Chapter I
Finances of the State Government

Profile of Kerala

The State of Kerala, located at the southern end of the country, accounts for one *per cent* of the total area of the country and about three *per cent* of the population. The State ranks highest (0.790) in the Human Development Index as against the All India value of 0.467. The literacy rate of 93.91 *per cent* and life expectancy at birth of 74 years are the highest in the country. Further, the infant mortality rate of the State (12 per thousand) is the lowest in the country. As shown in the **Appendix 1.1**, the State has less population below poverty line as compared to All India average. The State has shown marginally lower economic growth in the past decade. However, its Gross State Domestic Product (GSDP) for the period 2002-03 to 2011-12 has been 15.85 *per cent* as compared to 14.46 *per cent* in General Category States. During this period, its population also grew by 5.03 *per cent* only (lowest among General Category States) against 13.90 *per cent* in General Category States. The per capita income compound annual growth rate in Kerala (15.22 *per* cent) has been higher than that of the General Category States (13.09 *per* cent) in the current decade. However, the State has slightly higher urban and rural inequality compared to the All India average.

1.1 Introduction

This chapter is based on the audit of Finance Accounts and makes an assessment of the Kerala Government's fiscal position as on 31 March 2012. It provides a broad perspective of the finances of the Government of Kerala during 2011-12 and analyses critical changes in the major fiscal aggregates relative to the previous year, keeping in view of the overall trends during the last five years. The structure and form of Government Accounts have been explained in **Appendix 1.2 Part A** and the layout of the Finance Accounts is shown in **Appendix 1.2 Part B**. The methodology adopted for the assessment of the fiscal position of the State and norms/ceilings prescribed by the Kerala Fiscal Responsibility Act, 2003 are given in **Appendix 1.3.** As prescribed in the Act, the Government laid its Medium Term Fiscal Policy and Strategy Statement with Medium Term Fiscal Plan for 2011-12 to 2013-14 in the State legislature in July 2011.

1.1.1 Summary of Current Year's Fiscal Transactions

Table 1.1 presents the summary of the State Government's fiscal transactions during the current year (2011-12) *vis-à-vis* the previous year, while **Appendix 1.4** provides details of receipts and disbursements as well as the overall fiscal position during the current year.

Table 1.1 Summary of Current Year's Fiscal Operations

(₹in crore)

2010-11	Receipts	2011-12	2010-11	Disbursements	2011-12		
Section-A: Revenue					Non Plan	Plan	Total
30990.95	**Revenue receipts**	**38010.36**	**34664.81**	**Revenue expenditure**	**40717.41**	**5327.21**	**46044.62**
21721.69	Tax revenue	25718.60	15418.39	General services	20227.04	72.98	20300.02
1930.79	Non-tax revenue	2592.18	12110.80	Social services	12821.94	3401.92	16223.86
5141.85	Share of Union Taxes/ Duties	5990.36	4357.46	Economic services	4279.35	1852.31	6131.66
2196.62	Grants from Government of India	3709.22	2778.16	Grants-in-aid and Contributions	3389.08		3389.08
Section-B: Capital					Non Plan	Plan	Total
24.61	Miscellaneous Capital Receipts	**16.05**	**3363.69**	Capital Outlay	454.82	3398.10	**3852.92**
44.23	Recoveries of Loans and Advances	**54.90**	**761.74**	Loans and Advances disbursed	581.86	416.68	**998.54**
7188.90	Public Debt receipts*	**9798.96**	**1975.03**	Repayment of Public Debt*			**2893.06**
26.27	Contingency Fund	**33.92**	**33.92**	Contingency Fund			**20.80**
73753.97	Public Account receipts	**95829.74**	**70558.27**	Public Account disbursements			**91200.26**
4388.26	Opening Cash Balance	**5059.73**	**5059.73**	Closing Cash Balance			**3793.46**
116417.19	**Total**	**148803.66**	**116417.19**	**Total**			**148803.66**

Source: Finance Accounts of the State for 2010-11and 2011-12.

* Excluding net transactions under Ways and Means advances and overdraft

The following are the significant changes in fiscal transactions during 2011-12 over the previous year.

- The Revenue receipts, which include debt relief of ₹47.69 crore given by the Government of India during 2011-12 on the recommendations of Thirteenth Finance Commission (ThFC), grew by 22.65 *per cent* (₹ 7019.41 crore) relative to the previous year. The increase was due to increase in tax revenue (₹ 3,996.91 crore), grants-in-aid from the Government of India (₹ 1,512.60 crore), State's share of Union taxes and duties (₹ 848.51 crore) and non-tax revenue (₹ 661.39 crore). The total of tax revenues collected during 2011-12 (₹ 25,718.60 crore) was ₹ 953.54 crore more than the normative assessment made by the ThFC (₹ 24,765.06 crore) for the year but was lesser by ₹ 923.4 crore (3.5 *per cent*) than the projection made in the Medium Term Fiscal Plan (₹ 26,642 crore). The State's Own Non-tax revenue (₹ 2,592.18 crore) was in line with the target fixed in the Medium Term Fiscal Plan (₹ 2,531 crore) for the year 2011-12.

- The Revenue expenditure increased by ₹ 11,379.81 crore (32.83 *per cent*) due to increase in expenditure under General Services (₹ 4,881.63 crore), Social Services (₹ 4,113.06 crore), Economic Services (₹ 1,774.20 crore) and Grants-in-aid and Contributions (₹ 610.92 crore). Actual Non-Plan Revenue Expenditure during 2011-12 (₹ 40,717.41 crore) exceeded the normative assessment made by the ThFC (₹ 30,775.81 crore) by ₹ 9,941.6 crore (32.30 *per cent*).

- Capital expenditure increased by ₹ 489.23 crore (14.54 *per cent*) mainly due to increase in expenditure under Economic Services (₹ 329.80 crore), especially under 'Roads and Bridges' (₹ 252.92 crore).

- Public debt receipts increased by ₹ 2,610.06 crore due to increase in internal debt receipts by ₹ 2,564.31 crore and increase in borrowings from GOI by ₹ 45.75 crore. Public debt repayment increased by ₹ 918.03 crore.

- Public Account receipts and disbursements increased by ₹ 22,075.77 crore and ₹ 20,641.99 crore respectively over the previous year.

- The cash balance of the State decreased by ₹ 1,266.27 crore from ₹ 5,059.73 crore as on 31 March 2011 to ₹ 3,793.46 crore as on 31 March 2012.

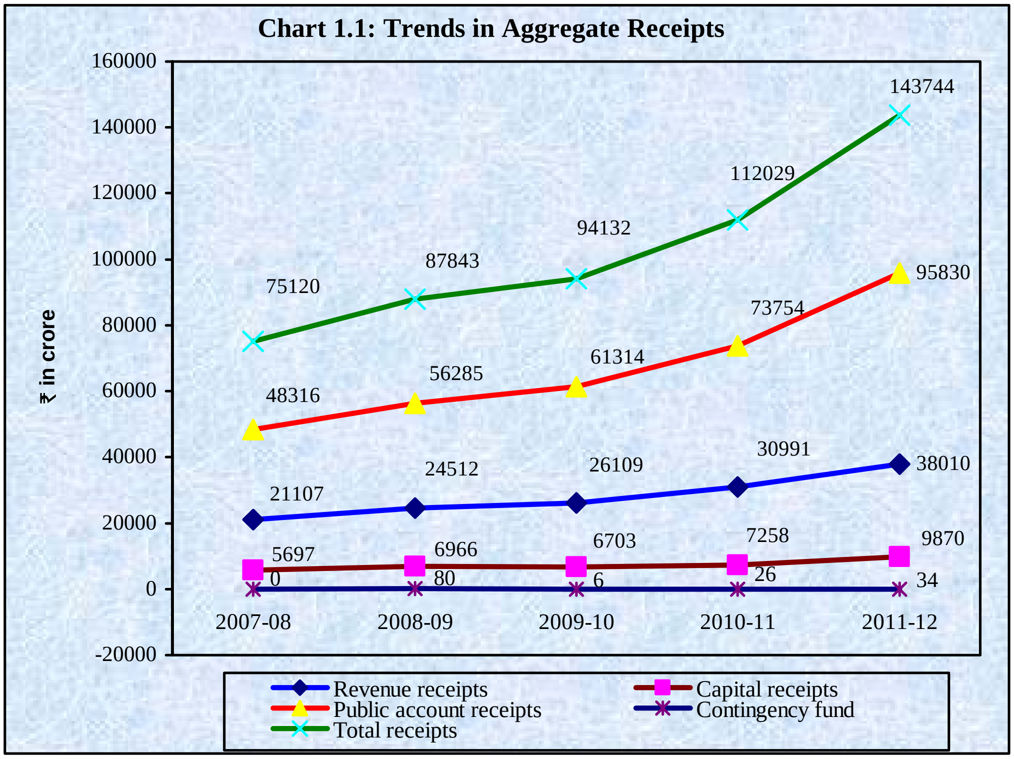
1.2 Resources of the State

1.2.1 Resources of the State as per Annual Finance Accounts

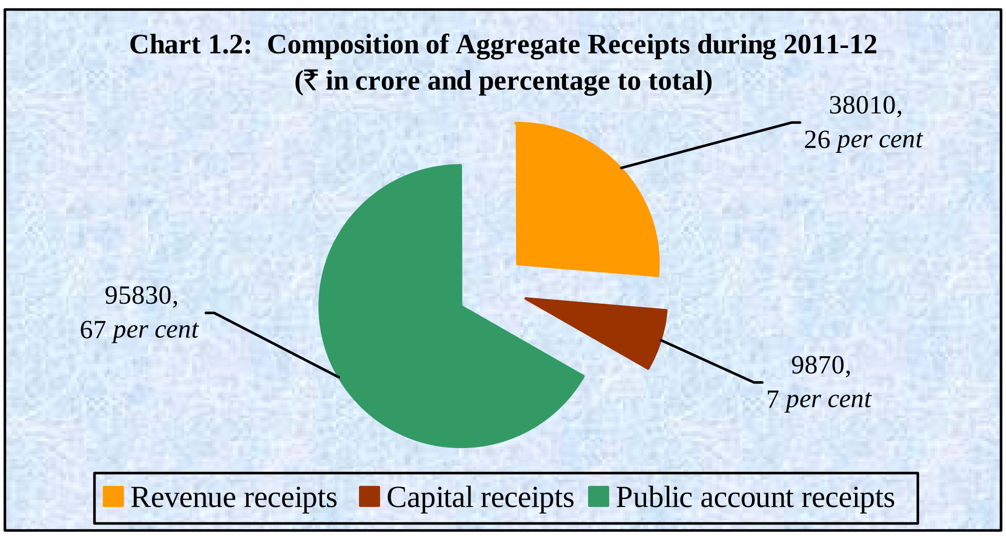
Revenue[1] and capital[2] are the two streams of receipts that constitute the resources of the Government. **Table 1.1** presents the receipts and disbursements of the Government during 2011-12 as recorded in the Finance Accounts 2011-12 while **Chart 1.1** depicts the trends in various components of the receipts of the State during 2007-12. **Chart 1.2** depicts the composition of resources of the State during 2011-12.

[1] Revenue receipts consist of tax revenues, non-tax revenues, State's share of Union taxes and duties and grants-in-aid from GOI.

[2] Capital receipts comprise miscellaneous capital receipts such as proceeds from disinvestment, recoveries of loans and advances, debt receipts from internal sources (market loans, borrowings from financial institutions/commercial banks) and loans and advances from GOI as well as accruals from the Public Account.



Source : State Finance Accounts of respective years



Note: Share of Contingency Fund was insignificant

The total receipts of the State Government for the year 2011-12 were ₹ 1,43,744 crore. Of these, Public Account receipts constituted ₹ 95,830 crore (67 *per cent*), revenue receipts constituted ₹ 38,010 crore (26 *per cent*) and capital receipts constituted ₹ 9,870 crore (7 *per cent*).

1.2.2 Funds transferred to State implementing agencies outside the State Budgets

The Government of India (GOI) has been transferring a sizeable quantum of funds directly to the State implementing agencies[3] for the implementation of various schemes/programmes in social and economic sectors for human and social development of the population. As these funds are not routed through the State Budget/State Treasury System, the Annual Finance Accounts do not capture the flow of these funds and to that extent, the State's receipts and expenditure as well as other fiscal variables/parameters derived from them remain understated. To present a holistic picture on the availability of aggregate resources in the State, details of funds directly transferred to the State implementing agencies during 2009-10 to 2011-12 are presented in **Table 1.2**.

Table-1.2: Funds transferred directly to State implementing agencies

(₹in crore)

Sl. No.	Programme/Scheme	Implementing agency in the State	2009-10	2010-11	2011-12
1.	Mahatma Gandhi National Rural Employment Guarantee Scheme	District Rural Development Agencies (Poverty Alleviation Unit)	467.71	704.23	951.05
2.	Pradhan Mantri Gram Sadak Yojana	Kerala State Rural Roads Development Agency	100.11	146.27	200.00
3.	Rural Housing - Indira Awaas Yojana	District Rural Development Agencies (Poverty Alleviation Unit)	194.71	185.91	196.20
4.	Rashtriya Madhyamik Shiksha Abhiyan	Secondary Education Development Society Kerala	8.93	15.13	19.10
5.	Ajeevika[4]	District Rural Development Agencies (Poverty Alleviation Unit)	44.27	42.62	38.43
6.	National Horticulture Mission	Kerala State Horticulture Mission	Nil	44.00	53.63
7.	National Rural Drinking Water Programme	Kerala Water Authority	152.04	159.83	113.39
8.	Sarva Shiksha Abhiyan	Primary Education Development Society of Kerala	119.90	196.61	170.22
9.	Swarna Jayanti Shahari Rozgar Yojana	State Poverty Eradication Mission (Kudumbashree)	9.50	4.74	13.77
10.	National Rural Health Mission	State Health and Family Welfare Society	245.83	236.86	343.85
11.	Rashtriya Swasthya Bima Yojana	Comprehensive Health Insurance Agency of Kerala	18.34	52.69	65.92
12.	Integrated Watershed Management Programme	District Rural Development Agencies (Poverty Alleviation Unit)	3.20	16.88	10.82
13.	Others[5]		237.59	358.14	297.62
	Total		**1602.13**	**2163.91**	**2474.00**

Source: Appendix VII of Finance Accounts 2011-12.

