EXECUTIVE SUMMARY

Responding to the recommendations of the Twelfth Finance Commission (TFC), the Jammu and Kashmir Government enacted Fiscal responsibility and Budget Management (FRBM) Act in August 2006. The Act sets out a reform agenda for achieving medium and long term growth stability for the economy of the State through fiscal correction path. To carry out the reforms enshrined in the Act, the State Government took some decisions like introduction of new pension scheme, bringing more items under the ambit of VAT and a host of other institutional and sectoral reform measures as announced in the annual budgets subsequently. The measures undertaken are intended to improving the quality of public expenditure and to promote fiscal stability. The reforms undertaken have shown signs of improvement in the financial health of the State as the State has done well in maintaining the revenue surplus and there has also been increase in capital expenditure which is encouraging.

The State Government has done well in establishing an institutional mechanism on fiscal transparency and accountability as is evident from the year on year presentation of outcome budgets. These outcomes indicators tend to serve the limited purpose of measuring the department–wise performance against the targets. They do not, however, give the macro picture of the status of financial management including debt position for the benefit of the State Legislature and other stake holders.

The Comptroller and Auditor General's civil audit reports step in to fill this gap. The reports have been commenting upon the Government's finances in its composite reports containing the audit paragraphs, performance reviews as well apart from the chapter on the finances of the State. Since these comments formed part of the civil audit reports, it was felt that the audit findings on State finances remained camouflaged in the large body of the audit findings on compliance and performance audit. The obvious fallout of this reporting was that the financial management portion of these findings did not receive proper attention. In recognition of the need to bring State finances to centre stage once again, a Stand alone Report on State Government finances is considered as an appropriate audit response to this challenge. Accordingly, from the report year 2009 onwards, Comptroller and Auditor General of India has decided to bring out a separate volume titled "Report on State Finances".

The Report

Based on the audited accounts of the Government of Jammu and Kashmir for the year ending March 2009, this report provides an analytical review of the Annual Accounts of the State Government. This report is structured in three Chapters.

Chapter I *is based on audit of Finance Accounts and makes an assessment of State Government's fiscal position as on 31 March 2009. It provides an insight into trends in committed expenditure, borrowing pattern besides a brief account of central funds transferred directly to the State implementing agencies through off budget route.*

Chapter 2 *is based on audit of Appropriation Accounts and it gives the grant-by-grant description of appropriations and the manner in which the allocated resources were managed by service delivery departments.*

Chapter 3 *is an inventory of the State Government's compliances with various reporting requirements and financial rules. The report also has an appendage of additional data collated from several sources in support of the findings. Appendix 1.2 at the end gives a glossary of selected terms related to State economy, as used in this report.*

Audit findings and recommendations

The rules under the FRBM act are yet to be approved by the Government (March 2009). The State Government did not meet the FRBM targets by the prescribed deadline (31 March 2009) due to which the State was denied a debt relief estimated at Rs. 473 crore recommended under the TFC award. The State also lost Rs. 229 crore as the Government did not hold Panchayat elections. The State Government needs to implement the Panchayat Raj Act and hold the panchayat elections to avail of the benefits.

The expenditure pattern of the State reveals that the revenue expenditure exhibited a declining trend during 2004-09, but continued to share a dominant proportion in the total expenditure of the State and was around 71 per cent during 2008-09. Moreover, within the revenue expenditure, the non-plan revenue expenditure at Rs 11,734 crore constituted about 97 per cent. The continued prevalence of fiscal and primary deficits indicates the increasing reliance of the State on borrowed funds. This is coupled with non collection of revenue arrears for the past several years which are increasing day by day. Suitable measures need to be initiated to compress the non-plan revenue expenditure and to mobilise additional resources both through tax and non tax sources in the ensuing years.

