Executive Summary

Background

In June 2005, Orissa Government responded to the Twelfth Finance Commission's recommendation by legislating its "Fiscal Responsibilities and Budget Management Act (FRBM)." It sets out a reform agenda through fiscal correction path in the medium term with the long-term goal of securing growth stability for its economy. The State Government's commitment to carry forward these reforms is largely reflected in their policy initiatives announced in the budget subsequently. While the benefits of FRBM legislation have been realized to a great extent already, in terms of reduction in major deficit indicators etc, several other policy measures and institutional reform will have to be undertaken to enable building up of the much needed 'fiscal space' for improving the quality of public expenditure and to promote fiscal stability. Fiscal indicators alone, however, do not give the 'big picture' of the status of financial management including cash management for the benefit of the State and other stakeholders.

The Comptroller and Auditor General's civil audit reports step in to fill this gap. C&AG's reports have been commenting upon the Government's finances for over three years since the FRBM legislation and have published three reports already. Since these comments formed part of the civil audit report, it was felt that the audit findings on State finances remained camouflaged in the large body of audit findings on compliance and performance audits. The obvious fallout of this well-intentioned but all-inclusive 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 center-stage once again, a stand-alone report on State Government finances is considered an appropriate audit response to this challenge. Accordingly, from the report year 2009 onwards, C&AG has decided to bring out a separate volume titled "Report on State Finances."

The report

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

Chapter 1 is based on the audit of Finance Accounts and makes an assessment of Orissa Government's fiscal position as at 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 the service delivery departments.

Chapter 3 is an inventory of Government's compliance 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 4.1 at the end gives a glossary of selected terms related to State economy, as used in this report.

Audit findings and recommendations

Return to fiscal correction

Built upon early gains in achieving deficit targets, the government continued to consolidate the same in the current year (2008-09) despite an overall slump in the economy in the country as a whole and pressure on the committed expenditure due to implementation of the Sixth Pay Commission award and higher food subsidy costs due to introduction of Rupees two a kilo of rice for certain segment of the population. Given the robustness of the economy, the State can still achieve the FRBM targets with a concerted effort through better tax compliance, reductions in tax-collection costs, focusing on regaining revenue arrears (para 1.3.3) and by pruning unproductive expenditure. The State also needs to ensure that the Government of India releases all grants due to it by timely fulfillment of all conditionalties / pre-requisites (para 1.3).

Greater priority to capital expenditure

The State may consider reprioritising its outlays, in view of the fact that its capital expenditure-aggregate expenditure ratio is lower than the average for all the States (Table 1.13).

Adequate thrust to development and social sector expenditure

The per capita development expenditure and per capita social sector expenditure in Orissa is much lower than the national average even though the state is spending adequate amounts compared to the rest of the country (Table 1.13). This calls for a serious introspection on whether the capacity of the State to utilize expenditure for developmental and social outcomes can be improved by better design of schemes, reducing administration costs, timely implementation, closer monitoring etc. Cost and time overruns of incomplete projects (para 1.6.2) are inevitable by-products of weak control systems. The State can work towards further improvements in this area so that people derive envisaged benefits in the quickest possible time. Outcome budgeting should be able to mitigate this weakness.

Need for emphasis on Outcome Budgeting

The State Government has done well in establishing an institutional mechanism on fiscal transparency and accountability as evident from the State's Fiscal Correction Path and year-on-year presentation of Fiscal Strategy Policy Statement and Medium Term Fiscal Plan along with certain actionable fiscal indicators to the State Legislature. However, the Government's critical part of fiscal reforms did not include outcome budgets during 2005-09 as recommended by the Twelfth Finance Commission (Para 4.61). Thus, the issues of economy, efficiency and effectiveness were not taken into consideration while preparing the budgets to evaluate whether the same outcomes can be achieved at lower costs and the same costs can produce better results and the budgets are delivering the intended outcomes to the stakeholders.

