



Speech of
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(Retd.)

CHIEF MINISTER OF UTTARAKHAND

On the Occasion of the

Visit of the
Thirteenth Finance Commission
To
Dehradun

Government of Uttarakhand

January 28, 2009

1. Hon'ble Dr. Kelkar, Chairman, Thirteenth Finance Commission, other distinguished members and officers of the Commission. It gives me immense pleasure to welcome you all to the state of Uttarakhand.
2. Your visit to the state has come at a time when the global economic meltdown and its impact on growth in India have made the immediate future uncertain. This is going to pose a new challenge to a Special Category State like Uttarakhand which is still trying to find its feet after coming into existence in 2000.
3. Mr. Chairman Sir, although you and your colleagues are well aware of the nature and problems being faced by the Special Category States and how critically dependent they are on the dispensations of the Finance Commissions, I would like to take this opportunity to say few words at the outset about the creation of Uttarakhand and some specific problems faced by it and thereafter I will dwell on the current and projected fiscal situation of the state.
4. Uttarakhand was carved out of Uttar Pradesh not because it was regarded as a financially viable state but mainly as recognition to the aspirations of the people of this hitherto neglected region. Given the specific nature of its terrain, economic structure,

resource endowments and weak fiscal capabilities it was accorded a 'special category' status.

5. Although creation of a new state should have given Uttarakhand an opportunity to start on a clean slate, this unfortunately did not turn out to be the case. The State has been disadvantaged right from the beginning. It inherited a debt of Rs. 2642.6 crore from its parent state at the time of attaining statehood. The debt burden thrust upon it during its separation from UP was not fair. Not only was it burdened with an unfair share of UP's debt, it received a measly sum of Rs 17 crore as opposed to Rs 4549 crore non-plan deficit grants received by Himachal Pradesh during the award period of the Eleventh Finance Commission. Besides this, the state was not given any additional assistance for the creation of minimum necessary infrastructure to establish even the mandatory organs of the state. This resulted in the state resorting to heavy borrowing to meet even its basic infrastructure requirements with a consequent rise in the debt burden.

6. As the revenue raising capability of a state as well as its expenditure needs are critically linked to its economic and demographic features, a brief introduction to the profile of Uttarakhand at this juncture would be in order.

7. Covering an area of 53483 sq kms, Uttarakhand has a very diverse topography ranging from plains in the South to snow-

covered peaks in the North. About 61 per cent of its area is under forest cover. The geography of the state has direct expenditure implications. The state is characterised by a large number of relatively small and dispersed habitations, as the terrain does not support large clusters of households. These features do not permit the state to exploit scale economies in public service delivery and therefore significantly increases the cost of delivering a minimal level of services to its people.

8. Creation of the state of Uttarakhand has indeed helped this erstwhile hilly region of Uttar Pradesh to improve its economic performance. Between 1999-2000 and 2006-07 its GDP grew at 9.0 per cent per annum as opposed to 7.0 per cent recorded by the Indian economy. However, the state still has a lot of catching up to do in view of the neglect of the region when it was part of Uttar Pradesh. This is obvious from its growth performance during 1993-94 and 1999-2000, which was a paltry 2.9 percent as against 6.6 % for the Indian Economy as a whole.

9. Although industrial growth in Uttarakhand has been impressive during 1999 -00 and 2006-07 out-migration amongst adult males is still very high in the state. This has led to a high incidence of both child and old age dependence. In addition, health indicators of women and children are also relatively weak. Another worrying aspect lately has been the literacy rates. These factors

call for a concerted increase in the level and quality of public services in the state.

10. Partly due to terrain, but also because of relatively low levels of investment, the state has come into existence with a weak infrastructure base. Per capita Plan outlay, though it showed some increase between 2001-02 and 2005-06, continues to be one of the lowest among the special category states. Substantial investments are needed to enhance the growth potential of the state and these need to be maintained and operated to derive full value. It may also be mentioned here that the share of Railways in GSDP has come down from 1.78 per cent in 1999-00 to 1.29 per cent in 2006-07. The present policy of Railways to extend Railway network in only those states who share the cost of the project is detrimental to improvement of infrastructure in backward areas. The Commission is requested to recommend that this practice should be discontinued, at least in the case of Special Category States as lack of a Railway network is a big impediment to economic growth in general and to industrialisation in particular.

