projections of Key Fiscal Indicators upon Reverting to OPS

Andhra Pradesh: Projections of Key Fiscal Indicators upon Reverting to OPS					
Indicator	**2022**	**2030**	**2040**	**2050**	**2100**
Salary and Pensions as % of States' Own Revenues	74.10	97.70	110.60	129.20	NA
Pension as % of Revenue Receipts	11.00	16.00	19.50	28.60	38.90
Fiscal Deficit	3.00	4.80	6.10	8.10	10.70
Debt-to-GSDP Ratio	38.00	53.00	77.00	107.00	211.00

NA: Not Available

Data from this table has been used to generate Figures 4(a-d).

Source: *Government of Andhra Pradesh communication dated 28/08/2022*

Annexure 7: Unfunded Pension Liabilities of Select States and Local Governments in the US

Annexure 7a: California (in USD millions)

California (in USD millions)			
Year	Pension assets	Pension liabilities	Funding status
2020	1,090,963	1,981,889	-890,926
2019	975,627	1,927,595	-951,968
2018	871,237	1,834,551	-963,314
2017	898,914	1,755,050	-856,137
2016	785,773	1,660,970	-875,197
2015	746,370	1,563,083	-816,713
2014	752,750	1,487,128	-734,378
2013	713,875	1,398,733	-684,858
2012	625,905	1,196,011	-570,106
2011	560,186	1,138,203	-578,017
2010	575,736	1,098,787	-523,051
2009	525,482	1,006,560	-481,077
2008	476,311	955,598	-479,287
2007	638,184	895,072	-256,887
2006	597,222	832,327	-235,105
2005	531,954	772,757	-240,803
2004	517,878	724,848	-206,969
2003	450,082	648,120	-198,037
2002	381,330	612,480	-231,150

Data from this table has been used to generate Figure 5a.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 7b: Florida (in USD millions)

Florida (in USD millions)			
Year	Pension assets	Pension liabilities	Funding status
2020	230,037	357,585	-127,547
2019	212,144	350,584	-138,440
2018	189,316	342,428	-153,112
2017	198,712	335,572	-136,860
2016	178,183	323,300	-145,117
2015	177,716	311,930	-134,214
2014	182,713	303,655	-120,942
2013	175,363	290,928	-115,565
2012	157,105	254,845	-97,739
2011	144,037	247,876	-103,838
2010	150,779	241,927	-91,148
2009	139,787	224,176	-84,389
2008	121,863	212,186	-90,324
2007	154,474	198,363	-43,889
2006	144,220	188,378	-44,159
2005	132,183	176,685	-44,502
2004	135,949	164,177	-28,227
2003	117,849	147,613	-29,764
2002	98,979	143,381	-44,402

Data from this table has been used to generate Figure 5b.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 7: Unfunded Pension Liabilities of Select States and Local Governments in the US

Annexure 7c: Illinois (in USD millions)

Illinois (in USD millions)			
Year	**Pension assets**	**Pension liabilities**	**Funding status**
2020	204,618	591,780	-387,162
2019	188,977	573,506	-384,529
2018	169,433	556,851	-387,417
2017	180,903	547,979	-367,076
2016	158,673	533,160	-374,486
2015	153,252	513,053	-359,801
2014	155,684	489,047	-333,363
2013	147,401	458,644	-311,243
2012	130,993	397,401	-266,408
2011	119,087	382,822	-263,735
2010	124,028	367,349	-243,321
2009	115,930	331,775	-215,845
2008	103,954	314,459	-210,505
2007	137,142	298,748	-161,605
2006	131,562	281,411	-149,849
2005	122,380	265,000	-142,620
2004	121,615	250,670	-129,055
2003	103,699	223,371	-119,672
2002	89,801	207,931	-118,130

Data from this table has been used to generate Figure 5c.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 7d: New York (in USD millions)