As per Finance Accounts 2011-12, GOI directly transferred ₹ 2,474 crore to the State implementing agencies for implementation of 30 central schemes (total release of ₹ five crore and above) during 2011-12. While the direct transfer of funds increased under Mahatma Gandhi National Rural Employment Guarantee Scheme, Pradhan Mantri Gram Sadak Yojana, National Rural Health Mission etc.,

[3] State implementing agency includes any organisation/institution including non-governmental organisation which is authorised by the State Government to receive funds from the Government of India for implementing specific programmes in the State, e.g. Primary Education Development Society of Kerala for Sarva Shiksha Abhiyan, Kerala State Health and Family Welfare Society for the National Rural Health Mission and Kerala State Rural Roads Development Agency for Pradhan Mantri Gram Sadak Yojana .

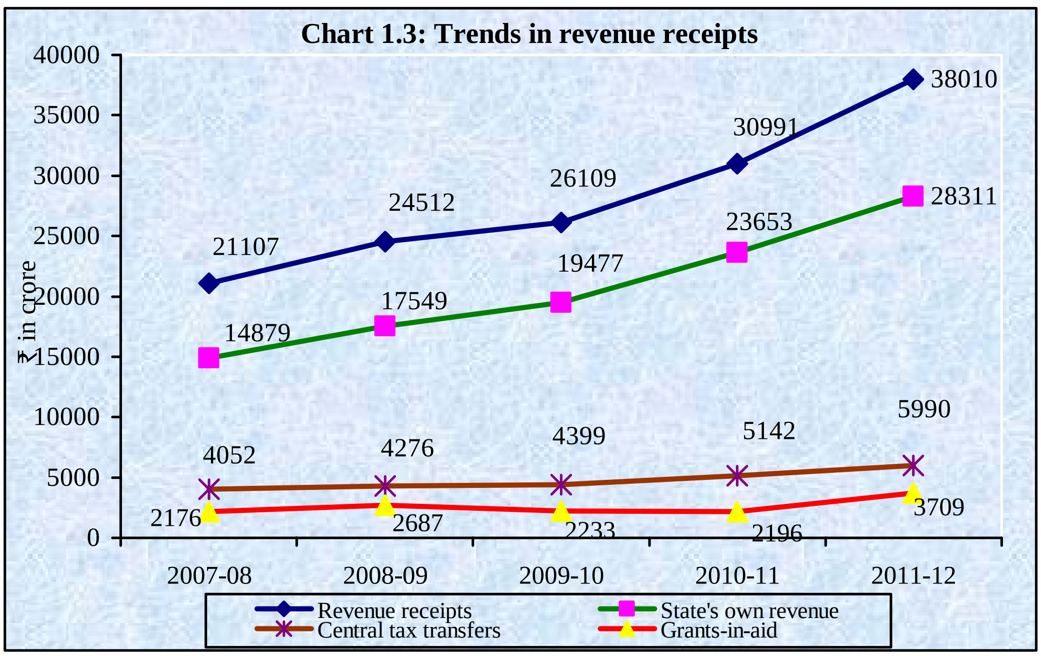
[4] The scheme name 'Swaranjayanti Gram Swarozgar Yojana' was changed to 'Ajeevika'.

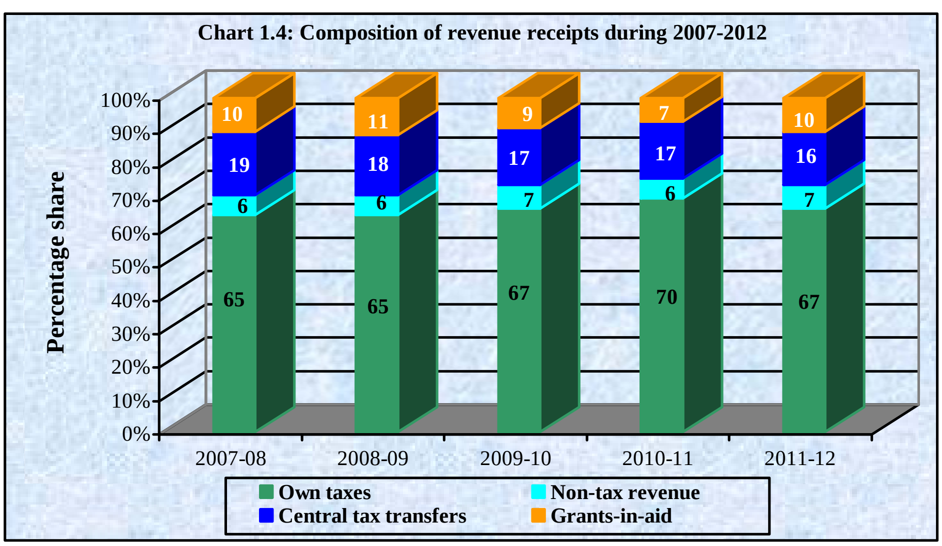
[5] Please see Appendix VII of Finance Accounts – Vol.II for details of 18 individual programme/scheme.

it declined under Sarva Shiksha Abhiyan, Integrated Watershed Management Programme etc. Direct transfer of funds from the GOI to State implementing agencies which increased by 16 *per cent* ran the risk of improper monitoring of utilisation of funds by these agencies. Unless uniform accounting practices are followed by all these agencies, with proper documentation and timely reporting of expenditure, it would be difficult to monitor the end use of these direct transfers.

1.3 Revenue Receipts

Statement-11 of the Finance Accounts details the revenue receipts of the Government. The revenue receipts consist of the State's own tax and non-tax revenues, Central tax transfers and grants-in-aid from GOI. The trend and composition of revenue receipts over the period 2007-12 are presented in **Appendix 1.5** and also depicted in **Charts 1.3** and **1.4** respectively.





The Revenue receipts of the State increased by 80 *per cent* during the period from 2007-08 to 2011-12. During the same period, the State's own revenue increased by 90 *per cent* and the grants-in-aid from GOI increased by 70 *per cent*. The share of the State's own revenue (tax revenue and non-tax revenue) in the total revenue though increased by two percentage points during 2007-12, its share declined by three percentage points during the year 2011-12. The share of central tax transfers also declined by three percentage points during 2007-12.

During 2002-03 to 2010-11, the compound growth rate of revenue receipts (14.31 *per cent*) was lesser than the growth rate of other General Category States (16.86 *per cent*). This growth rate for the period 2002-03 to 2011-12 increased to 15.20 *per cent* (**Appendix 1.1**).

Revenue collected (₹ 38,010 crore) during 2011-12 was lower than the projection made (₹ 39,428 crore) in the Medium Term Fiscal Plan by ₹ 1,418 crore.

The trends in revenue receipts relative to GSDP are presented in **Table 1.3.**

Table 1.3: Trends in revenue receipts relative to GSDP

	2007-08	2008-09	2009-10	2010-11	2011-12
Revenue receipts (RR) (₹ in crore)	**21,107**	**24,512**	**26,109**	**30,991**	**38,010**
State's own taxes (₹ in crore)	13,669	15,990	17,625	21,722	25,719
Rates of growth					
Revenue receipts (*per cent*)	16.1	16.1	6.5	18.7	22.6
State's own taxes (*per cent*)	14.5	17.0	10.2	23.2	18.4
RR/GSDP (*per cent)*	12.1	12.1	11.2	11.2	11.6
Buoyancy Ratios[6]					
Revenue Buoyancy w.r.t GSDP	1.2	1.0	0.4	1.0	1.3
State's own tax Buoyancy w.r.t GSDP	1.0	1.1	0.7	1.2	1.0

Source: Finance Accounts and information furnished by the Economics and Statistics department

- In 2007-08 and 2008-09, the growth rate of revenue receipts was 16.1 *per cent* each year. However, the growth rate declined to 6.5 *per cent* during 2009-10. Thereafter, the growth rate increased to 18.7 *per cent* in 2010-11 and 22.6 *per cent* in 2011-12. Increase in growth rate of revenue receipts was mainly due to increase of State's own tax revenue in respective years.
- Revenue buoyancy with reference to GSDP showed a declining trend from 2007-08 to 2009-10. However, it increased to 1.0 in 2010-11 and 1.3 in 2011-12 due to increased growth rate of revenue receipts in last two years.
- The State's own tax buoyancy with reference to GSDP was fluctuating during the last five years due to ups and downs in growth rate of State's own tax revenue. Buoyancy decreased from 1.2 in 2010-11 to 1.0 in

[6] Buoyancy ratios indicate the elasticity or degree of responsiveness of fiscal variables with respect to a given change in the base variable. For instance, for 2011-12, revenue buoyancy at 1.3 implies that revenue receipts tend to increase by 1.3 percentage points, if the GSDP increases by one *per cent*.

2011-12 due to fall in growth rate of State's own tax revenue from 23.2 *per cent* in 2010-11 to 18.4 *per cent* in 2011-12.

Grants-in-aid from the Government of India

Grants-in-aid from the Government of India increased by ₹ 1,512.60 crore (68.9 *per cent*) from ₹ 2,196.62 crore in 2010-11 to ₹ 3,709.22 crore in 2011-12. The increase was under 'Non-Plan Grants' (₹ 943.32 crore) and under 'Grants for Central Plan Schemes and Centrally Sponsored Plan Schemes' (₹ 599.16 crore) and this was partly offset by decrease under 'Grants for State Plan Schemes' (₹ 29.88 crore).

Central tax transfers

Central tax transfers increased by ₹ 848.51 crore (16.5 *per cent*), from ₹ 5,141.85 crore in 2010-11 to ₹ 5,990.36 crore in 2011-12. The increase was mainly under 'Corporation tax' (₹ 348.09 crore), 'Service tax' (₹ 202.29 crore), 'Customs' (₹ 139.51 crore) and 'Taxes on income other than corporation tax' (₹ 135.64 crore).

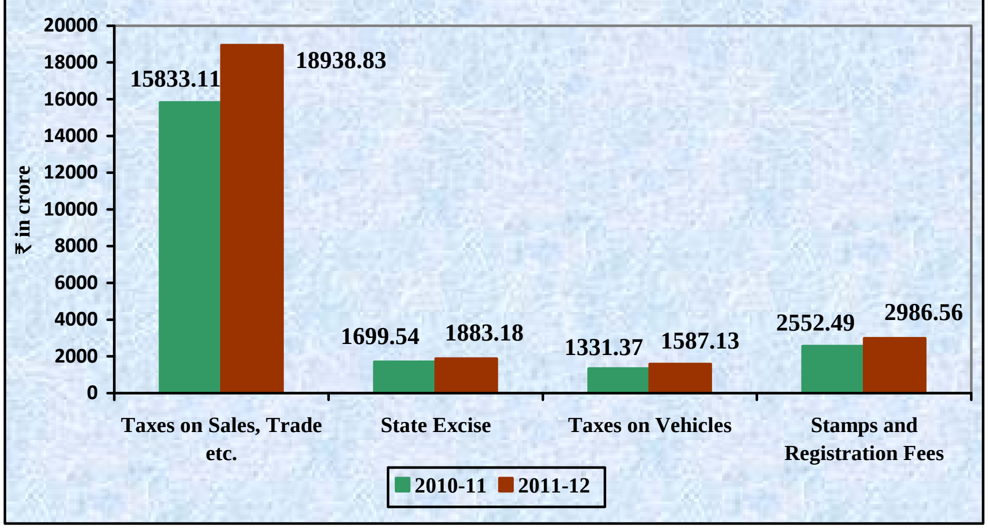
1.3.1 State's own resources

The State's share in Central taxes and grants-in-aid are determined on the basis of recommendations of the Finance Commission, collection of Central tax receipts, Central assistance for Plan schemes, etc. The State's performance in mobilisation of additional resources should be assessed in terms of its own resources comprising revenue from its own tax and non-tax sources.

1.3.1.1 Own Tax Revenue

The State's own tax revenue increased by 18.4 *per cent* from ₹ 21,722 crore to ₹ 25,719 crore during the current year. Component-wise increase is indicated in **Chart 1.5.**

Chart 1.5: Major components of tax revenue during 2010-11 and 2011-12



'Taxes on Sales, Trade etc.', was the major source of the State's own tax revenue during the year (74 *per cent)* followed by 'Stamps and Registration Fees'(12 *per cent*), 'State Excise' (seven *per cent*) and 'Taxes on Vehicles' (six *per cent*).

'Taxes on Sales, Trade etc.', increased by 19.6 *per cent* (₹ 3,105.72 crore) during 2011-12 over the previous year. This increase was mainly due to increase in receipts under 'Value Added Tax' (₹ 1,706.58 crore), 'Receipts under State Sales Tax Act' (₹ 1,352.32 crore) and 'Other Receipts' (₹ 64.59 crore). This was partly offset by decrease in receipts under 'Receipts under Central Sales Tax Act' (₹ 17.77 crore).

'Stamps and Registration Fees' increased by 17.01 *per cent* (₹ 434.07 crore) during 2011-12 over the previous year due to increase of receipts under 'Sale of Non-Judicial Stamps' (₹ 227.19 crore), 'Fees for registering documents' (₹ 154.33 crore) and 'Duty on Impressing of Documents' (₹ 43.77 crore).