Review of Government Investment

As of 31 March 2009, Government had invested Rs. 364.61 crore in Statutory Corporations, Rural Banks, Joint Stock Companies and Co-operatives. The average return on this investment was 8.60 per cent while the Government paid an average interest at the rate of 9.7 per cent on its borrowings during 2007-09. Out of 17 working companies, only one company (Jammu & Kashmir Bank) had finalised its accounts for 2008-09 (September 2009) and earned profit of Rs. 409.84 crore for the year. Of the fifteen other[1] *working companies, which*

[1] Excluding one company (viz. Jammu and Kashmir State Cable Car Corporation Limited), which has not prepared the Profit and Loss Account since inception.

finalised their accounts for previous years by September 2009, only three companies earned an aggregate profit of Rs. 2.51 crore. Of the 12 loss-incurring working Government companies, nine had accumulated losses aggregating Rs. 524.01 crore, which exceeded their aggregate paid-up capital of Rs. 67.05 crore. Despite their poor performance and complete erosion of paid-up capital, the State Government continued to provide financial support to these companies in the form of contribution towards equity, further grant of loans, subsidy, grants, etc. Time has come to revisit the working of loss making public sector undertakings incurring huge losses and work out either a revival strategy or close down the undertakings.

Cash management

Jammu and Kashmir Government have no agreement with RBI for carrying out State transactions. These activities are carried out by the State through Jammu and Kashmir Bank Limited. Government obtains temporary loan from Jammu and Kashmir Bank for its ways and means requirements. The State Government took temporary loan from the Bank for all the 365 days during the year. The maximum temporary loan obtained was Rs. 2480.43 crore as of 29 September 2008. The total temporary loans raised during the year amounted to Rs. 2,983.48 crore. A balance of Rs. 2,055.22 crore was also outstanding as on 1st April 2008. Government repaid Rs. 2,648.45 crore during the year leaving a balance of Rs. 2,290.25[2] crore as of 31 March 2009. During the year 2008-09, Rs. 217.65 crore was paid as interest by the Government on such loans. Necessary steps need to be taken to avoid overdrafts from the Bank by creating a fund to meet these temporary needs

Funds transferred directly by GOI to the State implementing agencies

The Central Government has been transferring a sizeable quantum of funds directly to the State Implementing Agencies for various schemes/ programmes in social and economic sectors. An approximate amount of Rs. 1,429 crore was transferred by the GOI directly to the implementing agencies during 2008-09. As these funds are not routed through the State Budget/Treasury System, Annual Finance Accounts do not capture the flow of these funds and to that extent State's receipts and expenditure as well as other fiscal variables/ parameters derived from them are understated.

Consolidated data-base at apex level was not maintained by the State Government. A system has to be urgently put in place to ensure proper accounting of these funds and the updated information should be validated by the State Government and sent to the Accountant General (Accounts & Entitlement).

Financial management and budgetary control

There was an overall excess of Rs. 982.50 crore as a result of excess of Rs. 3,277.38 crore in eight grants under

[2] The figures under reconciliation (July 2009)

Revenue Section and nine grants and one appropriation under Public Debt-Repayments (Loan Section), offset by saving of Rs. 2,294.88 crore in 21 grants and five appropriations under Revenue Section and 19 grants under Capital Section. There were also instances of persistent savings in some grants, excessive expenditure, expenditure without provision of funds, drawal of funds to avoid lapse of budget grant, unnecessary supplementary provisions, etc.

There was also significant pendency in submission of detailed countersigned bills against abstract contingent bills. Against a total amount of Rs. 2725 crore DC bills drawn by various DDOs (26 departments) during March 1996-2009 have not been submitted (June 2009) to the Principal Accountant General, despite lapse of period ranging from two months to eleven years. Non-rendition of DC bills for such a huge amount over a very long period is fraught with the risk of misappropriation.

Non-reconciliation of expenditure by State Offices with Principal Accountant General (Accounts & Entitlement) is the main area to be given attention for updated expenditure. 141 Controlling Officers did not reconcile expenditure amounting to Rs. 5791 crore as of October 2009 which constituted 34 per cent of the total net revenue and capital expenditure.

Errors in budgeting process were also noticed.

Financial reporting

State Government's compliance with various rules, procedures and directives was unsatisfactory as is evident from delays in furnishing of utilisation certificates against the loans and grants from various institutions. There was also delay in submission of annual accounts by some autonomous bodies. Accounts of Ladak Autonomous Hills District Councils', Leh and Kargil have not been prepared since their formation.