New York (in USD millions)			
Year	**Pension assets**	**Pension liabilities**	**Funding status**
2020	628,638	869,561	-240,924
2019	555,624	853,449	-297,825
2018	492,458	830,791	-338,333
2017	529,463	805,151	-275,688
2016	466,600	780,231	-313,630
2015	446,565	752,901	-306,337
2014	454,837	723,184	-268,347
2013	424,910	696,191	-271,281
2012	369,317	604,474	-235,157
2011	326,543	586,928	-260,385
2010	332,606	566,835	-234,229
2009	305,178	524,419	-219,241
2008	275,206	512,161	-236,954
2007	380,295	491,615	-111,320
2006	364,823	467,044	-102,221
2005	323,775	445,044	-121,269
2004	317,668	427,091	-109,424
2003	278,174	390,265	-112,091
2002	248,294	373,122	-124,828

Data from this table has been used to generate Figure 5d.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 7: Unfunded Pension Liabilities of Select States and Local Governments in the US

Annexure 7e: Ohio (in USD millions)

Ohio (in USD millions)			
Year	**Pension assets**	**Pension liabilities**	**Funding status**
2020	218,130	369,504	-151,374
2019	203,232	366,387	-163,155
2018	177,921	360,310	-182,389
2017	190,907	353,485	-162,578
2016	172,047	351,534	-179,487
2015	170,823	348,647	-177,823
2014	179,182	339,909	-160,726
2013	172,553	330,175	-157,621
2012	153,297	304,321	-151,024
2011	140,185	308,106	-167,921
2010	147,679	295,483	-147,804
2009	139,532	270,346	-130,814
2008	128,049	259,901	-131,852
2007	167,584	246,807	-79,223
2006	156,554	233,799	-77,245
2005	141,661	222,134	-80,473
2004	142,093	210,604	-68,512
2003	125,700	189,475	-63,775
2002	109,324	177,759	-68,436

Data from this table has been used to generate Figure 5e.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 7f: Texas (in USD millions)

Texas (in USD millions)			
Year	**Pension assets**	**Pension liabilities**	**Funding status**
2020	338,939	578,291	-239,352
2019	307,820	555,245	-247,425
2018	263,824	530,516	-266,692
2017	277,927	506,104	-228,177
2016	244,124	486,872	-242,747
2015	230,650	478,311	-247,661
2014	233,190	462,217	-229,027
2013	226,174	430,689	-204,515
2012	207,116	372,032	-164,916
2011	184,949	359,928	-174,980
2010	189,882	345,343	-155,461
2009	180,907	312,226	-131,319
2008	151,881	297,099	-145,218
2007	187,497	279,844	-92,347
2006	180,602	262,973	-82,371
2005	161,159	248,406	-87,246
2004	152,762	237,778	-85,016
2003	138,353	216,879	-78,526
2002	120,824	204,380	-83,555

Data from this table has been used to generate Figure 5f.

Source: *Federal Reserve System. (n.d). State and Local Government Pension Funding Status, 2002 - 2020. Retrieved from https://www.federalreserve.gov/releases/z1/dataviz/pension/funding_status/chart/*