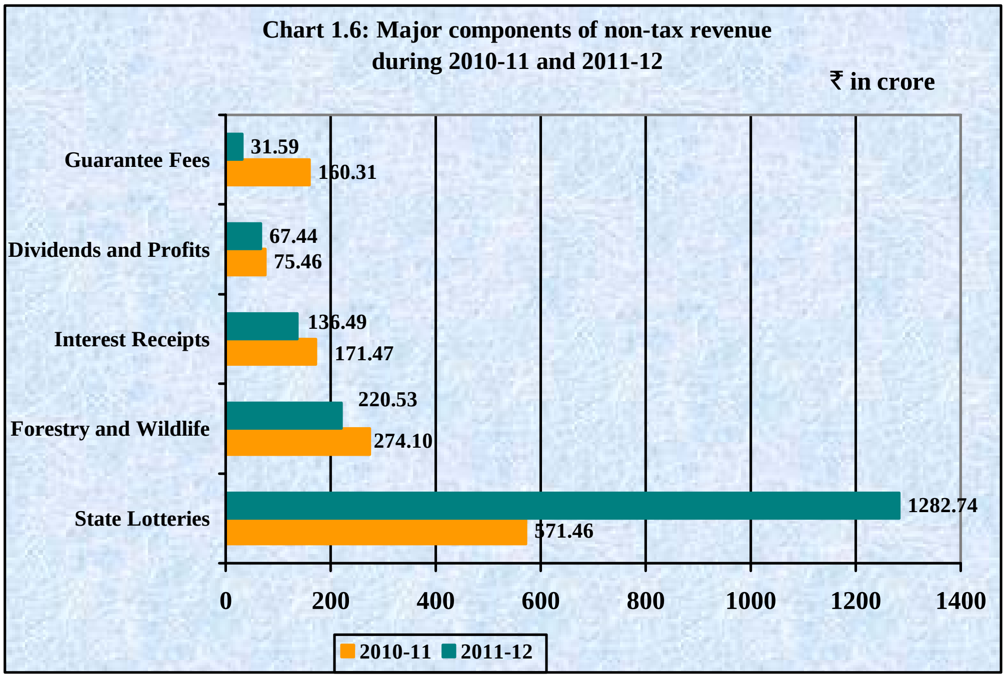
Receipts under 'State Excise' increased by 10.81 *per cent* (₹ 183.64 crore) during 2011-12 over the previous year. The increase was mainly under 'Malt Liquor' (₹ 113.16 crore), 'Country Fermented Liquors' (₹ 106.64 crore), and 'Other Receipts' (₹ 5.53 crore). This was partly offset by decrease in receipts under 'Foreign Liquors and Spirits' (₹ 41.36 crore).

Receipts under 'Taxes on Vehicles' increased by 19.21 *per cent* (₹ 255.77 crore) due to increased receipts mainly under 'Receipts under the State Motor Vehicles Taxation Act' (₹ 234.92 crore) and 'Receipts under Indian Motor Vehicles Act' (₹ 21.13 crore).

The total of tax revenues collected during 2011-12 (₹ 25,718.60 crore) was 3.9 *per cent* more than the normative assessment made by the ThFC (₹ 24,765.06 crore) for the year but it was 3.5 *per cent* less than the projections made in the Medium Term Fiscal Plan (₹ 26,642 crore) of the Government.

1.3.1.2 Non-Tax Revenue

Non-tax revenue, which includes debt relief of ₹47.69 crore given by the GOI during 2011-12 on the recommendations of ThFC, increased by ₹ 661.39 crore (34.25 *per cent*) during the current year (₹ 2,592.18 crore) over the previous year (₹ 1,930.79 crore). Component-wise details are shown in **Chart 1.6.**



Non-tax revenue sources mainly comprised receipts from 'State Lotteries' (49.5 *per cent*), 'Forestry and Wildlife' (8.5 *per cent*) and 'Interest Receipts' (5.3 *per cent*). During 2011-12 substantial increase in revenue was recorded under 'State Lotteries' (₹ 711.28 crore) but this was partly offset by decrease under 'Guarantee Fees' (₹ 128.72 crore), 'Forestry and Wildlife' (₹ 53.57 crore), 'Interest Receipts' (₹ 34.98 crore) and 'Dividends and Profits' (₹ 8.02 crore). Though the receipts under 'State Lotteries' (₹ 1,282.74 crore) recorded an increase of 124 *per cent* over the previous year, with an equally high expenditure (₹ 901.73 crore) during the current year the net yield from lotteries was only ₹ 381.01 crore, which was higher at ₹ 269.79 crore than the net yield of ₹ 111.22 crore of the previous year. Non-tax revenue realised during 2011-12 under various components *vis-à-vis* the budget estimates of 2011-12 was as in **Table 1.4.**

Table 1.4: Non-tax revenue realised *vis-à-vis* Budget estimates

(₹in crore)

Sl. No.	Component of non-tax revenue	Budget estimates 2011-12	Actuals
1.	Forestry and Wildlife	330.12	220.53
2.	Interest receipts	192.43	136.49
3.	Dividends and profits	52.38	67.44
4.	State Lotteries	710.96	1282.74
Total		1285.89	1707.20

Source: Finance Accounts and Annual Financial Statement 2011-12 of the State Government

Though, the actual realization of non-tax revenue fell short of estimated projections under 'Forestry and Wildlife' and 'Interest receipts', the collection exceeded the estimates under the heads 'State Lotteries' and 'Dividends and profits'. The additional revenue generation of ₹ 421.31 crore under the four revenue heads as mentioned in table 1.4 leaves much to be desired about the accuracy of the budget projections.

Expenditure on tax collection

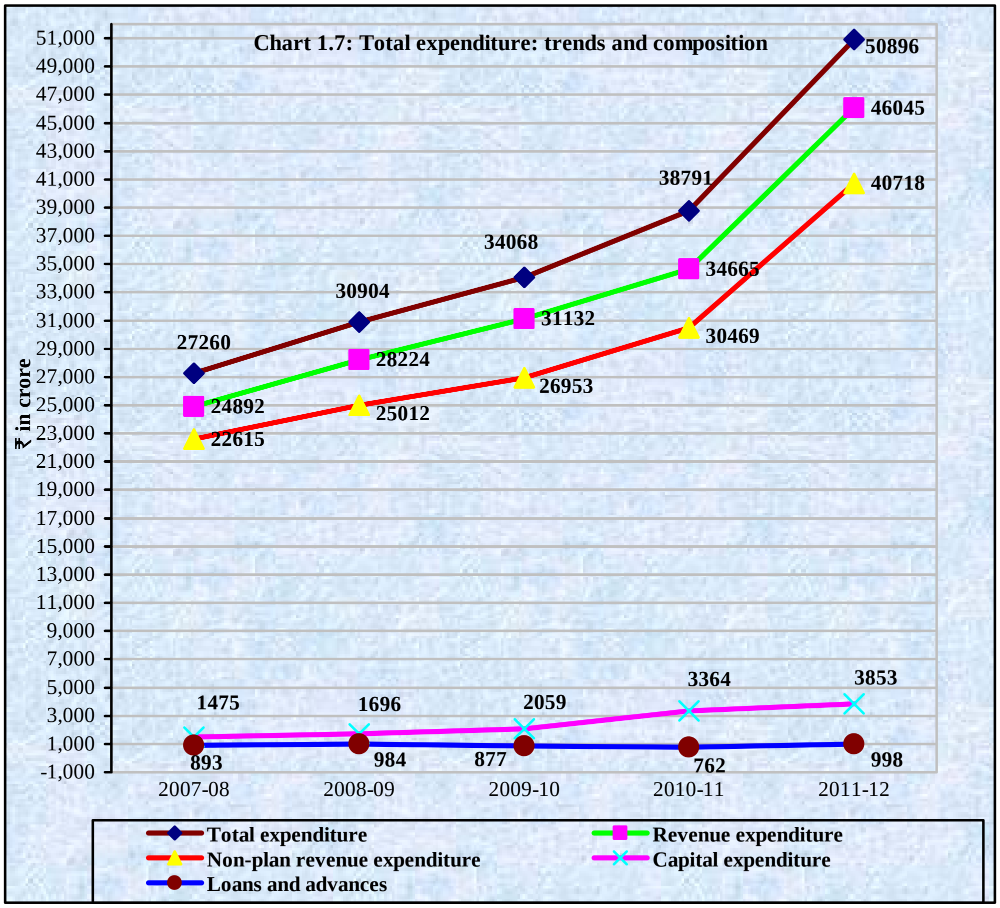
The expenditure on collection in respect of Stamps and Registration fees and State Excise was higher as compared to All India average during the period 2007-08 to 2010-11. However, it was lower than the All India average in respect of Taxes on Sales, Trade etc. (2010-11) and Taxes on vehicles (2009-10 and 2010-11). Details are given in **Appendix 1.6**. It would be prudent to improve the tax administration in order to increase the revenue and thereby reduce the cost of collection.

1.4 Application of Resources

Analysis of the allocation of expenditure at the State Government level assumes significance since responsibilities for major expenditure are entrusted with them. Within the framework of fiscal responsibility legislations, there are budgetary constraints in raising public expenditure financed by deficit or borrowings. It is, therefore, important to ensure that the ongoing fiscal correction and consolidation process at the State level is not at the cost of expenditure, especially expenditure directed towards development and social sectors.

1.4.1 Growth and composition of expenditure

The total expenditure of the State Government consists of revenue expenditure as well as capital expenditure which include expenditure on loans and advances. The trends in various components of total expenditure-Plan and Non-Plan revenue expenditure, committed expenditure such as salaries and wages, interest payments, pension payments and subsidies, financial assistance to local bodies, etc., are discussed in the succeeding paragraphs. **Chart 1.7** presents the trends in total expenditure of the State Government over a period of five years (2007-12). Its composition, both in terms of 'economic classification' and 'expenditure by activities' is depicted respectively in **Charts 1.8 and 1.9.**



The total expenditure increased by 31.2 *per cent* in 2011-12 to ₹ 50,896 crore from ₹ 38,791 crore in the previous year. The total expenditure, its annual growth rate, the ratio of expenditure to the State GSDP and to revenue receipts and its buoyancy with respect to GSDP and revenue receipts are indicated in **Table 1.5**. During 2002-03 to 2010-11, the compound growth rate of total expenditure (11.97 *per* cent) was less than the growth rate of other General Category States (14.58 *per* cent). The growth rate for the period 2002-03 to 2011-12 further increased to 13.96 *per* cent **(Appendix 1.1)**.

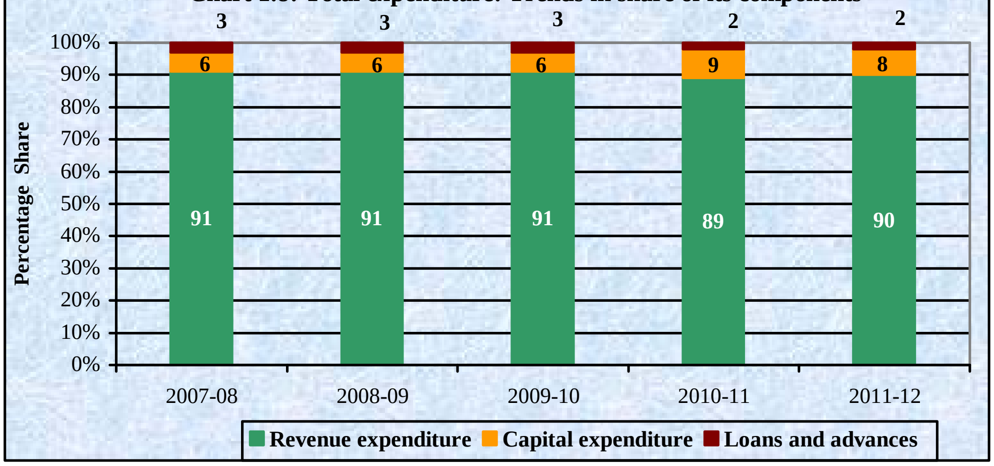
Table 1.5: Total expenditure – basic parameters

	2007-08	2008-09	2009-10	2010-11	2011-12
Total expenditure (TE) (₹ in crore)	27260	30904	34068	38791	50896
Rate of growth *(per cent)*	23.5	13.4	10.2	13.9	31.2
TE/GSDP ratio *(per cent)*	15.6	15.2	14.7	14.0	15.6
RR /TE ratio *(per cent)*	77.4	79.3	76.6	79.9	74.7
Buoyancy of Total expenditure with reference to:					
GSDP (ratio) (*)	1.7	0.8	0.7	0.7	1.7
RR (ratio)	1.5	0.8	1.6	0.7	1.4

(*) change in figures is due to adoption of new series of GSDP figures

The increase of ₹ 12,105 crore (31.2 *per cent*) in total expenditure in 2011-12 over the previous year was mainly on account of increase of ₹ 11,380 crore in revenue expenditure, ₹ 489 crore in capital expenditure and ₹ 236 crore in disbursement of loans and advances.

Chart 1.8: Total expenditure: Trends in share of its components



During the five-year period 2007-12, the share of revenue expenditure ranged between 89 to 91 *per cent* of the total expenditure whereas the share of capital expenditure ranged between six and nine *per cent* of the total expenditure during the same period. The revenue expenditure increased in absolute terms from ₹ 24,892 crore in 2007-08 to ₹ 46,045 crore in 2011-12 but its percentage to total expenditure remained almost static during the last five year period. Capital expenditure increased from ₹ 1,475 crore in 2007-08 to ₹ 3,853 crore in 2011-12 and its percentage to total expenditure increased from six *per cent* to nine *per cent* in 2010-11. However, it decreased to eight *per cent* in 2011-12.

Revenue expenditure increased by 32.8 *per cent* (₹ 11,380 crore) during 2011-12 when compared to previous year. The increase in revenue expenditure during 2011-12 was mainly due to increase in expenditure under the major heads 'Pension and Other Retirement Benefits' (₹ 2,933 crore), 'General Education' (₹ 2,433 crore), 'Medical and Public Health' (₹ 725 crore), 'Compensation and Assignments to Local Bodies and Panchayati Raj Institutions' (₹ 611 crore), 'Interest Payments' (₹ 604 crore), 'Police' (₹ 584 crore), 'Roads and Bridges' (₹ 494 crore), 'Social Security and Welfare' (₹ 449 crore), 'Food, Storage and Warehousing (₹ 395 crore), 'Miscellaneous General Services' (₹ 379 crore), Crop Husbandry (₹ 337 crore), 'Welfare of Scheduled Castes, Scheduled Tribes and other Backward classes' (₹ 307 crore) etc.

Capital expenditure increased by 14.5 *per cent* (₹ 489 crore) during 2011-12 when compared to previous year. This increase was mainly under the heads 'Roads and Bridges' (₹ 253 crore), 'Tourism' (₹ 88 crore), 'Public works' (₹ 52 crore) etc.

As per table 1.5, the buoyancy of total expenditure with reference to GSDP was more than one in 2007-08 and this ratio declined to less than one during the period 2008-09 to 2010-11 due to decrease in the rate of growth of total expenditure as compared to the rate of growth of GSDP. However, the rate of growth of total expenditure increased and buoyancy stood at 1.7 during 2011-12. The sharp increase in buoyancy (from 0.7 to 1.7) during the 2011-12 indicates that the rate of growth of total expenditure was higher than that of GSDP growth.