Review of Government investments

The average return on Government's investments in Statutory Corporations, Rural Banks, Joint Stock Companies and Co-operatives was very meager except for one Government company (Orissa Mining Corporation) in the last two years since 2007-08 (para 1.6.3). This is obviously an unsustainable proposition. The State Government should therefore hasten to seek better value for money in investments as otherwise high-cost borrowed funds will continue to burden investments with low financial return.

Prudent cash management

The State Government maintained more than the minimum cash balance (Rs 1.28 crore) including the cash balance investment with the Reserve Bank of India. One option for prudent financial management would be to maintain optimum cash balances and use the surpluses to settle some of the high cost bonds.

Debt sustainability

The Government consistently maintained reducing trend in the Fiscal-GSDP ratio from over 42 *per cent* in 2006-07 to around 32 *per cent* in 2008-09 indicating a tendency towards debt stabilization which would eventually improve the debt sustainability of the State. During 2008-09, the fiscal liabilities of the state increased by Rs 643 crore to Rs 39168 crore over the previous year but remained below 160 *per cent* of the Revenue Receipts as against the prescribed 300 *per cent* in State's FRBM Act.

Oversight of funds transferred directly from the GoI to the State implementing agencies

Funds flowing directly to the implementing agencies through off-budget routing inhibits FRBM requirements of transparency and therefore bypass accountability. There is no single agency monitoring its use and there is no readily available data on the amounts actually spent in any particular year on major flagship and other important schemes. 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 as well as the Accountant General (A&E).

As indicated above, several of the TFC recommendations viz. deficit indicators, introduction of VAT, Contributory Pension Scheme, Guarantee Redemption Fund, Consolidated Sinking Fund for debt redemption etc. have been successfully implemented by the State Government. In order to ensure that the State remains firmly on the fiscal correction path, the following areas of concern need to be adequately addressed – greater priority has to be given to capital expenditure and asset creation in the state so as to bring the state at par with other states of the country; salaries will have to be contained within the 35 *per cent* ceiling recommended by the TFC (at present it is 41 *per cent*); Outcome Budgeting should be introduced in order to ensure value for money; improved cost-recovery from irrigation projects, better returns from State Commercial Undertakings and prudent cash management – all these, if effectively addressed will enable the State to improve its fiscal and financial management in the years to come.

Financial Management and Budgetary Control

During 2008-09, there was overall savings of Rs 9312.05 crore as a result of savings of Rs 9313.13 crore offset by excess of Rs 1.08 crore in two grants under Revenue Section and one grant under Capital Section which needs regularization under Article 205 of the Constitution of India (Para 2.2 and 2.3.7). The savings were mainly due to slow programme implementation. There were instances of savings exceeding Rs 10 crore in 12 grants which included huge savings of Rs 4832.16 crore in seven cases under five grants (Para 2.3.1). There were persistent savings ranging from nine to 74 *per cent* in 10 grants during 2004-09 (Para 2.3.2). There were also instances of excess expenditure and expenditure without provision of funds, unnecessary/excessive/inadequate supplementary provision, substantial surrenders, surrender of savings and non surrender of anticipated savings and rush of expenditure during the current year. Detailed bills were not submitted against large amount of advances drawn on abstract contingent bills (Para 2.4.1). Besides, large amounts were lying unspent in Personal Deposit Accounts at the end of the current year. Budgetary controls should be strictly observed to avoid such deficiencies in financial management. Last minute fund releases and issue of re-appropriation / surrender statement should be avoided.

Financial reporting

State Government's compliance with various rules, procedures and directives was unsatisfactory as evident from delays in furnishing utilization certificates against the grants from various grantee institutions. Delays were also noticed in submission of annual accounts by some autonomous bodies and departmental undertakings. There were instances of embezzlements, losses and misappropriations which were pending for settlement. Departmental enquiries in such cases should be expedited to bring the defaulters to book. Internal controls in all the organizations should be strengthened to prevent such cases in future.