Annexure 8: Strength of Public Sector Workforce in India

Annexure 8a: Strength of Public Sector Workforce in States and Uts

Strength of Public Sector Workforce in States and UTs				
S. No.	**State/Union Territory**	**Number of Government Employees (in lakhs)[1]**	**Year (latest available)**	**Source**
1	Andhra Pradesh	3.95	2020	Report of the 11th Pay Revision Commission, Andhra Pradesh, 2020, Volume I, pg 23, available at: https: //apfinance.gov.in/downloads/Volume-1.pdf
2	Arunachal Pradesh	0.66	2019	*Arunachal: Khandu Announces Touch Location Alloawnces for Govt. Employees*, arunachal24.in, 09/01/2019, available at: https://arunachal24.in/arunachal-khandu-announces-tough-location-allowances-for-govt-employees/#:~:text=Arunachal%20Pradesh%20has%20around%2066%2C000,7th%20CPC%20despite%20resource%20constraint.
3	Assam	4.9	2018	Assam at a Glance 2019, Directorate of Economics and Statistics, pg 21, available at: https://des.assam.gov.in/sites/default/files/swf_utility_folder/departments/ecostat_medhassu_in_oid_3/portlet/level_1/files/assam_at_a_glance_-_2019.pdf
4	Bihar	4.5	2017	*Bihar government employees' pay revision report by May 15: Kang*, Hindustan Times, 08/05/2017, available at: https://www.hindustantimes.com/patna/bihar-government-employees-pay-revision-report-by-may-15-kang/story-Cb5xUVjIFstAu9Wj20NjaN.html
5	Chattisgarh	2.6	2017	*Chhattisgarh government announces implementation of the Seventh Pay Commission*, The New Indian Express, 29/03/2017, available at: https://www.newindianexpress.com/nation/2017/mar/29/chhattisgarh-government-announces-implementation-of-seventh-pay-commission-1587518.html
6	Delhi	0.85	2011	Census of Employees in Government of Delhi and Autonomous Bodies 2011, Government of National Capital Territory of Delhi, available at: https://des.delhi.gov.in/sites/default/files/DES/generic_multiple_files/final_report_census_of_emploees10-11.pdf
7	Goa	0.31	2007	A Report on Census of Government Employees - 2015, Directorate of Planning Statistics and Evaluation, Government of Goa, pg 4, available at: http://goadpse.gov.in/Census%20of%20Government%20Employees%202015.pdf
8	Gujarat	4.65	2018	*7th Pay Commission now cleared in Gujarat; 8.8 lakh government staff in BJP bastion get windfall news*, Zeebusiness, 03/03/2018, available at: https://www.zeebiz.com/india/news-7th-pay-commission-now-cleared-in-gujarat-88-lakh-government-staff-in-bjp-bastion-get-windfall-news-38252
9	Haryana	3.39	2016	Census of Haryana Government Employees as on 31-0-2016, Department of Economic and Statistical Analysis, Government of Haryana, available at: https://cdnbbsr.s3waas.gov.in/s32b0f658cbffd284984fb11d90254081f/uploads/2021/02/2021021830-3.pdf
10	Himachal Pradesh	1.81	2018	Employee Census 2018, Government of Himachal Pradesh, available at: https://himachalservices.nic.in/economics/pdf/employees_census2018_A1b.pdf
11	Jammu and Kashmir[2]	4.5	2019	Press Information Bureau release dated 22/10/2019, available at: https://pib.gov.in/Pressreleaseshare.aspx?PRID=1588690#:~:text=in%20respect%20of%204.5%20lakh,S.No.&text=1.
12	Jharkhand	1.19	2022	Calculated from the figures given in *As OPS weighs heavy on Jharkhand treasury, state govt wants its NPS funds back*, Punjab News Express, 06/05/2023, available at: https://www.punjabnewsexpress.com/national/news/as-ops-weighs-heavy-on-jharkhand-treasury-state-govt-wants-its-nps-funds-back-208080
13	Karnataka	5.11	2022	G.O. No. FD 45 SRP 2022, Government of Karnataka, 06/02/2023, available at: https://finance.karnataka.gov.in/storage/pdf-files/FD%2045%20SRP%202022%20Dt06-02-2023.pdf
14	Kerala	8	2021	Report of the XI Pay Revision Commission, Government of Kerala, available at: http://www.prc.kerala.gov.in/pcRpt.jsp
15	Madhya Pradesh	6.5	2018	*7th Pay Commission: Salaries likely to raise by 14% as MP govt decides on implementation*, Mint, 04/07/2017, available at: https://www.livemint.com/Politics/FL2Hn0U0SSl6ELK0qeAREM/Salaries-likely-to-rise-by-14-as-MP-govt-decides-to-impleme.html
16	Maharashtra	20	2018	*New Year gift for Maharashtra government employees*, The Hindu, 27/12/2018, available at: https://www.thehindu.com/news/national/other-states/new-year-gift-for-maharashtra-government-employees/article25843960.ece
17	Manipur	0.77	NA[3]	CMIS at a Glance Dashboard, MIS Directorate, Finance Department, Government of Manipur, available at: https://cmis.man.nic.in/sevaarth/home1/sevaarthhome_dashboard.php
18	Meghalaya	0.8	2006	*80,000 govt employees, ministers' salaries deferred in Meghalaya*, Deccan Herald, 29/04/2020, available at: https://www.deccanherald.com/national/80000-govt-employees-ministers-salaries-deferred-in-meghalaya
19	Mizoram	0.24	2018	Census of Government Employees and Workers Mizoram - 2018, Directorate of Economics and Statistics, Government of Mizoram, pg 7, available at: https://des.mizoram.gov.in/uploads/attachments/d27e7ff0f995df4508a56f8e248b6ae1/pages-180-census-of-govt-employees-workers-2018.pdf
20	Nagaland	0.4[4]	2012	Nagaland State Government Employees Census Report 2012, Directorate of Economics and Statistics, Government of Nagaland, pg 8, available at: https://statistics.nagaland.gov.in/storage/statistical_data/2013/2471601171206.pdf
21	Odisha	3.8	2022	*Odisha govt regularises 57,000 contractual workers*, HRKatha, 17/10/2022, available at: https://www.hrkatha.com/news/ir-labour-laws-news/odisha-govt-regularises-57000-contractual-workers/#:~:text=The%20State%20presently%20has%20about%203.8%20lakh%20permanent%20government%20employees.
22	Puducherry	0.28	2017	Census of Government Employeees 2016-17, Directorate of Economics and Statistics, Government of Puducherry, pg. 4, available at: https://statistics.py.gov.in/sites/default/files/CGE%202016-17.pdf
23	Punjab	2.77[5]	2019	2020 Statistical Abstract of Punjab, Economic and Statistical Organisation, Government of Punjab, pg. 344-345, available at: https://punjabassembly.nic.in/images/docs/Statistical%20Abstract.pdf
24	Rajasthan	8	2023	*Rajasthan government announces 4 per cent hike in DA of state employees, pensioners*, The Economic Times, 25/03/2023, available at: https://economictimes.indiatimes.com/news/economy/finance/rajasthan-govt-announces-4-pc-hike-in-da-of-state-employees-pensioners/articleshow/98995512.cms?from=mdr
25	Sikkim	0.37	NA	Government Employee Statistics, Directorate of Economics, Statistics & Monitoring and Evaluation, Government of Sikkim, available at: https://sikkim.gov.in/departments/desme/government-employee-statistics