Trends in total expenditure in terms of activities

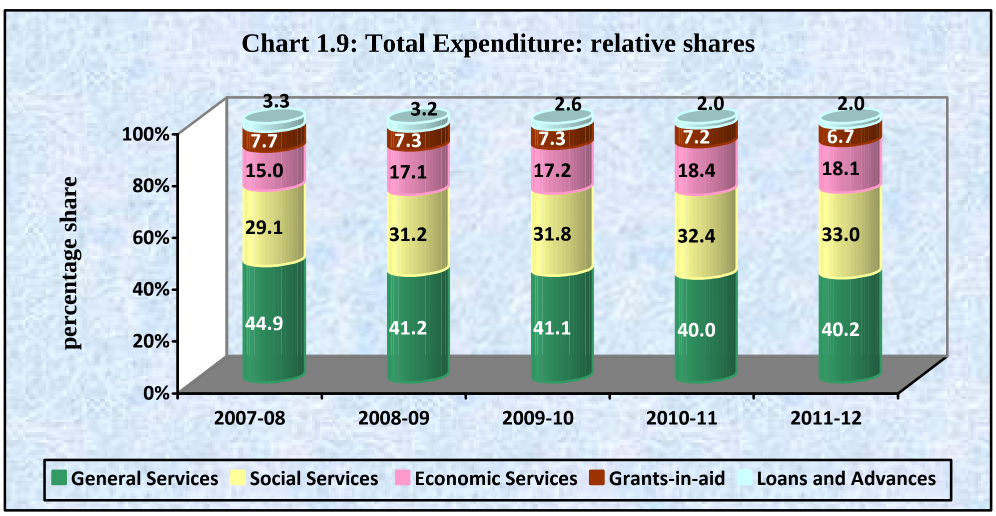
In terms of the activities, total expenditure could be considered as being composed of expenditure on General Services including interest payments, Social and Economic Services, grants-in-aid and loans and advances. Relative shares of these components in the total expenditure are indicated in **Table 1.6**.

Table-1.6: Components of expenditure – relative shares

(in *per cent*)

	2007-08	2008-09	2009-10	2010-11	2011-12
General Services	**44.9**	**41.2**	**41.1**	**40.0**	**40.2**
of which, Interest Payments	15.9	15.1	15.5	14.7	12.4
Social Services	**29.1**	**31.2**	**31.8**	**32.4**	**33.0**
Economic Services	**15.0**	**17.1**	**17.2**	**18.4**	**18.1**
Grants-in-aid	**7.7**	**7.3**	**7.3**	**7.2**	**6.7**
Loans and Advances	**3.3**	**3.2**	**2.6**	**2.0**	**2.0**

The movement of the relative shares of the above components of expenditure indicated that the shares of General Services and Social Services in the total expenditure marginally increased during 2011-12 over the previous year. These increases were partially set off by the decreases in Economic Services and Grants-in-aid.



The share of Social Services in total expenditure during 2011-12 increased mainly on account of increase in expenditure under 'Education, Sports, Art and Culture' (₹ 2,571 crore), 'Health and Family Welfare' (₹ 834 crore), 'Social Welfare and Nutrition' (₹ 421 crore) and Welfare of Scheduled Castes, Scheduled Tribes and Other Backward Classes (₹ 284 crore) whereas the share of General Services increased mainly due to increase in expenditure under 'Pension and

Miscellaneous Services' (₹ 3,312 crore) and 'Interest payments and Servicing of Debt' (₹ 339 crore).

Incidence of revenue expenditure

Revenue expenditure is incurred to maintain the current level of services and payment for past obligations and as such, does not result in any addition to the State's infrastructure and service network. Revenue expenditure had the predominant share of around 90 *per cent* in the total expenditure during 2011-12. The overall revenue expenditure, its rate of growth, the ratio of revenue expenditure to GSDP and to revenue receipts and its buoyancy are indicated in **Table 1.7.**

Table 1.7: Revenue expenditure – basic parameters

(₹ in crore)

	2007-08	2008-09	2009-10	2010-11	2011-12
Revenue expenditure (RE), *of which*	**24892**	**28224**	**31132**	**34665**	**46045**
Non-plan revenue expenditure (NPRE)	22615	25012	26953	30469	40718
Plan revenue expenditure (PRE)	2277	3212	4179	4196	5327
Rate of Growth of					
RE (*per cent*)	19.5	13.4	10.3	11.3	32.8
NPRE (*per cent*)	22.1	10.6	7.8	13.0	33.6
PRE (*per cent*)	(-) 1.4	41.1	30.1	0.4	27.0
Revenue expenditure as percentage to TE	91.3	91.3	91.4	89.4	90.5
NPRE/GSDP (*per cent*)	12.9	12.3	11.6	11.0	12.5
NPRE as percentage of TE	83.0	80.9	79.1	78.5	80.0
NPRE as percentage of RR	107.1	102.0	103.2	98.3	107.1
Buoyancy of revenue expenditure with					
GSDP (ratio) (*)	1.4	0.8	0.7	0.6	1.8
Revenue receipts (ratio)	1.2	0.8	1.6	0.6	1.4

Source : Finance Accounts

(*) change in figures is due to adoption of new series of GSDP figures

The revenue expenditure increased during 2011-12 by ₹ 11,380 crore (32.8 *per cent*) over the previous year. This was ₹ 2,282 crore more than the increase in the projections (₹ 9,098 crore) made in the Medium Term Fiscal Plan.

In absolute terms Non-Plan revenue expenditure (NPRE) and Plan revenue expenditure (PRE) showed an increasing trend during the period 2007-12. NPRE showed an increase of 33.6 *per cent* in 2011-12 (₹ 10,249 crore) over 2010-11. The increase in NPRE during the year compared to the previous year was mainly due to increase in expenditure under 'Pension and other retirement benefits' (₹ 2,933 crore), 'General Education' (₹ 2,427 crore), 'Compensation and Assignment to Local Bodies and Panchayati Raj Institutions' (₹ 611 crore), 'Interest Payments' (₹ 604 crore), 'Roads and Bridges' (₹ 584 crore), 'Police' (₹ 571 crore), 'Medical and Public Health' (₹ 554 crore), 'Miscellaneous General Services' (₹ 485 crore) and 'Food, Storage and Warehousing' (₹ 328 crore).

Plan Revenue Expenditure (PRE) also showed an increase of ₹ 1,131 crore in 2011-12 (₹ 5,327 crore) when compared to previous year (₹ 4,196 crore). This increase was mainly under 'Social Security and Welfare' (₹ 370 crore), 'Welfare of Scheduled Castes, Scheduled Tribes and other Backward classes' (₹ 279 crore), 'Medical and Public Health' (₹ 171 crore) and 'Crop Husbandry' (₹ 155 crore).

Actual NPRE during 2011-12 (₹ 40,718 crore) exceeded the normative assessment made by the ThFC (₹ 30,776 crore) by ₹ 9,942 crore (32.30 *per cent*).

1.4.2 Expenditure on salaries, wages, pensions, interests, etc.

The expenditure of the State Government on revenue account mainly consists of interest payments, expenditure on salaries and wages, pensions and subsidies. **Table 1.8** and **Chart 1.10** present the trends in the expenditure on these components during 2007-12.

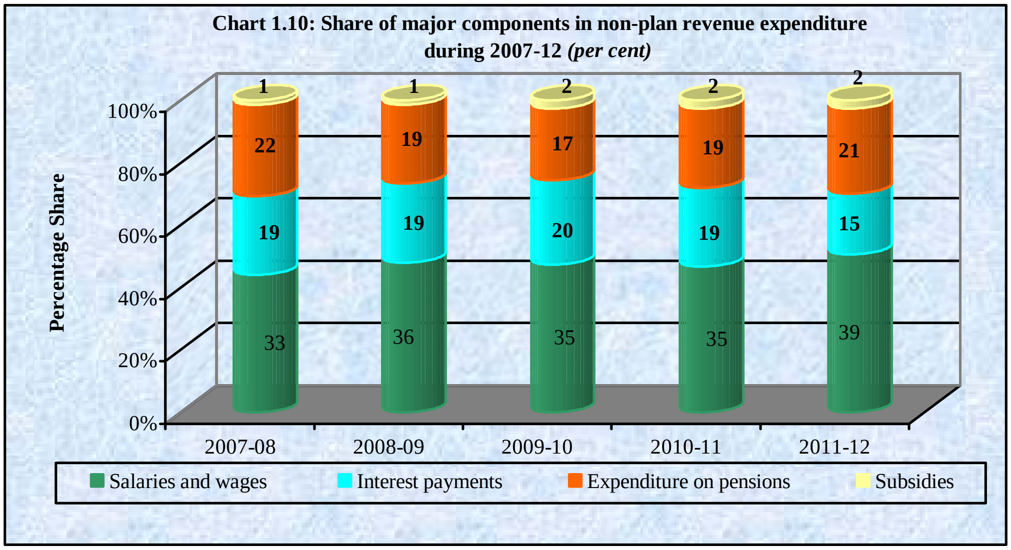
Table 1.8: Major components of revenue expenditure

(₹ in crore)

Components of committed expenditure	2007-08	2008-09	2009-10	2010-11	2011-12	
					Actuals	Percentage to NPRE
Salaries* and Wages, *Of which*	7,757 (36.8)	9,146 (37.3)	9,894 (37.9)	11,178 (36.1)	16,229 (42.7)	39.9
Non-Plan Heads	7,448	8,895	9,529	10,815	15,681	38.5
Plan Heads**	309	251	365	363	548	..
Interest Payments (MH 2049)	4,330 (20.5)	4,660 (19.0)	5,292 (20.3)	5,690 (18.4)	6,294 (16.6)	15.5
Expenditure on Pensions (MH 2071)	4,925 (23.3)	4,686 (19.1)	4,706 (18.0)	5,767 (18.6)	8,700 (22.9)	21.4
Subsidies	202 (1.0)	355 (1.4)	442 (1.7)	627 (2.0)	1,014 (2.7)	2.5
Revenue expenditure	24,892	28,224	31,132	34,665	46,045	..
Revenue receipts	21,107	24,512	26,109	30,991	38,010	..

* Salaries include teaching grant paid to aided educational institutions like schools and colleges to meet the salaries of their teaching and non-teaching staff.
** The Plan heads also include the salaries and wages paid under Centrally Sponsored schemes
NPRE: Non-plan Revenue Expenditure
Figures in the parentheses indicate percentage to revenue receipts

Source: Finance Accounts of the State Government



During 2011-12 expenditure on salaries under Non-Plan and Plan heads increased to ₹ 15,681 crore and ₹ 548 crore respectively from ₹ 10,815 crore and ₹ 363 crore in the previous year. This was 45 *per cent* and 51 *per cent* more than the Non-Plan and Plan expenditure of salaries recorded in the previous year. The increase in salary expenditure was due to payment of arrears of pay as a result of implementation of the recommendations of the Ninth State Pay Revision Commission. The expenditure on salaries was almost in line with the projections made (₹ 16,326 crore) in Medium Term Fiscal Plan for the year 2011-12.

Pension payment also increased to ₹ 8,700 crore in 2011-12 from ₹ 5,767 crore in 2010-11 and recorded an increase of 51 *per cent* over the previous year. Expenditure on pension exceeded the projections made by the State Government in the Medium Term Fiscal Plan (₹ 7,311 crore) by 19 *per cent* and the assessment made by the ThFC (₹ 6,051 crore) by 44 *per cent*.

Interest payments increased by 10.6 *per cent* during 2011-12 (₹ 6,294 crore) when compared to the previous year (₹ 5,690 crore). This was in line with the projections made by the State Government in the Medium Term Fiscal Plan (₹ 6,255 crore) but less than the assessment made by the ThFC (₹ 6,582 crore) by four *per cent*.

During the last five years, payment of subsidies increased steeply from ₹ 202 crore in 2007-08 to ₹ 1,014 crore in 2011-12. Subsidy payment of ₹ 1,014 crore in 2011-12 was 62 *per cent* more than the subsidy in previous year (₹ 627 crore). The huge increase in subsidy in 2011-12 over the previous year was mainly due to increase in the payment of subsidy to the Food Corporation of India (₹ 366 crore) in respect of reimbursement of price difference of ration rice and wheat and for 'Special support scheme for farm sector' (₹ 82 crore).

The expenditure on salaries, interest payments, pensions and subsidies which constituted 70 *per cent* of the revenue expenditure consumed 85 *per cent* of the revenue receipts of the State during the current year. This was ten percentage points more than the previous year. Further, the State Government has been releasing funds to meet the salary and pension liabilities of employees working in Universities and State Autonomous Bodies, salaries/honorarium payments of Local Self Government Institutions (who have no revenue of their own), Pension payments of Municipalities/ Corporations etc. As these payments are considered obligatory in nature, there is very little scope for reduction in this category of payments. Consequently, State Government is left with less than 15 *per cent* of the revenue receipts for meeting other developmental activities.

1.4.2.1 New Pension Scheme

Realising the enormous burden arising due to payment towards pension, Government of India introduced a defined contribution based New Pension Scheme for Government servants recruited after 1 January 2004. Though a number of State Governments have adopted the scheme, Government of Kerala has not yet switched over to the new scheme (September 2012).

As per the new pension scheme, All India Service Officers recruited to Kerala cadre and who have joined service after 1 January 2004 have to make a mandatory contribution at the rate of 10 *per cent* of pay and dearness allowance while the Government will have to make an equal matching contribution. The contributions and investment returns are to be kept in a non-withdrawable Pension Account. Scrutiny of records revealed that in the case of 49[7] All India Service Officers recruited after 1 January 2004 and posted in the State, mandatory contribution was not deducted from the salary of these officials and no provision was made in the State budget for payment of the matching Government's contribution. Though the Government nominated (May 2010) the Additional Secretary (Pension), Finance Department, as State Nodal Officer for implementing the scheme, no progress was achieved in this regard as of August 2012. Approximate contribution in respect of 49 All India Service Officers for the period from 1 January 2004 to 31 March 2012 as assessed by Audit (₹ 64.87 lakh) together with Government contribution comes to ₹ 1.30 crore. The Government's failure in implementing the scheme needs to be addressed to urgently.