11. Let me now dwell on the fiscal situation in Uttarakhand. Despite inheriting a debt of Rs. 2642.6 crore from its parent state at the time of attaining statehood, the state has come a long way on the fiscal front. Uttarakhand has made commendable revenue raising efforts ever since it came into existence. Its per capita sales

tax collection, at Rs 1107.3 in 2005-06, is the highest among the special category states. Thus, its tax effort in comparison to other special category states is indeed noteworthy.

12. However, the buoyancy witnessed during the award period of 12th Finance Commission, in our view, is over. Although we expect the composition of tax revenue to remain unchanged from 2010-11 to 2014-15 with Value Added Tax being the major revenue contributor followed by excise, we expect the tax buoyancy to be lower during the projection period as compared to the award period of 12th Finance Commission. As the buoyancy in VAT witnessed immediately after its introduction is tapering off, we have assumed the average buoyancy of VAT to be 1.09 for the forecast period. CST is being phased out and it will cease to exist by 2010-11. Excise revenue collection in the state although highly volatile till 2007-08, is projected to grow at the rate of nominal GSDP growth.

13. On the non tax revenue front also, the situation is not looking up as the sources of non-tax revenue are drying up for the state. Power was a major contributor to this pool. But due to change in power demand, there would be little power for trading and due to higher cost of maintenance of old projects, power would not be a major source of non-tax revenue. Similarly, the low buoyancy in revenues from forestry is a result of limits imposed on the

exploitation of forests for commercial purpose by stringent environmental regulations.

14. The expenditure needs of a hilly and backward state like Uttarakhand are much higher in comparison to the plains because of higher costs of creation and maintenance of assets, higher transport costs and higher cost of delivery of essential services. All these are critically linked to the harsh terrain, which do not permit the state to take advantage of agglomeration economies that characterise the provision of many essential services. The expenditures on social and economic services are projected to grow at the compound annual rate of 12 per cent between 2010-11 and 2014-15.

15. The total pre-devolution non-plan revenue deficit has been projected at Rs 39,397.41 cores for the period 2010-11 to 2014-15. The overall pre-devolution revenue deficit has been projected at Rs 54,765.86 crore for the same period. Our forecast takes into account the endeavor of the state to step up its revenue efforts. The expenditure requirements of this fiscally disadvantaged state are higher both on account of higher cost of delivery of services (due to terrain) and for bridging the gap with respect to the more prosperous states. Therefore, the support of the Finance Commission in meeting the projected revenue gap of Uttarakhand

will go a long way in ensuring the future prosperity as well as financial viability of Uttarakhand.

16. About 61 per cent of Uttarakhand's area is under forests. I would like to emphasise that Uttarakhand's forest resources should be treated as a special feature with important implications for centre-state financial transfers. It is now well established that forests are a resource that generates benefits to a multiple groups of stakeholders far beyond the confines of the state where they are located. The potential beneficiaries exist at four levels – local, state, national and global. These benefits include direct consumptive (salvage, timber, fuel wood, fodder and minor forest products) and non-consumptive benefits such as ecotourism. Indirect benefits include carbon sequestration, biodiversity and watershed conservation.

17. Ecosystem services (ESS) flowing out of forest cover are defined as a wide range of conditions and processes through which natural ecosystems, and the species that make them up, sustain and fulfil human life. Indeed, it is almost impossible to give a precise value of ESS flowing from a state to other states/regions of the country. However, in order to maintain the natural capital and flow of ESS, individuals, communities and states must be given economic incentive.