Annexure 8: Strength of Public Sector Workforce in India

Annexure 8a: Strength of Public Sector Workforce in States and Uts

Strength of Public Sector Workforce in States and UTs				
S. No.	State/Union Territory	Number of Government Employees (in lakhs)[1]	Year (latest available)	Source
26	Tamil Nadu	16	2022	*Tamil Nadu increases DA by 3% for State government employees*, Businessline, 15/08/2022, available at: https://www.thehindubusinessline.com/news/tamil-nadu-increases-da-by-3-for-state-government-employees/article65771166.ece
27	Telangana	3.5	2022	*Telangana state govt employees in limbo over salary*, Deccan Chronicle, 30/12/2022, available at: https://www.deccanchronicle.com/nation/in-other-news/291222/telangana-state-government-employees-in-limbo-over-salary.html
28	Tripura	1.05	2022	*Tripura declares 12 per cent hike in DA for government employees*, The Economic Times, 27/12/2022, available at: https://economictimes.indiatimes.com/news/india/tripura-declares-12-per-cent-hike-in-da-for-government-employees/articleshow/96539880.cms
29	Uttar Pradesh	16	2021	*Uttar Pradesh CM Yogi Adithyanath approves DA hike for 28 lakh government employees, pensioners*, The Times of India, 29/07/2021, available at: https://timesofindia.indiatimes.com/city/lucknow/cm-approves-da-hike-for-28l-govt-staff-pensioners/articleshow/84842261.cms
30	Uttarakhand	1.65	2019	Uttarakhand At A Glance 2019-20, Directorate of Economics and Statistics, Government of Uttarakhand, pg. 20, available at: https://des.uk.gov.in/department6/library_file/file-11-05-2022-06-01-10.pdf
31	West Bengal	3.53	2014	Report on Staff Census 2013-14, Bureau of Applied Economics and Statistics, Government of West Bengal, pg 3, available at: http://wbpspm.gov.in/SiteFiles/Publications/12_18052017134945.pdf
	Total	**128.91**		

UT: Union Territory with Legislature

Note:
1. The sources for the data are not uniform across the States and some of the figures may be inclusive of employees of Public Sector Undertakings.
2. Jammu and Kashmir is now an Union Territory. The Union goverment employees figure pertains to 2014 (Annexure 5b) when Jammu and Kashmir was a state. Therefore, the goverment employees in Jammu and Kashmir would not reflect in the 2014 Union figure.
3. Latest available figure from the official Dashboard, Government of Manipur.
4. Includes only the permanent employees.
5. The figure does not include employees that are 'contingency paid, on contract basis or any other'.