1.4.3 Financial assistance given by the State Government to local bodies and other institutions

The quantum of assistance provided by the Government as grants and loans to local bodies, educational institutions, Government companies, Welfare Fund Boards, etc during the current year relative to the previous years is presented in **Table 1.9.**

[7] Indian Administrative Service : 22, Indian Police Service : 18 and Indian Forest Service: 9

Table 1.9: Financial assistance to local bodies, educational institutions,etc.

(₹ in crore)

Financial Assistance to Institutions	2007-08	2008-09	2009-10	2010-11	2011-12
Educational Institutions (Aided Schools, Aided Colleges, Universities, etc.)	2812.88	3306.81	3546.61	4087.83	5605.77
Municipal Corporations and Municipalities	485.85	966.99	834.46	901.87	1073.78
Zilla Parishads and Other Panchayati Raj Institutions	2421.93	2600.11	2996.66	3411.65	4203.98
Development Agencies	1.36	1.95	2.04	5.25	5.50
Hospitals and Other Charitable Institutions	53.98	56.66	76.40	139.02	144.46
Other Institutions[8]	468.50	658.83	1159.47	1252.58	1065.96
Total	**6244.50**	**7591.35**	**8615.64**	**9798.20**	**12099.45**
Assistance as percentage of revenue expenditure	25	27	28	28	26

Source: Finance Accounts and information received from the State Government

The financial assistance to local bodies and other institutions increased from ₹ 6,244.50 crore in 2007-08 to ₹ 12,099.45 crore in 2011-12. As a percentage of revenue expenditure, it ranged between 25 to 28 *per cent* during the period 2007-12. The financial assistance to Zilla Parishads, Municipalities, Corporations, etc., increased (₹ 964.24 crore) to ₹ 5,277.76 crore in 2011-12 from ₹ 4,313.52 crore in 2010-11 which was mainly due to more devolution of funds to local bodies towards maintenance of assets, expansion and development and traditional functions.

1.5 Quality of Expenditure

The availability of better social and physical infrastructure in the State generally reflects the quality of its expenditure. Improvement in the quality of expenditure basically involves three aspects, viz., adequacy of public expenditure (i.e. adequate provisions for providing public services); efficiency of expenditure use and its effectiveness (assessment of outlay-outcome relationships for select services).

1.5.1 Adequacy of public expenditure

The responsibilities relating to expenditure on the social sector and the economic infrastructure assigned to the State Governments are largely State subjects. Enhancing human development levels requires the States to step up their expenditure on key social services like education, health, etc. Low fiscal priority (ratio of expenditure under a category to aggregate expenditure) is attached to a particular sector, if it is below the respective national average. **Table 1.10** analyses the fiscal priority of the State Government with regard to development

[8] Other institutions, *inter alia*, include Kerala Water Authority (₹ 240.12 crore), Kerala State Road Transport Corporation (₹ 140 crore), INFOPARK (₹ 83.50 crore), State Council for Science, Technology & Environment (₹ 69.56 crore), Kerala Industrial Infrastructure Development Corporation (₹ 39.79 crore), Kerala Khadi and Village Industries Board (₹ 26.50 crore), Kerala State Information Technology Mission (₹ 20.35 crore), State Horticulture Mission (₹ 17.73 crore), etc.

expenditure, social expenditure and capital expenditure during 2008-09 and 2011-12.

Table 1.10: Fiscal priority of the State in 2008-09 and 2011-12

(in per cent)

Fiscal Priority by the State*	AE/GSDP	DE#/AE	SSE/AE	CE/AE	Education/ AE	Health/AE
General Category States' Average (Ratio) 2008-09	17.00	67.09	34.28	16.47	15.41	3.97
Kerala's Average (Ratio) 2008-09	15.24	51.49	33.32	5.49	17.58	5.09
General Category States' Average (Ratio) 2011-12	16.09	66.44	36.57	13.25	17.18	4.30
Kerala's Average (Ratio) 2011-12	15.58	52.85	34.06	7.57	18.67	5.69

* As *per cent* to GSDP
AE: Aggregate (Total) Expenditure DE: Development Expenditure
SSE: Social Sector Expenditure CE: Capital Expenditure.
\# Development expenditure includes Development Revenue Expenditure, Development Capital expenditure and Loans and Advances disbursed (Social and Economic sector).
General category States exclude Delhi, Goa and Puducherry.

- In 2008-09 and 2011-12, the State Government spent relatively less as a proportion of its GSDP compared to the General Category States' average.

- In 2008-09 and 2011-12, development expenditure as a proportion of aggregate expenditure has also been lower than the General Category States' average. Developmental expenditure consists of both economic sector expenditure and social sector expenditure.

- Adequate priority has not been given to Social sector during 2008-09 and 2011-12. As far as health sector and education sector's fiscal priority is concerned, the State has given adequate priority to these sectors.

- The proportion of capital expenditure has been much lower as compared to General Category States during 2008-09 and 2011-12. However, it is observed that the State has shown some improvement in 2011-12 as compared to 2008-09 by increasing expenditure on capital but it is still lower than General Category States' average.

- The Government may consider enhancing the proportion of expenditure on economic and capital sectors in order to create the much needed assets to stimulate growth and give priority to physical capital formation that will further increase the growth prospects of the State by creating durable assets.

1.5.2 Efficiency of expenditure use

In view of the importance of public expenditure on development heads from the point of view of social and economic development, it is important for the State

Government to take appropriate expenditure rationalisation measures and lay emphasis on provision of core public and merit goods[9]. Apart from improving the allocation towards development expenditure[10], particularly in view of the fiscal space being created on account of decline in expenditure on debt servicing in recent years, the efficiency of expenditure use is also reflected by the ratio of capital expenditure to total expenditure (and/or GSDP) and the proportion of revenue expenditure being spent on operation and maintenance of the existing social and economic services. The higher the ratio of these components to total expenditure (and/or GSDP), the better would be the quality of expenditure. Development expenditure comprised revenue and capital expenditure including loans and advances in socio-economic services. **Table 1.11** presents the trends in development expenditure relative to the aggregate expenditure of the State during the period 2007-08 to 2011-12. **Chart 1.11** presents component-wise development expenditure during 2007-12. **Table 1.12** provides the details of capital expenditure and the components of revenue expenditure incurred on the maintenance of the selected social and economic services.

Table 1.11: Development expenditure

(₹ in crore)

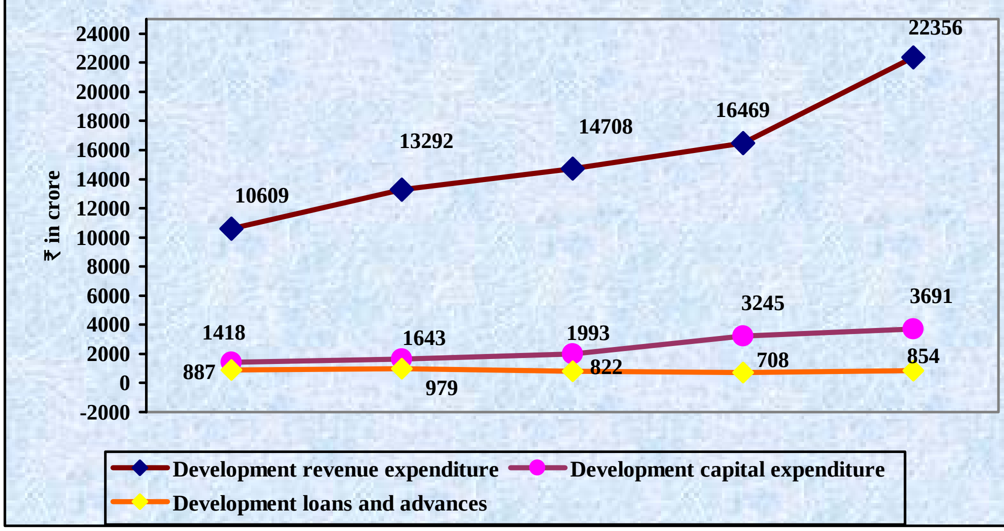
Components of Development Expenditure	2007-08	2008-09	2009-10	2010-11	2011-12	
					BE	Actuals
Development Expenditure (a to c)						
a. Development revenue expenditure	10609 (38.9)	13292 (43.0)	14,708 (43.2)	16,469 (42.5)	22,956	22,356 (43.9)
b. Development capital expenditure	1418 (5.2)	1643 (5.3)	1,993 (5.9)	3245 (8.4)	3,581	3,691 (7.3)
c. Development loans and advances	887 (3.3)	979 (3.2)	822 (2.4)	708 (1.8)	1,122	854 (1.7)
Figures in parentheses indicate percentage to aggregate expenditure						

Source: Finance Accounts and Annual Financial Statement of the State Government for 2011-12

[9] *Core public goods* are goods which all citizens enjoy in common in the sense that each individual's consumption of such goods leads to no subtractions from any other individual's consumption of that good, e.g. enforcement of law and order, security and protection of our rights; pollution free air and other environmental goods and road infrastructure etc. *Merit goods* are commodities that the public sector provides free or at subsidized rates because an individual or society should have them on the basis of some concept of need, rather than ability and willingness to pay the Government and therefore, wishes to encourage their consumption. Examples of such goods include the provision of free or subsidized food for the poor to support nutrition, delivery of health services to improve quality of life and reduce morbidity, providing basic education to all, drinking water and sanitation etc.

[10] The analysis of expenditure data is disaggregated into development and non-development expenditure. All expenditure relating to Revenue Account, Capital Outlay and Loans and Advances is categorized into Social Services, Economic Services and General Services. Broadly, the social and economic services constitute development expenditure, while expenditure on general services is treated as non-development expenditure.

Chart 1.11: Components of development expenditure



Development expenditure increased by 108 *per cent* (₹ 13,987 crore) from ₹ 12,914 crore in 2007-08 to ₹ 26,901 crore in 2011-12. Development revenue expenditure constituted 83 *per cent* of development expenditure whereas the share of development capital expenditure, including loans and advances was only 17 *per cent*.

Development revenue expenditure increased by 35.7 *per cent* (₹ 5,887 crore) from ₹ 16,469 crore in 2010-11 to ₹ 22,356 crore in 2011-12. The increase was mainly due to increase in expenditure under the accounts heads; 'General Education' (₹ 2,433 crore), 'Medical and Public Health' (₹ 725 crore), 'Roads and Bridges' (₹ 494 crore), 'Social Security and Welfare' (₹ 449 crore), 'Food, Storage and Warehousing' (₹ 395 crore), 'Crop Husbandry' (₹ 337 crore) and 'Welfare of Scheduled Castes, Scheduled Tribes and Other Backward Classes' (₹ 307 crore).

Development capital expenditure increased by 13.7 *per cent* (₹ 446 crore) from ₹ 3,245 crore in 2010-11 to ₹ 3,691 crore in 2011-12. The increase was mainly due to increase in expenditure under the accounts heads; 'Roads and Bridges' (₹ 253 crore), and 'Other Social Services' (₹ 144 crore).

Table 1.12: Efficiency of expenditure in selected Social and Economic Services

(in per cent)

Social/Economic Infrastructure	2010-11			2011-12		
	Ratio of CE to STE	In RE, the share of		Ratio of CE to STE	In RE, the share of	
		S&W	O&M		S&W	O&M
Social Services (SS)						
General Education	0.7	86.1	0.1	0.2	89.2	(*)
Health and Family Welfare	4.8	75.8	0.7	4.1	73.9	0.1
Water Supply, Sanitation, Housing and Urban Development	16.6	3.4	2.6	13.4	5.9	2.3
Total (SS)	3.8	62.8	1.0	3.4	67.0	0.7

Social/Economic Infrastructure	**2010-11**			**2011-12**		
	Ratio of CE to STE	**In RE, the share of**		**Ratio of CE to STE**	**In RE, the share of**	
		S&W	**O&M**		**S&W**	**O&M**
Economic Services (ES)						
Agriculture and Allied Activities	13.7	29.4	0.7	9.5	28.4	0.1
Irrigation and Flood Control	47.2	49.4	46.8	40.6	66.1	32.7
Power and Energy	--	0.1		0.1	0.3	
Transport	64.6	19.9	37.5	58.3	16.2	39.5
Total (ES)	36.0	28.1	10.2	32.4	29.5	10.6
Total (SS+ES)	15.9	53.6	3.4	13.7	56.7	3.4
STE : Sectoral total Expenditure under Capital and Revenue heads; CE: Capital Expenditure; RE: Revenue Expenditure; S&W :Salaries and Wages; O&M: Operations and Maintenance.						

(*) insignificant

Source: Finance Accounts and information furnished by Accountant General (A&E)

The ratio of capital expenditure to total expenditure under Social Services decreased from 3.8 *per cent* in the previous year to 3.4 *per cent* in the year 2011-12. It shows that capital expenditure under Social Services was not commensurate with the increase recorded in revenue expenditure. The ratio of capital expenditure to total expenditure under all the sub-sectors in Social Services was less than the previous year.

The percentage of capital expenditure to total expenditure under Economic Services also decreased from 36 *per cent* in 2010-11 to 32.4 *per cent* in 2011-12. Though the capital expenditure under Economic Services recorded an increase of ₹ 330 crore, it was not commensurate with the increase recorded in the total Economic Sector Expenditure.

The share of salaries and wages in revenue expenditure under Social Services increased from 62.8 *per cent* in 2010-11 to 67 *per cent* in 2011-12. Similarly the expenditure increase under Economic services was from 28.1 *per cent* in 2010-11 to 29.5 *per cent* in 2011-12.

1.6 Financial Analysis of Government Expenditure and Investments

In the post-FRBM framework, the State is expected to keep its fiscal deficit (and borrowings) not only at low levels but also meet its capital expenditure/ investment (including loans and advances) requirements from its own sources of revenue. In addition, in a transition to complete dependence on market-based resources, the State Government is required to initiate measures to earn adequate returns on its investments and recover its cost of borrowed funds rather than bearing the same on its budget in the form of implicit subsidies. The State is also required to take requisite steps to infuse transparency in financial operations. This section presents the broad financial analysis of investments and other capital expenditure undertaken by the Government during the current year *vis-à-vis* previous years.

1.6.1 Financial results of irrigation works

In the case of eight irrigation projects, which have been declared commercial, with a cumulative capital outlay of ₹ 132.22 crore as on 31 March 2012, the revenue realised from them during 2011-12 was ₹ 1.86 crore which was only 1.4 *per cent* of the total outlay. After considering the working and maintenance expenses of ₹ 30.99 crore and interest charges of ₹ 11.76 crore, these projects suffered a net loss of ₹ 40.89 crore (as detailed in Appendix IX to Finance Accounts).