18. I would therefore make an earnest request to the Finance Commission to give due weight to the role of Uttarakhand's forests as a national and even global resource. Since this is a permanent feature of the state's economic structure, the best way to address it is to build it into the devolution formula with an appropriate weight. In the absence of such an amendment to the formula, it should be treated as special problem and given due consideration in arriving at the total quantum of transfers to the state.

19. Now I would like to draw your kind attention to another unique feature of Uttarakhand- the Yatra tourism. Uttarakhand is host to Haridwar, Rishikesh, the Char Dham and the sources of the sacred Ganga & Yamuna. Beside these, there are many other pilgrimage sites and sites of historical and religious importance. These pilgrimage sites are a national heritage and play an important role in promoting national unity and integrity.

20. The pressure of yatri inflow mounts during the May-November period when most of the shrines become accessible. While the number of tourists has increased from 12.9 million in 2003 to 22.3 million in 2007, the population of the state is only 8.5 million as per the 2001 Census. While the state's revenue earnings from these *yatris* are very little or negligible due to their low spending power, the state has to incur huge expenditure in providing them basic infrastructure. Besides the Char Dham and

the prayags, there are a number of other pilgrimage sites and sites of historical and religious importance which attract a lot of visitors. The requests for grants to cope up these special problems are detailed in Volume IV of the memorandum.

21. Uttarakhand by virtue of its geo-tectonic setting, physiographic conditions and extreme seasonal precipitation is vulnerable to a large variety of disasters. The state faces the fury of flash-floods and landslides during monsoons. Earthquake, avalanches, hailstorms and forest fires are other common disasters in the state. The Uttarakhand government, therefore, after carefully reviewing the performance of the CRF has suggested some modifications in its memorandum in order to extend its coverage and to enlarge its scope.

22. In view of the special circumstances/problems arising out of reorganization of the state and the dire need for up-gradation of standards in Uttarakhand, we request the Commission to take a pragmatic approach in this regard and recommend these grants, request for which is detailed in a separate volume (Volume IV).

23. Last, but not least, I would like to suggest some improvements in the devolution formula. While it is important to incentivise revenue transfers to states to promote efficiency, it is equally important to ensure that the criteria used are objective and reliable. While per capita income is a good criterion for determining the

revenue raising capacity of a state, the structure of the economy also plays a critical role and should be given due weight in the devolution formula.

24. The use of infrastructure index as a criterion for the devolution of taxes is important as it recognises the disabilities of the states with poor infrastructure particularly in attracting investments. This assumes greater significance in the context of the present regime of liberalisation and de-licensing, where infrastructure-related factors are influential in shaping the investment decisions of private investors. However, the 12th Finance Commission chose to drop it. We would, therefore, urge the Commission to reintroduce the infrastructure index into the tax devolution criteria and assign it a suitable weight.

25. The criteria of tax effort and fiscal discipline are welcome developments and much needed for providing incentive to the states to give up a profligate fiscal stance. As fiscal discipline is often linked to the state's own revenue and expenditure, I would like to submit that Uttarakhand still has a low revenue base and a sub-normal expenditure pattern. The existing expenditure levels in Uttarakhand are likely to be sub-normal because all the programmes for creating infrastructure and pursuing developmental goals are not yet in place. Added to this is the relatively higher financial burden in providing a given level of

public services in a hilly state. Also at present, over 25 percent of the sanctioned posts in Uttarakhand are vacant. As the number of vacancies gets filled up, the wage bill too will go up. While keeping a check on government employment may be a laudable objective, the current vacancies are essentially in public services like health and education, police and cannot be done away with.

26. I must re-emphasize that the state is committed to improving its fiscal situation in the coming years. The fiscal situation in the state was improving until recently and the state was able to achieve revenue as well as primary surplus in the past. However, the impact of the Sixth Pay Commission award has substantially altered the situation for the worse and it is quite unlikely that without substantial support from the Finance Commission, the state would be able to regain its fiscal health in the medium-term. Therefore, the support of the Finance Commission will be critical for the financial viability and future prosperity of the state.

Jai Hind