Annexure 8: Strength of Public Sector Workforce in India

Annexure 8b: Strength of Union Government Workforce

Strength of Union Government Workforce	
Category	**Number of Employees (in lakhs) (2014)**
Civilian personnel*	33.02
Defence forces Personnel	13.86
Total	**46.88**

*Includes government employees in Union Territories

Source:
1. Report of the Seventh Central Pay Commission, 2015, pg. 23 and 105.

Annexure 8c: Share of Public Sector Workforce in Total Workforce and Population

Share of Public Sector Workforce in Total Workforce and Population		
A	Total Public Sector workforce in States and UTs (in crores)	1.24
B	Total Union Government workforce (in crores)	0.47
C	**Total number of Government Employees in the country (A+B)**	**1.71**
D	Total workforce in India	53.53
E	**Public Sector workforce as a share of total workforce [(C/D)*100]**	**3.19%**
F	Population of India (in crores)	142.58
G	**Public Sector workforce as a share of the total population**	**1.20%**

UT: Union Territory with Legislature

Source:
Total Workforce in India
1. Economic Survey 2021-22, Government of India, pg. 372.
Population of India
2. World Population Prospects 2022, United Nations

Annexure 9: Current Retirement Age in Select Countries

Current Retirement Age in Select Countries (for a person entering labour force at age 22)	
Country	**Retirement Age**
Australia	66
Belgium	65
Canada	65
Denmark	65.5
Finland	65
France	64.5
Germany	65.7
Greece	62
Iceland	67
Ireland	66
Israel[1]	67(M)/62(F)
Italy	62
Japan	65
South Korea	62
Mexico	65
Netherlands	66.3
New Zealand	65
Norway	67
Portugal	65.3
Spain	65
Sweden	65
Switzerland[1]	65(M)/64(F)
United Kingdom	66
United States	66
India[2]	**60**

Note:
1. Different retirement ages for men and women. M indicates male and F indicates female.
2. The retirement age varies from state to state. The average retirement age is 60 years.

Source:
All countries, except India
1. OECD Pensions at a Glance Database.

Annexure 10: Comparison of Countries Across Select Socio-Economic Indicators

Comparison of Countries Across Select Socio-Economic Indicators*											
Rank	GDP Per Capita (PPP, 2019)	Life Expectancy (2019)	IMR (Infant Mortality Rate, 2019)	MMR (Maternal Mortality Rate, 2017)	OOPE (Out-of-Pocket Expenditure on Healthcare, 2018)	EYS (Expected Years of Schooling, 2020)	MYS (Mean Years of Schooling, 2020)	HDI (Human Development Index, 2020)	Power Consmuption (Kwh Per capita, 2020)	Employment in Agriculture (in ascending order, 2019)	LFPR (Labor Force Participation Rate - Female, 2020)
1	Switzerland	Hong Kong	Hong Kong	Hongkong	South Africa	Australia	Germany	Norway	Norway	Singapore	Sweden
2	Ireland	Japan	Japan	Italy	France	Belgium	Canada	Ireland	Canada	Argentina	New Zealand
3	Norway	Switzerland	Finland	Norway	Netherlands	Sweden	Switzerland	Switzerland	Sweden	Hong Kong	China
4	Singapore	Spain	Norway	Poland	United States	Finland	United States	Hong Kong	UAE	Belgium	Switzerland
5	United States	Singapore	Sweden	Czechia	Thailand	Denmark	United Kingdom	Germany	United States	Israel	Vietnam
6	Denmark	Italy	Singapore	Finland	Ireland	New Zealand	Israel	Sweden	Finland	United Kingdom	Norway
7	Australia	South Korea	Czech Republic	Israel	Germany	Ireland	Norway	Australia	Taiwan	Germany	Singapore
8	Netherlands	Sweden	Spain	United Arab Emirates	United Arab Emirates	Netherlands	Finland	Netherlands	Saudi Arabia	United States	Australia
9	Sweden	Australia	Italy	Denmark	Japan	Norway	Japan	Denmark	South Korea	UAE	Netherlands
10	Austria	Norway	South Korea	Spain	New Zealand	Argentina	New Zealand	Finland	Australia	Canada	Canada
11	Finland	Israel	Belgium	Sweden	Denmark	Spain	Australia	Singapore	New Zealand	Sweden	Thailand
12	Hong Kong	France	Austria	Austria	Sweden	United Kingdom	Czechia	United Kingdom	Singapore	Norway	United Kingdom
13	Germany	Ireland	Ireland	Belgium	Czech Republic	Germany	Ireland	Belgium	France	Netherlands	Israel
14	Belgium	Canada	Israel	Ireland	Norway	Hong Kong	Denmark	New Zealand	Switzerland	Denmark	Denmark
15	Canada	Netherlands	Australia	Japan	Saudi Arabia	Czechia	Austria	Canada	Israel	Saudi Arabia	UAE
16	Israel	Austria	Portugal	Netherlands	Canada	Turkey	Poland	United States	Austria	France	Peru
17	UAE	Finland	Germany	Switzerland	Colombia	South Korea	Sweden	Austria	Czechia	Australia	Germany
18	New Zealand	Belgium	Denmark	Australia	United Kingdom	Portugal	Netherlands	Israel	Japan	Switzerland	United States
19	United Kingdom	New Zealand	Netherlands	Germany	Turkey	Singapore	Hong Kong	Japan	Belgium	Czech Republic	Austria