1.6.2 Incomplete projects/works

Department-wise information pertaining to incomplete projects/works (each costing above ₹ one crore) as on 31 March 2012 is given in **Table 1.13**.

Table 1.13: Status of incomplete projects in the State

(₹ in crore)

Sl. No	Name of the department/project	No. of incomplete projects/ works	Initial budgeted cost	Cumulative actual expenditure as on 31 March 2012
1.	Water Resources Department – (Irrigation project)	11	31.94	29.59
2.	Water Resources Department – (Irrigation and Minor Irrigation Works)	34	63.00	31.58
3.	Public Works Department – (Roads and Bridges)	148	428.54	255.25
4.	Public Works Department – (Buildings)	62	195.56	130.84
5.	Harbour Engineering Department	4	62.28	44.72
	Total	**259**[11]	**781.32**	**491.98**

Source: Appendix X of Finance Accounts 2011-12

According to information included in the Finance Accounts, 259 projects/works on which an expenditure of ₹ 491.98 crore was incurred up to March 2012 were not completed at the end of March 2012 though the stipulated period of completion was over. Delay in completion of projects/works may result in cost overrun.

1.6.3 Investment and returns

As of 31 March 2012, the State Government had invested ₹ 4,206.43 crore in Statutory Corporations, Government Companies, Joint Stock Companies and Co-operatives **(Table 1.14)**. The average return on these investments was 1.3 *per cent* in the last five years, while the Government paid an average interest rate ranging from 7.2 *per cent* to 7.9 *per cent* on its borrowings during 2007-2012.

[11] Includes projects commenced upto 2011

Table 1.14: Return on investments

Investment/Return/Cost of Borrowings	2007-08	2008-09	2009-10	2010-11	2011-12
Investment at the end of the year (₹ in crore)	2483.99	3153.10	3328.25	3807.52	4206.43
Return (₹ in crore)	28.63	33.53	27.29	75.46	66.99
Return (*per cent)*	1.2	1.1	0.8	2.0	1.6
Average rate of interest on Government borrowing *(per cent)*	7.9	7.5	7.5	7.3	7.2
Difference between interest rate and return *(per cent)*	6.7	6.4	6.7	5.3	5.6

Source: Finance Accounts of the State Government

During 2011-12, the State Government invested ₹ 52.44 crore in Statutory Corporations, ₹ 150.40 crore in Government Companies, ₹ 20.25 crore in Other Joint Stock Companies and ₹ 185.93 crore in Co-operative Banks and Societies. Two Statutory Corporations and 51 Government Companies with aggregate Government investments of ₹ 1632.60 crore were incurring losses and their accumulated losses amounted to ₹ 4,028.76 crore as per the latest accounts furnished by these Companies.

Nine major Companies which had accumulated profits as per the latest accounts furnished by them are listed in **Table 1.15.**

Table 1.15: Major profit making companies

(₹in crore)

Sl. No	Name of Government Company	Accounts for the year ended	Accumulated profit
1.	Kerala State Electricity Board	2011-12	1967.61
2.	The Kerala Minerals and Metals Limited	2011-12	550.35
3.	Kerala State Beverages (Manufacturing and Marketing) Corporation Limited	2009-10	330.89
4.	Malabar Cements Limited	2010-11	161.35
5.	The Kerala State Financial Enterprises Limited	2010-11	171.13
6.	The Rehabilitation Plantations Limited	2011-12	128.07
7.	The Kerala Agro-Machinery Corporation Limited	2010-11	96.51
8.	The Plantation Corporation of Kerala Limited	2011-12	147.22
9.	Kerala State Industrial Development Corporation Limited	2011-12	118.27

Source: Annexure 2 of Audit Report (Commercial) for the year ended 31 March 2012

1.6.4 Departmentally managed Commercial Undertakings

Activities of quasi-commercial nature are performed by certain Government departments. There were three[12] departmental commercial undertakings in the State as of March 2012. The department-wise position of the investments made by the Government up to the year for which *pro forma* accounts were finalised, net profit/loss as well as return on capital invested in these undertakings are given in **Appendix 1.7.** The following was observed:

[12] Kerala State Insurance Department, Text Book Office and State Water Transport Department

- There was three to eight years delay in finalization of accounts by these undertakings and no accounts were finalized by any of the undertakings during 2011-12. Present financial position of the undertakings could not be assessed due to delay in finalization of accounts.
- As per the latest accounts finalized by these undertakings an amount of ₹ 183.43 crore had been invested by the State Government in these undertakings. The Kerala State Insurance Department earned a net profit of ₹ 11.40 crore against the capital of ₹ 3.18 crore invested (accounts finalized upto 2008-09) by the Government.
- Two loss-making undertakings viz. State Water Transport Department and Text Book Office were incurring losses continuously for more than five years. The accumulated losses of the State Water Transport Department were ₹ 150.66 crore as against the total investment of ₹ 158.99 crore.

Timely finalization of accounts should be ensured by the Government to assess the financial status and to take corrective steps for their improvement.

1.6.5 Loans and advances by the State Government

In addition to investments in Co-operative Societies, Corporations and Companies, the Government has also been providing loans and advances to many institutions/organisations. **Table 1.16** presents the outstanding loans and advances as on 31 March 2012 and interest receipts *vis-à-vis* interest payments during the last five years**.**

Table 1.16: Average interest received on loans advanced by the State Government

(₹ in crore)

Quantum of Loans/Interest Receipts/Cost of Borrowings	2007-08	2008-09	2009-10	2010-11	2011-12
Opening balance	5,562[13]	6,280[14]	6910[15]	7749	8461[16]
Amount advanced during the year	893	984	877	762	998
Amount repaid during the year	45	36	38	44	55
Closing balance	6,410	7228	7749	8467	9404
Net addition	848	948	839	718	943
Interest receipts	51	48	46	54	23
Interest receipts as a percentage of outstanding loans and advances	0.9	0.7	0.6	0.7	0.2
Interest payments as a percentage of outstanding fiscal liabilities of the State Government	7.9	7.5	7.5	7.3	7.2
Difference between interest payments and interest receipts (*per cent*)	(-) 7.0	(-) 6.8	(-) 6.9	(-) 6.6	(-)7.0

Source: Finance Accounts of the State Government.

[13] Difference of ₹ 152.42 crore with reference to the previous year's closing balance was on account of *pro forma* adjustments vide footnote (b) of Statement no.5 of the Finance Accounts 2007-08.

[14] Difference of ₹ 130.26 crore with reference to the previous year's closing balance was on account of *pro forma* adjustments vide footnotes (b), (d) and (e) of Statement no.5 of the Finance Accounts 2008-09.

[15] Difference of ₹ 317.93 crore with reference to previous year's closing balance was on account of *pro forma* adjustments vide footnote (pp) of Statement no.16 of Finance Accounts 2009-10.

[16] Difference of ₹ 5.65 crore with reference to previous year's closing balance was on account of *pro forma* adjustments vide footnote (Z) of Statement no.16 of Finance Accounts 2011-12.

The total outstanding loans and advances as on 31 March 2012 increased by ₹ 943 crore compared to those of the previous year. The major disbursement of loans during the current year was mainly to the Kerala State Housing Board for the settlement of dues with Housing Development Finance Corporation (₹ 269 crore), to the Kerala Water Authority for implementing the Water Supply Project assisted by the Japan International Co-operation Agency (₹ 232.33 crore) and to the Kerala State Road Transport Corporation (₹ 140 crore). Interest received against these loans remained less than one *per cent* during the period 2007-08 to 2011-12 and was 0.2 *per cent* during 2011-12 as against the cost of borrowing of 7.2 *per cent* during the year.

1.6.5.1 Defaulted loan repayment

Government has been providing loan assistance to Statutory Corporations, Government Companies, Autonomous Bodies/Authorities etc., and the same was treated as assets in the Government accounts. At end of March 2012, the State Government has ₹ 9,404.46 crore as loan balance outstanding in the accounts. Scrutiny of the accounts revealed that 65 *per cent* of the outstanding loan balance was pertaining to four institutions viz. Kerala State Road Transport Corporations (₹ 449.51 crore), Kerala Water Authority (₹ 2,410.17 crore), Kerala State Electricity Board (₹ 2,661.65 crore), Kerala State Housing Board (₹ 617.67 crore). In this regard, the following observations are made:-

- Government has been releasing the loan assistance to these institutions without ascertaining the repayment capacity of the institutions. This has resulted in default in repayment by these institutions. Audit observed that the Government subsequently issues orders to convert accumulated loan amount and interest thereon into share capital/grant based on the request of these institutions.
- During the last five years, Government released ₹ 2,867.84 crore to the above four institutions but received only ₹ 0.44 crore as repayment of loan.
- In respect of the above loans, at the end of March 2012 the arrears in recovery of amounts overdue was ₹ 4,056.43 crore (principal: ₹ 2,429.28 crore and interest: ₹ 1,627.15 crore)

Considering the above facts, Government should not only take stringent steps to recover the loan outstanding but also take necessary steps to write off irrecoverable loans to have clarity in financial status of the Government.

1.6.6 Cash Balances and investment of cash balances

The cash balances and investments made by the State Government out of the cash balances during the year are shown in **Table 1.17**.

Table 1.17: Cash balances and investment of cash balances

(₹ in crore)

Particulars	As on 31 March 2011	As on 31 March 2012	Increase/ Decrease(-)
Cash balances	**5059.73**	**3793.46**	**(-)1266.27**
Investments from cash balances (a + b)	**3517.46**	**2709.85**	**(-)807.61**
a. GOI Treasury Bills	3506.98	2702.62	(-)804.36
b. GOI Securities	10.48	7.23	(-) 3.25
Fund-wise break-up of investments from earmarked balances (a to d)	**1480.74**	**1608.50**	**127.76**
a. Reserve funds bearing interest	…	…	…
b. Reserve funds not bearing interest	1480.74	1608.50	127.76
c. Deposit bearing interest	…	…	…
d. Deposit not bearing interest	…	…	…
Interest realised during the year on investment of cash balances	**106.58**	**82.38**	**(-)24.20**

Source: Finance Accounts of the State Government

- The cash balance as on 31 March 2012 decreased by ₹ 1,266.27 crore over the previous year.
- The interest realised during the year on investment of cash balances also decreased by ₹ 24.20 crore as compared to the previous year.

1.6.6.1 Outstanding balances under the head 'Cheques and Bills'

This head is an intermediary accounting head for initial record of transactions which are to be cleared eventually. As per paragraph 3.2 of the Suspense Manual, when a cheque is issued, the functional head is debited and the Major Head-8670-Cheques and Bills is credited. On clearance of the cheque by the bank, the minus credit is given to Major Head 8670-Cheques and Bills by crediting the Major Head- 8675-Deposits with Reserve Bank and thereby reducing the cash balance of the Government. Thus, the outstanding balance under the Major Head 8670-Cheques and Bills represents the amount of uncashed cheques.

As on 31 March 2012, there was an outstanding balance (cumulative) of ₹ 1,895.52 crore and to this extent, the Government cash balance stood overstated.

1.7 Assets and Liabilities

1.7.1 Growth and composition of assets and liabilities

In the existing Government accounting system, comprehensive accounting of fixed assets like land and buildings owned by the Government is not done. However, the Government accounts do capture the financial liabilities of the Government and the assets created out of the expenditure incurred. **Appendix 1.4** gives an abstract of such liabilities and assets as on 31 March 2012, compared with the corresponding position as on 31 March 2011. While the liabilities in this Appendix consist mainly of internal borrowings, loans and advances from GOI, receipts from the Public Account and Reserve Funds, the assets mainly comprise the capital outlay and loans and advances given by the State Government and its cash balances.

According to the definition given in the Kerala Fiscal Responsibility Act, 2003, total liabilities mean liabilities upon the Consolidated Fund and the Public Account of the State. The ratio of financial liabilities *vis-à-vis* assets, indicates that sixty *per cent* of liabilities are without any backup due to unbridled increasing revenue expenditure.

1.7.2 Fiscal liabilities

The trends of outstanding fiscal liabilities of the State are presented in **Appendix 1.5.** The composition of fiscal liabilities during the current year *vis-à-vis* the previous year is presented in **Charts 1.12** and **1.13.**

Chart 1.12: Composition of outstanding fiscal liabilities as on 1 April 2011 (₹ in crore)

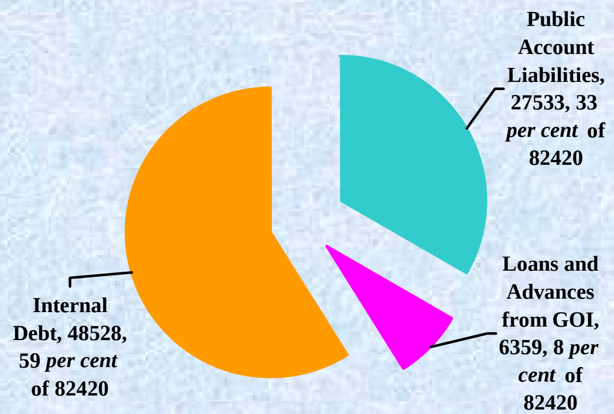
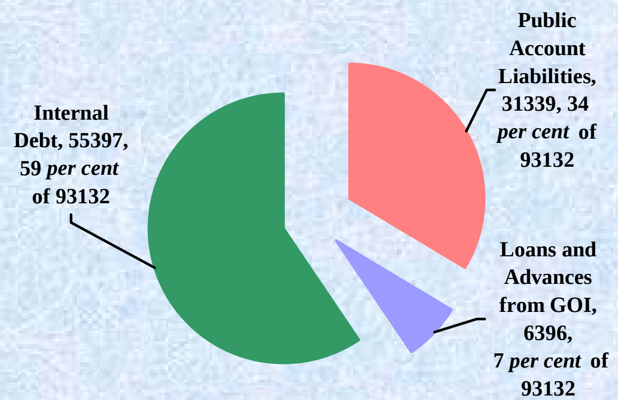


Chart 1.13: Composition of outstanding fiscal liabilities as on 31 March 2012 (₹ in crore)



The overall fiscal liabilities of the State increased from ₹ 82,420 crore in 2010-11 to ₹ 93,132 crore in 2011-12, a growth rate of 13 *per cent*. Fiscal liabilities of the State comprised Consolidated Fund liabilities and Public Account liabilities. As at the end of March 2012, the Consolidated Fund liabilities (₹ 61,793 crore) comprised Market Loans (₹ 38,239 crore), Loans from the Government of India (₹ 6,396 crore) and Other Loans (₹ 17,158 crore). The Public Account liabilities (₹ 31,339 crore) comprised Small Savings, Provident Funds, etc., (₹ 27,625 crore)[17], interest bearing obligations (₹ 44 crore) and non-interest bearing obligations like Deposits and other earmarked funds (₹ 3,670 crore). The fiscal liabilities which were 29.8[(*)] *per cent* of GSDP in 2010-11 decreased to 28.5 *per cent* of GSDP in 2011-12. These liabilities stood at 2.5 times the revenue receipts at the end of 2011-12 compared to 2.7 times at the end of 2010-11. As per the Kerala Fiscal Responsibility (Amendment) Act, 2011 the

[17] This includes liabilities from the Treasury Savings Bank Account (₹ 5,645 crore) and Treasury Fixed Deposits (₹ 5,968 crore)

(*) change in figure is due to adoption of new series of GSDP figures

State has to reduce the State's total debt liabilities to 29.8 *per cent* of the estimated GSDP within a period of four years commencing on the 1 April, 2011 and ending with the 31 March, 2015 by reducing the total debt liability in the years of 2011-12, 2012-13, 2013-14 and 2014-15 to the order of 32.3 *per cent*, 31.7 *per cent*, 30.7 *per cent* and 29.8 *per cent* respectively of the gross state domestic product. During 2011-12 the percentage of State's fiscal liabilities to GSDP (28.5) was much better than the target (32.3) fixed in the Kerala Fiscal Responsibility (Amendment) Act, 2011.

