

## Background

In Karnataka, fiscal reforms and consolidation were brought to the forefront with the State Government formulating the first Medium Term Fiscal Plan (MTFP) for the period 2000-05, based on broad parameters of fiscal correction laid down by the Eleventh Finance Commission (EFC). MTFP became a rolling annual document and the fiscal targets and policies set out in MTFP were dovetailed to the annual budgetary exercise to operationalise the restructuring plan. Karnataka was the first State to enact (September 2002) the Fiscal Responsibility Act (FRA) providing statutory backing to MTFP. The Act aims at ensuring fiscal stability and sustainability, enhancing the scope for improving social and physical infrastructure and human development by achieving revenue surplus, reducing fiscal deficit, removing impediments to effective conduct of fiscal policy and prudent debt management through limits on borrowings, debt and deficits and greater transparency in fiscal operations by the use of medium-term fiscal framework.

## The Report

Based on the audited accounts of the Government of Karnataka for the year ended March 31, 2013, the report provides an analytical review of the annual accounts of the State Government. The financial performance of the State has been assessed based on the FRA, budget documents, Thirteenth Finance Commission Report (XIII FC) and other financial data obtained from various Government departments and organizations. The report is structured in three chapters.

**Chapter I** is based on the audit of Finance Accounts and makes an assessment of Government of Karnataka's fiscal position as at March 31, 2013. It provides an insight into trends in committed expenditure and borrowing pattern, besides a brief account of Government of India funds transferred directly to the State implementing agencies through off-budget route. It also contains a study on the open market borrowings covering the period 2008-13.

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

**Chapter III** is an inventory of Karnataka Government's compliance with various reporting requirements and financial rules.

The report also includes appendices of additional data collected from several sources in support of these findings. A glossary of selected terms has been given at the end of the Report.

## **Audit findings and recommendations**

### **• Fiscal position**

The State continued to maintain revenue surplus during 2008-13 and kept fiscal deficit relative to Gross State Domestic Product (GSDP) below the limit laid down under FRA as amended from time to time. During 2012-13, the State had a revenue surplus of ₹ 1,883 crore, a decrease of ₹ 2,638 crore over previous year. This was on account of increase in revenue expenditure by 17 *per cent* over previous year, while the growth rate of revenue receipts were 12 *per cent*.

Fiscal deficit during the year was ₹ 14,507 crore, an increase of ₹ 2,037 crore over previous year. Primary deficit increased by ₹ 1,187 crore during the year from ₹ 5,866 crore in 2011-12.

Incremental non-debt receipts of ₹ 8,231 crore was less than the incremental primary expenditure of ₹ 9,588 crore and could not cover the incremental interest burden (₹ 850 crore).

### **• State's own resources**

The ratio of the State's tax revenue to GSDP had shown an increasing trend since 2008-09, it increased from 8.91 *per cent* in 2008-09 to 10.23 *per cent* during the year.

Ratio of non-tax revenue to revenue receipts has significantly reduced from 7.30 *per cent* in 2008-09 to 5.10 *per cent* during the year. Its ratio to GSDP was insignificant, implying the need for mobilizing non-tax revenue in the coming years by revising user charges, as recommended by Expenditure Reforms Commission.

### **• Revenue expenditure**

Expenditure under social and economic sector registered growths of 21 and 13 *per cent* respectively over the previous year, while the growth in general services was 23 *per cent*. The share of plan expenditure in total revenue expenditure increased from ₹ 18,567 crore in 2011-12 to ₹ 21,212 crore in 2012-13. Eighty eight *per cent* of revenue expenditure consisted of committed expenditure on salaries, pensions, interest payments, subsidies administrative expenses, grants-in-aid and financial assistance and devolutions to Local Bodies. The committed expenditure consumed 94 *per cent* of revenue receipts. Explicit subsidy increased from ₹ 7,390 crore in 2011-12 to ₹ 10,709 crore during the year and implicit subsidy increased from ₹ 1,313 crore in 2011-12 to ₹ 1,893 crore during the year. As per the recommendation of Twelfth Finance Commission, expenditure forming implicit subsidy should be brought out for transparency in accounts.

### **• Quality of expenditure**

The share of capital expenditure to total expenditure during the current year was 18 *per cent* which was three percentage point less than the previous year. Funds aggregating ₹ 773 crore were blocked in incomplete projects as at the end of 2012-13. The return from investment of ₹ 49,464 crore as of March 31, 2013 in companies / corporations was negligible (₹ 56.29 crore). The investment included ₹ 20,110 crore (41 *per cent*) in Companies/ Corporations under perennial loss.

The State Government should review the working of State Public Sector

Undertakings incurring huge losses and take suitable decisions. The State

Government should formulate guidelines for quick completion of incomplete projects and strictly monitor time and cost overrun with a view to taking corrective action.

- **Monitoring of funds transferred directly from the GOI to the State implementing agencies**

Government of India directly transferred ₹ 6,649 crore to the State implementing agencies during 2012-13. But transfer of funds from GOI to 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. The State Government have to put in place an appropriate control mechanism to ensure proper accounting and timely utilisation of funds flowing directly to implementing agencies through off-budget route.

- **Funds and other Liabilities**

The operation of the State Disaster Response Fund was not in tune with the rules governing the Fund. The transactions relating to Karnataka Silk Worm Cocoon and Silk Yarn Development and Price Stabilisation Fund were not carried out during the year due to lack of budget provision. The Guarantee Redemption Fund has not been revived. Funds which have remained dormant over a period of time are required to be analyzed for their continuation or otherwise. The adjustment to the Sinking Fund was questionable.

- **Debt sustainability**

Forty six per cent of the open market borrowings are in the maturity bracket of above seven years. The State Government has to schedule its borrowings in a prudent manner so as not to burden future generation with high cost debt. The practice of borrowing based on necessity rather than availability should be strictly adhered to. Parking of funds either in nationalized bank/deposit account should be avoided.

## **Financial Management and Budgetary Control**

Against total provision of ₹ 1,26,395 crore during 2012-13, an expenditure of ₹ 99,955 crore was incurred. This resulted in an unspent provision of ₹ 26,440 crore (21 *per cent*). Excess expenditure of ₹ 494 crore under Demand number 8 for the year 2012-13 is required to regularized under Article 205 of the Constitution. Expenditure aggregating ₹ 90.86 crore in eight cases which should have been treated as 'New Service/New instrument of service' was incurred without the approval of the Legislature. While, supplementary provision of ₹ 1,053 crore in 14 cases was unnecessary, re-appropriation of funds in 57 cases was made injudiciously, resulting in either un-utilised provision or excess over provision. In 13 grants, ₹ 7,387 crore was surrendered in the last two working days of the financial year. Contingency Fund transactions were not in accordance with the rules governing the fund (two cases).

Budgetary control should be strengthened in all departments to avoid cases of provision remaining unutilized. The departmental budgets should be more realistic and cases of persistent non-utilisation of funds, excessive provision of funds should be avoided.