Annexure 10: Comparison of Countries Across Select Socio-Economic Indicators

Comparison of Countries Across Select Socio-Economic Indicators*											
Rank	GDP Per Capita (PPP, 2019)	Life Expectancy (2019)	IMR (Infant Mortality Rate, 2019)	MMR (Maternal Mortality Rate, 2017)	OOPE (Out-of-Pocket Expenditure on Healthcare, 2018)	EYS (Expected Years of Schooling, 2020)	MYS (Mean Years of Schooling, 2020)	HDI (Human Development Index, 2020)	Power Consmuption (Kwh Per capita, 2020)	Employment in Agriculture (in ascending order, 2019)	LFPR (Labor Force Participation Rate - Female, 2020)
20	Japan	United Kingdom	Switzerland	United Kingdom	Australia	Chile	South Korea	South Korea	Netherlands	Japan	Malaysia
21	France	Denmark	United Kingdom	France	Austria	Switzerland	Russia	Spain	Russia	Austria	Finland
22	Italy	Germany	France	Portugal	Finland	United States	Belgium	France	Germany	Finland	Russia
23	South Korea	Taiwan	Poland	Singapore	Belgium	Poland	UAE	Czechia	Ireland	Italy	Ireland
24	Spain	Portugal	Taiwan	New Zealand	Romania	Canada	Taiwan	Italy	Spain	Spain	Hong Kong
25	Taiwan	Chile	New Zealand	Canada	Poland	Israel	Singapore	UAE	China	Ireland	Portugal
26	Czech Republic	Czech Republic	Canada	Taiwan	Israel	Austria	France	Poland	Portugal	Taiwan	Japan
27	Portugal	United States	Russia	South Korea	Spain	Italy	Romania	Portugal	Malaysia	South Korea	South Korea
28	Saudi Arabia	UAE	United States	Chile	Italy	Saudi Arabia	Argentina	Saudi Arabia	Denmark	South Africa	Indonesia
29	Poland	Poland	Saudi Arabia	Russia	Brazil	France	Chile	Chile	Hong Kong	Portugal	Czech Republic
30	Chile	Turkey	Romania	Saudi Arabia	Argentina	Brazil	Italy	Argentina	Italy	Russia	Spain
31	Romania	Colombia	Chile	Turkey	Switzerland	Japan	Malaysia	Romania	United Kingdom	New Zealand	Taiwan
32	Russia	Thailand	United Arab Emirates	Uruguay	Peru	Russia	Spain	Russia	Poland	Chile	France
33	Malaysia	China	China	Romania	Portugal	Peru	Saudi Arabia	Turkey	Chile	Brazil	Colombia
34	China	Argentina	Malaysia	China	Singapore	Thailand	South Africa	Malaysia	South Africa	Poland	Belgium
35	Mexico	Peru	Thailand	Malaysia	Hong Kong SAR, China	Mexico	Peru	Mexico	Turkey	Malaysia	Nigeria
36	Argentina	Malaysia	Argentina	Mexico	South Korea	Colombia	Philippines	Peru	Argentina	Mexico	Brazil
37	Turkey	Brazil	Turkey	Egypt	Chile	United Arab Emirates	Portugal	Thailand	Romania	Colombia	Poland
38	Brazil	Romania	Peru	Thailand	Indonesia	Romania	Mexico	Colombia	Brazil	Turkey	Argentina
39	Thailand	Vietnam	Colombia	Argentina	Malaysia	China	Colombia	Brazil	Vietnam	Egypt	Romania
40	Peru	Mexico	Mexico	Viet Nam	Taiwan	South Africa	Viet Nam	China	Thailand	Romania	Chile
41	Colombia	Saudi Arabia	Brazil	Brazil	China	Malaysia	Indonesia	Indonesia	Mexico	Philippines	South Africa
42	South Africa	Russia	Vietnam	Colombia	Russia	Indonesia	China	Philippines	Egypt	China	Philippines
43	Indonesia	Bangladesh	Egypt	Peru	Mexico	Egypt	Turkey	South Africa	Peru	Peru	Mexico
44	Philippines	Egypt	Indonesia	South Africa	Vietnam	Philippines	Brazil	Egypt	Colombia	Indonesia	Italy