The overall fiscal liabilities of the State include balance under Reserve Funds amounting to ₹ 1,948.72 crore (as on 31 March 2012). The details in respect of two of the reserve funds are given in succeeding paragraphs:

(a) State Disaster Response Fund

The State Disaster Response Fund (SDRF) has been set up from 1 April 2010 replacing the existing Calamity Relief Fund. At the beginning of the year there was ₹ 37.56 crore as opening balance in the Fund. The size of the Fund for Kerala for the year 2011-12 fixed by the ThFC was ₹ 137.63 crore, 75 *per cent* (₹ 103.22 crore) of which was to be contributed by the Central Government and 25 *per cent* (₹ 34.41 crore) by the State Government. During the year the Central and the State Governments contributed their share. After setting off the expenditure for disaster relief operations (₹ 130.71 crore), the balance in SDRF as on 31 March 2012 was ₹ 44.48 crore.

In addition to the yearly contribution the State Government had received an amount of ₹ 109.69 crore from National Disaster Response Fund (March 2012) towards relief on account of Flood/Landslide of 2011 which has not been transferred to SDRF as of March 2012. This has also resulted in understatement of revenue expenditure and revenue deficit to the extent of ₹ 109.69 crore.

According to the guidelines issued by the Government of India, the accretions to SDRF were to be invested in Central Government dated securities and/or Auctioned Treasury Bills and/or interest earning deposits and Certificates of deposits with Scheduled Commercial Banks. However, no such investments were made by the State Government during 2011-12.

(b) Consolidated Sinking Fund

The State Government had set up a Consolidated Sinking Fund from the financial year 2007-08, according to which the Fund was to be utilised as an Amortisation Fund for redemption of all outstanding liabilities of the Government commencing from the financial year 2012-13. The Fund was to be credited with contributions from revenue at the prescribed rate and interest accrued on investments made out of the Fund. Only the interest accrued and credited in the Fund was to be utilised for redemption of the outstanding liabilities of the Government. As per paragraph 5 of revised model scheme for the constitution and administration of Consolidated Sinking Fund of Kerala, the rate of contribution to the Consolidated Sinking Fund was 0.5 *per cent* of the outstanding liabilities as at the end of the previous year. According to this, the State Government had to contribute ₹ 380.30 crore during

2011-12 to the Consolidated Sinking Fund. However, the State Government contributed only ₹ 10.00 crore to the Fund, which resulted in a shortfall of ₹ 370.30 crore during the year. The balance outstanding in the Sinking Fund as on 31 March 2012 was ₹ 1,601.44 crore.

1.7.3 Status of guarantees – contingent liabilities

Guarantees are liabilities contingent on the Consolidated Fund of the State in cases of default by borrowers for whom the guarantees have been extended. Section 3 of the Kerala Ceiling on Government Guarantees Act, 2003 which came into effect on 5 December 2003 stipulates that the total outstanding Government Guarantees as on the first day of April every year shall not exceed ₹ 14,000 crore. As per Section 6 of the Act, the Government was to constitute a Guarantee Redemption Fund. The guarantee commission charged under Section 5 of the Act was to form the corpus of the Fund. However, the Fund had not been constituted and consequently, guarantee commission of ₹ 474.53 crore collected during 2003-04 to 2011-12 had not been credited to the Fund, but was treated as non-tax revenue in the relevant years and used for meeting the revenue expenditure of the Government.

The maximum amount for which guarantees were given by the State and outstanding guarantees at the end of the year since 2007-08 are given in **Table 1.18.**

Table 1.18: Guarantees given by the Government of Kerala

(₹ in crore)

Guarantees	2007-08	2008-09	2009-10	2010-11	2011-12
Maximum amount guaranteed	14,871.08	11,385.54	10,225.78	12,625.07	11332.11
Outstanding amount of guarantees	8,317.34	7,603.32	7,495.00	7,425.79	8277.44
Percentage of maximum amount guaranteed to total revenue receipts	70	46	39	41	30
Criteria as per Kerala Ceiling on Government Guarantees Act, 2003 (Outstanding amount of guarantees as on the first day of April)	14,000	14,000	14,000	14,000	14,000

Source: Finance Accounts of the State Government

The outstanding guarantees at the end of the past five years i.e. 2007-12 ranged between ₹ 7,426 crore and ₹ 8,317 crore, which were well within the ceiling prescribed by the Kerala Ceiling on Government Guarantees Act.

The arrears of guarantee commission receivable as of March 2012 were ₹ 132.34 crore.

1.8 Debt Sustainability

Apart from the magnitude of debt of the State Government, it is important to analyse various indicators that determine the debt sustainability[18] of the State. This

[18] Debt sustainability is defined as the ability of the State to maintain a constant debt-GDP ratio over a period of time and also embodies the concern about the ability to service its debt. Sustainability of debt, therefore, also refers to sufficiency of liquid assets to meet current or committed obligations and the capacity to keep a balance between costs of additional borrowings with returns from such borrowings. It means that the rise in fiscal deficits should match the increase in the capacity to service the debts.

section assesses the sustainability of debt of the State Government in terms of debt stabilisation[19]; sufficiency of non-debt receipts[20]; net availability of borrowed funds[21]; burden of interest payments (measured by interest payments to revenue receipts ratio) and the maturity profile of State Government securities. **Table 1.19** analyses the debt sustainability of the State according to these indicators for the period of five years beginning from 2007-08.

Table 1.19: Debt sustainability: indicators and trends

(₹ in crore)

Indicators of Debt Sustainability	**2007-08**	**2008-09**	**2009-10**	**2010-11**	**2011-12**
Debt Stabilisation (Quantum Spread + Primary Deficit)	1360	3,136(*)	2,113(*)	6,792(*)	2,298
Sufficiency of Non-debt Receipts (Resource Gap)	(-) 2278	(-) 247	(-) 1,525	141	(-)5,084
Net Availability of Borrowed Funds	1629	3,334	2,834	2,507	4,426
Burden of Interest Payments (Interest Payment/Revenue Receipts *percent*)	21	19	20	18	17

Maturity Profile of debt

	2008-09	**2009-10**	**2010-11**	**2011-12**
Up to one year	1.59	1587.67 (3.2)	2566.98 (4.7)	2154.64 (3.5)
One to three years	5852.42 (13.1)	4503.59 (9.1)	5205.33 (9.5)	8401.13 (13.6)
Three to five years	5349.27 (11.9)	5215.70 (10.5)	6260.17 (11.4)	9100.09 (14.7)
Five to seven years	6241.10 (13.9)	6786.36 (13.7)	9314.78 (17.0)	13156.00 (21.3)
Seven years and above	26576.50 (59.3)	27363.90 (55.1)	28162.37 (51.3)	24240.81 (39.2)
Information not furnished by State Government	801.97 (1.8)	4216.09 (8.4)	3377.55 (6.1)	4740.42 (7.7)

Figures in parentheses indicate the percentage to total State debt

Source: Finance Accounts of the State Government

(*) change in figure is due to adoption of new series of GSDP figures

During 2007-08 to 2011-12, the quantum spread together with primary deficit was positive, indicating a declining trend in Debt-GSDP ratio. The resource gap (sufficiency of non-debt receipts) was negative during the period 2007-12 (except during 2010-11) which showed that the incremental non-debt receipts were inadequate to finance incremental primary expenditure and incremental interest

[19] A necessary condition for stability states that if the rate of growth of the economy exceeds the interest rate or the cost of public borrowings, the debt-GSDP ratio is likely to be stable provided primary balances are either zero or positive or are moderately negative. Given the rate spread (GSDP growth rate – interest rate) and quantum spread (Debt x rate spread), the debt sustainability condition states that if the quantum spread together with the primary deficit is zero, their debt-GSDP ratio would be constant or their debt would stabilize eventually. On the other hand, if the primary deficit together with the quantum spread turns out to be negative, the debt-GSDP ratio would be rising. In case it is positive, the debt-GSDP ratio would eventually be falling.

[20] Adequacy of incremental non-debt receipts of the State to cover the incremental interest liabilities and incremental primary expenditure. The debt sustainability could be significantly facilitated if the incremental non-debt receipts could meet the incremental interest burden and the incremental primary expenditure.

[21] Defined as the ratio of debt redemption (Principal + Interest Payments) to total debt receipts and indicates the extent to which the debt receipts are used in debt redemption indicating the net availability of borrowed funds.

burden. During 2011-12, the State Government borrowed ₹ 8,880 crore from the market against ₹ 5,500 crore in the previous year resulting in a net increase of ₹ 3,380 crore in market borrowings. The net availability of borrowed funds after providing interest and repayment of principal was ₹ 4,426 crore against ₹ 2,507 crore in 2010-11 resulted in a net increase of ₹ 1,919 crore. This shows that a larger part of the borrowings in 2011-12 could not be used for developmental activities and were used for meeting Government's current expenditure.

The maturity profile of State debt indicates that the Government will have to repay 49.6 *per cent* of its debt between one and seven years. A well thought out debt management strategy will ensure that no additional borrowings which mature in these critical years are undertaken.

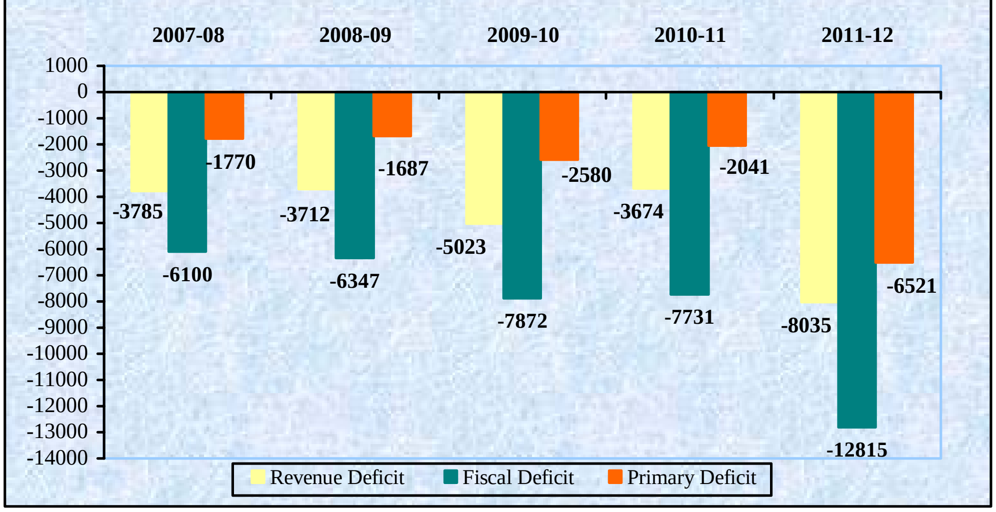
1.9 Fiscal Imbalances

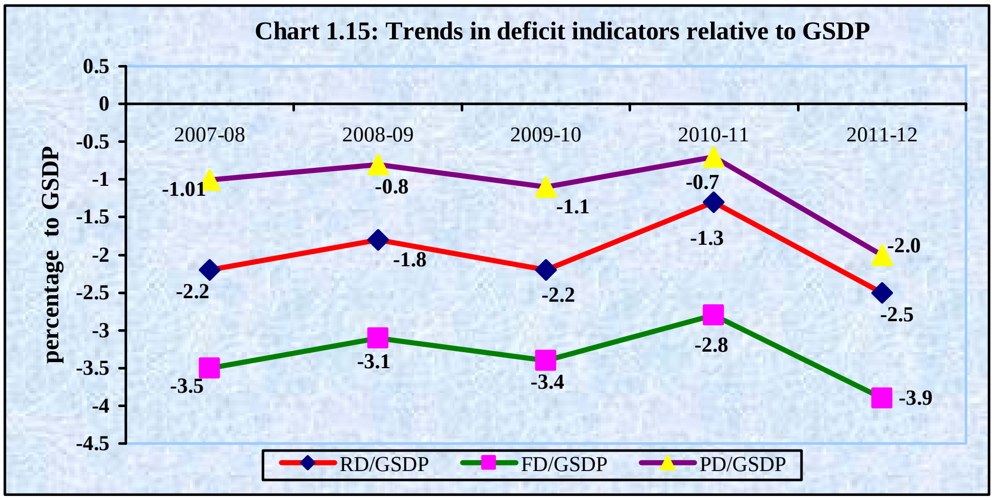
Three key fiscal parameters - revenue, fiscal and primary deficits - indicate the extent of overall fiscal imbalances in the finances of the State Government during a specified period. The deficit in the Government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the Government. Further, the ways in which the deficit is financed and the resources are raised and applied are important pointers to its fiscal health. This section presents the trends, nature, magnitude and the manner of financing these deficits and also the assessment of actual levels of revenue and fiscal deficits *vis-à-vis* targets set under the Fiscal Responsibility Act/Rules for the financial year 2011-12.

1.9.1 Trends in deficits

Charts 1.14 and **1.15** presents the trends in deficit indicators over the period 2007-12.

Chart 1.14 : Trends in deficit indicators (₹ in crore)





The revenue deficit of the State which indicates the excess of its revenue expenditure over revenue receipts showed inter-year variations during 2007-12. Revenue deficit of ₹ 3,785 crore in 2007-08 increased to ₹ 5,023 crore in 2009-10 and decreased sharply to ₹ 3674 crore in 2010-11. However, in 2011-12 it increased enormously by ₹ 4,361 crore (119 *per cent*) and stood at ₹ 8,035 crore due to disproportionate growth of 32.8 *per cent* in revenue expenditure compared to the growth rate of 22.6 *per cent* in revenue receipts.

The fiscal deficit, which represents the total borrowing of the Government and its total resource gap increased steadily from ₹ 6,100 crore in 2007-08 to ₹ 7,872 crore in 2009-10 but narrowly decreased to ₹ 7,731 crore in 2010-11. However, it sharply increased to ₹ 12,815 crore in 2011-12, mainly due to enormous increase in revenue deficit (₹ 4,361 crore).

As a proportion of GSDP, the revenue deficit (1.3 *per cent*) and fiscal deficit (2.8 *per cent*) in 2010-11 were the lowest during the last five year period. These ratios declined further to 2.5 *per cent* and 3.9 *per cent* respectively in 2011-12. However, these percentages were more than the targets fixed (1.81 *per cent* and 3.43 *per cent*) in the Medium Term Fiscal Plan for 2011-12 to 2013-14.

Primary deficit also increased from ₹ 1,770 crore in 2007-08 to ₹ 6,521 crore in 2011-12, recording a three-fold increase during the last five years. Increase in revenue deficit, fiscal deficit and primary deficit indicate the disproportionate growth of expenditure with regard to revenue realization.

These deficits have been calculated after accounting for the debt relief of ₹47.69 crore, given by the GOI during 2011-12 as per the recommendations of the ThFC, as revenue receipts. If the debt relief of ₹47.69 crore is not accounted for as revenue receipts, as recommended by the ThFC, the Revenue deficit, Fiscal deficit and Primary deficit would be ₹8,083 crore, ₹12,863 crore and ₹6,569 crore respectively.

1.9.2 Components of fiscal deficit and its financing pattern

The financing pattern of the fiscal deficit has undergone a compositional shift as reflected in the **Table 1.20.** Receipts and disbursements under the components of financing the fiscal deficit during 2011-12 are given in **Table 1.21.**

Table 1.20: Components of fiscal deficit and its financing pattern

(₹ in crore)

	Particulars	2007-08	2008-09	2009-10	2010-11	2011-12
Decomposition of fiscal deficit						
1	Revenue deficit	3785	3712	5023	3674	8035
2	Net capital expenditure	1467	1687	2010	3339	3837
3	Net loans and advances	848	948	839	718	943
Total fiscal deficit		**6100**	**6347**	**7872**	**7731**	**12815**
Financing pattern of fiscal deficit*						
1	Market borrowings	3634	4782	4710	4770	7496
2	Loans from Government of India	161	476	297	54	36
3	Special Securities Issued to National Small Savings Fund	107	(-) 102	(-) 140	42	(-)491
4	Loans from Financial Institutions	309	116	(-) 16	348	(-)7
5	Small Savings, PF etc	1324	2589	2849	2490	3839
6	Deposits and Advances	492	132	437	469	(-)52
7	Suspense and Miscellaneous	118	(-) 85	370	(-) 197	852
8	Remittances	49	23	57	27	(-)157
9	Others	(-) 160	72	(-) 31	399	32
10	**Total (1 to 9)**	**6034**	**8003**	**8533**	**8402**	**11548**
11	Increase (-)/Decrease (+) in Cash Balance	66	(-)1656	(-) 661	(-) 671	1267
12	**Overall deficit**	**6100**	**6347**	**7872**	**7731**	**12815**
*All these figures are net of disbursements/outflows during the year.						

Source: Finance Accounts of the State Government

Table 1.21: Receipts and disbursements under components financing the fiscal deficit during 2011-12

(₹ in crore)

Sl.No.	Particulars	Receipt	Disbursement	Net
1	Market borrowings	8880	1384	7496
2	Loans from Government of India	407	371	36
3	Special Securities Issued to National Small Savings Fund	0	491	-491
4	Loans from Financial Institutions	457	464	-7
5	Small Savings, PF etc	22982	19143	3839
6	Deposits and Advances	6370	6422	-52
7	Suspense and Miscellaneous	56922	56070	852
8	Remittances	9270	9427	-157
9	Others	374	342	32
10	**Total (1 to 9)**	**105662**	**94114**	**11548**
11	Increase (-)/Decrease (+) in Cash Balance			1267
12	**Overall deficit**			**12815**

Source: Finance Accounts of the State Government

Table 1.20 reveals that during the last five years market borrowings and net accretions in Public Account (especially in Small Savings, PF etc.) are the main source utilized by the State Government to finance the fiscal deficit. During 2011-12 Market borrowings increased from ₹ 5,500 crore to ₹ 8,880 crore, recording an increase of 61.5 *per cent* over the previous year.

During the last five years (2007-12) fiscal deficit was financed mainly by market borrowings, provident funds and small savings. The net accretions from other sources in the Public Account such as deposits, suspense, remittance, etc., was also utilised to finance the fiscal deficit.

During 2011-12, the State Government raised ₹ 8,880 crore as market loans at an average interest rate of 8.85 *per cent*, loans amounting to ₹ 457 crore from NABARD at an interest rate of 6.5 *per cent* and ₹ 54.80 crore from NCDC at interest rates ranging from 8.50 to 13.00 *per cent*. The State Government also received loans amounting to ₹ 407.15 crore from the Government of India during the year for which the details of interest rate on all loans were not available.

The State Government has been mobilising deposits from its employees, pensioners, institutions and general public through treasuries. During 2011-12, the State Government received ₹ 15,218.06 crore as deposits through Treasury Saving Bank accounts at an average interest rate of five *per cent* and ₹ 2,345.50 crore as Treasury Fixed Deposits at interest rates ranging from 7.25 *per cent* and 9.5 *per cent*. The balance of such deposits as on 31 March 2012 was ₹ 11,612.49 crore.

1.9.3 Quality of deficit/surplus

The ratio of revenue deficit to fiscal deficit and the decomposition of primary deficit into primary revenue deficit and capital expenditure (including loans and advances) would indicate the quality of deficit in the States' finances. The ratio of revenue deficit to fiscal deficit indicates the extent to which borrowed funds were used for current consumption. Further, persistently high ratios of revenue deficit to fiscal deficit also indicates that the asset base of the State was continuously shrinking and a part of the borrowings (fiscal liabilities) did not have any asset backup. The bifurcation of the primary deficit **(Table 1.22)** indicates the extent to which the deficit has been on account of enhancement in capital expenditure which may be desirable to improve the productive capacity of the State's economy.

Table 1.22: Primary deficit/surplus – bifurcation of factors

(₹ in crore)

Year	Non-debt receipts (NDR)	Primary revenue expenditure	Capital expenditure	Loans and advances	Primary expenditure	Primary revenue deficit (-)/surplus (+)	Primary deficit (-)/ surplus (+)
1	**2**	**3**	**4**	**5**	**6 (3+4+5)**	**7 (2-3)**	**8 (2-6)**
2007-08	21,160	20,562	1,475	893	22,930	(+) 598	(-) 1,770
2008-09	24,557	23,564	1,696	984	26,244	(+) 993	(-) 1,687
2009-10	26,196	25,840	2,059	877	28,776	(+) 356	(-) 2,580
2010-11	31,060	28,975	3,364	762	33,101	(+) 2,085	(-) 2,041
2011-12	38,081	39,751	3,853	998	44,602	(-) 1,670	(-) 6,521

Source: Finance Accounts of the State Government

The bifurcation of the factors leading to primary deficit or surplus of the State reveals that during the period from 2007-08 to 2010-11 non-debt receipts (NDR) of the State was enough to meet the primary revenue expenditure[22] of the State. However, during 2011-12 NDR was not sufficient to meet the primary revenue expenditure indicating disproportionate growth of primary revenue expenditure during the year and the shortfall being by ₹ 1,670 crore.

1.10 Conclusion

Revenue Receipts : During the current year, the State's Revenue receipts (₹ 38010.36 crore) increased by 22.65 *per cent* over the previous year. There was increase in Tax revenue (₹ 3,996.91 crore) and Non-tax revenue (₹ 661.39 crore) during the year. The State's revenue receipt as a percentage of GSDP marginally declined from 12.1 *per cent* in 2007-08 to 11.6 *per cent* in 2011-12, which indicates that the growth in tax revenue had not kept in pace with that of GSDP.

Revenue Expenditure : The revenue expenditure recorded a steep increase of 32.83 *per cent* during the year. Of the total expenditure of ₹ 50,896 crore during 2011-12, share of revenue expenditure was 90.47 *per cent* (₹ 46,045 crore). Nearly 70 *per cent* of the Revenue expenditure was incurred on salaries, wages, pension payments, interest payments and subsidies.

Capital Expenditure : During the year Capital expenditure (₹ 3,853 crore) increased by ₹ 489 crore (14.5 *per cent*) over the previous year and it accounted for eight *per cent* of the total expenditure of the State. Proportion of Capital expenditure has been much lower as compared to General Category States during 2008-09 and 2011-12.

Investment and returns : As of 31 March 2012, the State had invested ₹ 4,206.43 crore in Statutory Corporations, Government companies, Joint Stock Companies and Co-operatives. The average return on these investments was 1.3 *per cent* during the last five years, while the Government paid an average interest rate ranging from 7.2 *per cent* to 7.9 *per cent* on its borrowings during the same period.

It is not uncommon for a State to borrow for increasing its social and economic infrastructure support and creating additional income generating assets. However, increase in non-developmental expenditure like salaries, interest payments, pension and subsidies year after year reduces the net availability of funds from the borrowings for infrastructure development. The State's low return on investments indicates an implicit subsidy and use of high cost borrowings for investments, which yields low return and is not sustainable.

Loans and Advances : Outstanding loans and advances given by the State Government to Statutory Corporations, Government companies and Co-operative

[22] Primary revenue expenditure represents revenue expenditure less expenditure on interest.

Societies was ₹ 9,404 crore, recording an increase of ₹ 943 crore over the previous year. Sixty five *per cent* of the outstanding loan balance was pertaining to Kerala State Road Transport Corporations (₹ 449.51 crore), Kerala Water Authority (₹ 2,410.17 crore), Kerala State Electricity Board (₹ 2,661.65 crore) and Kerala State Housing Board (₹ 617.67 crore).

Deficit : All the key fiscal parameters, ie revenue, fiscal and primary deficits increased during 2011-12 when compared to previous year. The revenue, fiscal and primary deficit increased to ₹ 8,035 crore, ₹ 12,815 crore and ₹ 6,521 crore in 2011-12 from ₹ 3,674 crore, ₹ 7,731 crore and ₹ 2,041 crore respectively in 2010-11. The ratio of revenue deficit to fiscal deficit increased from 47.5 *per cent* in 2010-11 to 62.7 *per cent* in 2011-12. As a proportion of GSDP, the revenue deficit increased to 2.5 *per cent* and fiscal deficit to 3.9 *per cent* in 2011-12 from 1.3 *per cent* and 2.8 *per cent* respectively in 2010-11.

Increasing revenue and fiscal deficit shows growing fiscal imbalance of the State. Similarly, increase in the ratio of revenue deficit and fiscal deficit indicates that the application of borrowed funds has largely been to meet current expenditure.

Debt Management: Fiscal liabilities at the end of the current year worked out to ₹ 93,132 crore and stood at 28.5 *per cent* of GSDP in 2011-12, which was below the target of 32.3 *per cent* fixed in the Kerala Fiscal Responsibility (Amendment) Act, 2011. During 2008-09 to 2011-12, the quantum spread together with primary deficit was positive indicating a declining trend in Debt-GSDP ratio. During 2011-12 though the State Government borrowed ₹ 8,880 crore from the market, the net availability funds was only ₹ 4,426 crore. Larger part of the borrowings in 2011-12 could not be used for developmental activities and were used for meeting the current expenditure of the Government. The maturity profile of State shows that the State will have to repay 49.6 *per cent* of its debt between one and seven years.

There has been a decline in net availability of funds from its borrowings as large portion of these funds are being used for debt servicing. The ratio of financial assets to liabilities has also deteriorated indicating the greater part of liabilities was without an asset backup. The Balance from Current Revenue (BCR) which plays a critical role in determining its plan size and a negative BCR adversely affects the same and reduces the availability of funds for additional infrastructure requirement.

Monitoring of funds transferred directly from the GOI to the State implementing agencies: Government of India directly transferred ₹ 2,474 crore to the state implementing agencies during the year. But transfer of funds from Government of India to the state implementing agencies directly ran the risk of inadequate monitoring of utilisation of funds by these agencies in the absence of uniform accounting procedures and effective monitoring system.

1.11 Recommendations

- The State Government should evolve an appropriate control mechanism to ensure proper accounting and timely utilisation of funds flowing directly to implementing agencies through off-budget route.

- Timely finalization of accounts of Departmental Commercial Undertakings should be ensured by the Government to assess the financial status and to take corrective steps for their improvement.

- Before release of loans to statutory corporations/Government companies, Government should review the repaying capacity of these institutions and alternate methods may be considered for releasing funds.

- The State Government should constitute Guarantee Redemption Fund as envisaged in the Kerala Ceiling on Government Guarantees Act, 2003 and credit guarantee commission collected so far, into the fund.

- The State Government should make yearly contribution to the Consolidated Sinking Fund as envisaged in view of the increase in the amount of debt servicing in the coming years.

- The State Government should ensure re-investment of fund balances for possible accretions to the fund balance.

- The State Government should take necessary steps to increase the net availability of borrowed funds for use in developmental activities.