Annexure 10: Comparison of Countries Across Select Socio-Economic Indicators

Comparison of Countries Across Select Socio-Economic Indicators*

Rank	GDP Per Capita (PPP, 2019)	Life Expectancy (2019)	IMR (Infant Mortality Rate, 2019)	MMR (Maternal Mortality Rate, 2017)	OOPE (Out-of-Pocket Expenditure on Healthcare, 2018)	EYS (Expected Years of Schooling, 2020)	MYS (Mean Years of Schooling, 2020)	HDI (Human Development Index, 2020)	Power Consmuption (Kwh Per capita, 2020)	Employment in Agriculture (in ascending order, 2019)	LFPR (Labor Force Participation Rate - Female, 2020)
45	Egypt	Indonesia	Philippines	Philippines	Philippines	Viet Nam	Thailand	Viet Nam	Indonesia	Thailand	Bangladesh
46	Vietnam	Philippines	Bangladesh	Pakistan	Pakistan	India	Egypt	India	India	Nigeria	Saudi Arabia
47	Nigeria	India	South Africa	India	Egypt	Bangladesh	Nigeria	Bangladesh	Philippines	Pakistan	Turkey
48	India	Pakistan	India	Bangladesh	India	Nigeria	India	Pakistan	Pakistan	Vietnam	India
49	Bangladesh	South Africa	Pakistan	Indonesia	Bangladesh	Pakistan	Bangladesh	Nigeria	Bangladesh	Bangladesh	Pakistan
50	Pakistan	Nigeria	Nigeria	Nigeria	Nigeria	**Taiwan	Pakistan	**Taiwan	Nigeria	India	Egypt

Note:
* Countries with Gross Domestic Product (GDP) exceeding USD 200 Billion have been included in the comparison. The countries have been arranged based on their performance on various indicators, with the top-ranked country being the best performer. In terms of the indicator 'Employment in Agriculture', the country with the lowest share of the workforce in agriculture has been assigned the first rank.
** Information not available.

Sources:
GDP Per Capita; Life Expectancy; IMR; OOPE; Employment in Agriculture
1. World Development Indicators, World Bank.
MMR
2. All Countries except Taiwan and Hongkong –
World Health Organisation portal.
3. Taiwan – Gender at a Glace report in R.O.C. (Taiwan);
4. Hongkong – Accessed at https://www.socialindicators.org.hk/en/indicators/women/28.4
EYS; HDI
5. Human Development Index Report 2020, United Nations Development Programme
MYS
6. Global Data Lab, Institute for Management Research, Radboud University.
LFPR
7. Labor Force Statistics, International Labor Organisation
Power Consumption
8. Our World in Data portal.

Annexure 11: Calculation of Tax-to-GDP Ratio of India

Calculation of Tax-to-GDP Ratio of India						
Level of Government	**Heads (in ₹ Crore)**	**2019-20**	**2018-19**	**2017-18**	**2016-17**	**2015-16**
Union Government	a. Gross Tax Revenue	2,010,059	2,080,465	1,919,009	1,715,822	1,455,648
	b. Non-Tax Revenue (excl. Dividends and Profits)	141,025	122,284	101,384	149,814	139,133
State Governments	c. Own Tax and Own Non-Tax Revenue (States' Own Revenue)	1,484,884	1,433,590	1,310,098	1,117,616	1,034,936
General Government	d. Total Tax Revenue (a+b+c)	3,635,968	3,636,339	3,330,491	2,983,252	2,629,717
	e. Gross Domestic Product (at Current Prices)	20,103,593	18,899,668	17,090,042	15,391,669	13,771,874
	f. Tax-to-GDP ratio (d/e)	**18.08%**	**19.24%**	**19.48%**	**19.38%**	**19.09%**

Note:
1. Union's Non-Tax Revenue here does not include Dividends and Profits because of high variability over the years. For instance, Dividend/ Surplus of the RBI, Nationalized Banks, and Financial Institutions transferred to the Union Government recorded a substantial increase from Rs. 70,868 Crores in FY19 to Rs. 150,589 Crores in FY20 due to a one-time windfall transfer from the RBI.

Source:
a) Union Government – Gross Tax Revenue; Non-Tax Revenue
1. Budget at a Glance, Union Budget Documents of 2017-18, 2018-19, 2019-20, 2020-21, 2021-22.
b) State Governments – Own Tax Revenue; Own Non-Tax Revenue
2. Handbook of Statistics on Indian States, Reserve Bank of India.
c) Gross Domestic Product (at Current Prices)
3. Annual and Quarterly Estimates of GDP at Current Prices (2011-12 series), Official Website of the Ministry of Statistics and Programme Implementation.

Annexure 12: Composition of Outstanding Liabilities of States and Union Territories

Composition of Outstanding Liabilities of States and Union Territories (in ₹ Crore)				
Year	**Outstanding Liabilities**	**Market Borrowings**	**Loans and Advances from Centre**	**Other***
2004	903,173.7	179,916.7	192,981.2	530,275.8
2009	1,470,195.0	401,923.7	143,870.2	924,401.1
2014	2,471,263.3	1,050,369.1	145,809.4	1,275,084.8
2019	4,786,769.5	2,561,386.8	171,534.3	2,053,848.4
2022 RE	6,793,770.0	4,235,944.3	457,434.3	2,100,391.4

*Other sources includes liabilities in Public Account i.e. transactions relating to Provident Funds, Reserve Funds, and Deposit and Advances, and others like power bonds, Ujwal Discoms Assurance Yojana (UDAY) bonds, Compensation and other bonds, WMA from RBI, Loans from Banks and FIs, and Contingency Fund.

Data from this table has been used to generate Figure 9.

Source:

For the years 2009, 2014, 2019 and 2022

1. State Finances: A Study of Budgets of 2022-23, Reserve Bank of India

For the year 2004

2. State Finances: A Study of Budgets of 2021-22, Reserve Bank of India.

Annexure 13: Article 280 of the Constitution of India

Article 280. Finance Commission.
(1) The President shall, within two years from the commencement of this Constitution and thereafter at the expiration of every fifth year or at such earlier time as the President considers necessary, by order constitute a Finance Commission which shall consist of a Chairman and four other members to be appointed by the President. (2) Parliament may by law determine the qualifications which shall be requisite for appointment as members of the Commission and the manner in which they shall be selected. (3) It shall be the duty of the Commission to make recommendations to the President as to – (a) the distribution between the Union and the States of the net proceeds of taxes which are to be, or may be, divided between them under this Chapter and the allocation between the States of the respective shares of such proceeds; (b) the principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India; (bb) the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Panchayats in the State on the basis of the recommendations made by the Finance Commission of the State; (c) the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Municipalities in the State on the basis of the recommendations made by the Finance Commission of the State; (d) any other matter referred to the Commission by the President in the interests of sound finance. (4) The Commission shall determine their procedure and shall have such powers in the performance of their functions as Parliament may by law confer on them.

Source: *Constitution of India, accessed at http://constitutionofindia.etal.in/*

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