EXECUTIVE SUMMARY

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Background

The State is located at the southern end of the country, sharing borders with Tamil Nadu and Karnataka. In terms of geographical area, Kerala is ranked 21st in the country with an area of 38,863 sq.km. While the State is having a population of 3.34 crore (12th in the country), it remains the third most densely populated State with a density of 860 persons per sq.km. The State's population increased from 3.18 crore in 2001 to 3.34 crore in 2011 recording a decadal growth of five *per cent*. The State's percentage of population below the poverty line is less than the all-India average. The State's Gross State Domestic Product (GSDP) in 2013-14 at current prices was ₹4,02,972 crore. The State's literacy rate increased from 90.9 *per cent* (as per 2001 census) to 94 *per cent* (as per 2011 census). The per capita income (2012-13) of the State at current prices stands at ₹99,977against the country average of ₹68,757.

About the Report

This Report of the Finances of the Government of Kerala is being brought out with a view to assess objectively, the financial performance of the State during 2013-14 and to provide the State Government and the State Legislature with timely inputs based on audit analysis of financial data. In order to give a perspective to the analysis, an effort has been made to compare the achievements with the targets envisaged by the State Government in the budget estimates of 2013-14. Based on the audited accounts of the Government of Kerala for the year ended March 2014, this Report provides an analytical review of the Annual Accounts of the State Government. This Report is structured in three Chapters.

Chapter 1 is based on the audit of Finance Accounts and makes an assessment of the Kerala Government's fiscal position as on 31 March 2014. It provides an insight into trends in committed expenditure and borrowing pattern, besides giving a brief account of Government of India funds transferred directly to the State implementing agencies through off-budget route.

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

Chapter 3 is an inventory of the Kerala Government's compliance with various reporting requirements and financial rules. The report also compiles the data compiled from various Government departments/organizations in support of the findings.

Audit findings and recommendations

Chapter I : Finances of the State Government

Overall financial status: With a view to ensuring prudence in fiscal management and fiscal stability by progressive elimination of revenue deficit and sustainable debt management, the State Government enacted Kerala Fiscal Responsibility Act, 2003 which came into force on 5 December 2003. Based on the recommendations of Thirteenth Finance Commission, the Act was amended in 2011. Medium Term Fiscal Plan for ensuing three years were presented along with annual budget of each year to highlight the effect to the fiscal management principles laid down in the Act. However, fiscal targets fixed in the Medium Term Fiscal Plan were not achieved by the State.

All the three fiscal parameters, viz. primary, revenue and fiscal deficits increased during the last three years. Increasing gap between revenue receipts and revenue expenditure indicates that State has to depend more on borrowed funds for meeting revenue expenditure. Though, 60 *per cent* increase was there in fiscal liabilities during the last five years, its ratio with respect to GSDP was within the target fixed in the Kerala Fiscal Responsibility (Amendment) Act, 2011.

Revenue Receipts: The growth rate of revenue receipts was 11 *per cent* during the year against 16 *per cent* showed during the last year (2012-13). State Government estimated a revenue of ₹58,057.88 crore in its original budget and subsequently reduced to ₹54,966.85 crore while presenting the revised estimate. However, State could realize only ₹49,176.93 crore, resulting in a shortfall of ₹5,789.92 crore. Non-realisation of revenue as anticipated led to enhancement in revenue deficit and consequent failures in achievement of fiscal targets fixed for the year.

As in the previous year, taxes on Sales, Trade, etc were the main sources of tax revenue of the State. However, revenue from Stamps and Registration fees and State Excise decreased when compared with the revenue of the previous year. Income from State Lotteries was major source of revenue under Non-tax Revenue, but equally high expenditure towards payment of prize, commission, etc. resulted in net yield only ₹two crore more than the previous year.

In order to achieve the fiscal targets fixed by Thirteenth Finance Commission and in the Kerala Fiscal Responsibility (Amendment) Act, 2011, State needs to increase the revenue receipts in the coming years.

Revenue Expenditure: During 2013-14, revenue expenditure increased by 13 *per cent* over the previous year. Major share of this increase was under non-plan revenue expenditure. While non-plan revenue expenditure recorded a growth of 98 *per cent*, plan expenditure recorded only 69 *per cent* during last five years. This shows low priority of the State towards plan expenditure. Significantly, 65 *per cent* of the revenue expenditure in 2013-14 was incurred on salaries, wages, pension payments, interest payments and subsidies. This was also 79 *per cent* of the revenue receipts during the year, a matter of concern for the State Government. Government should consider increase in share of plan expenditure in revenue expenditure to enhance the scope of socio-economic growth of the State.

Capital Expenditure: As compared with previous year, the Capital expenditure during 2013-14 decreased by ₹309 crore (seven *per cent*). More significantly, share of capital expenditure in total expenditure ranged between six to nine *per cent* during last five years. Compared with the status of General Category States, expenditure on capital projects (including loans and advances) in Kerala was five percentage lower than those States. Though, the State Government provided adequate priority to Education and Health sector, expenditure on Social Services sector and Development sector was lower than General Category States. Government should review the inadequate growth of capital expenditure so as to match with the ratio of General Category States.

Loans and Advances: During the year, State Government had released an amount of ₹1,464 crore to Statutory Corporations, Government companies, Co-operative Societies, etc., and accumulated balance outstanding at the end of March 2014 was ₹11,721 crore. However, as against only ₹124 crore (Principal:₹103 crore and Interest:₹21 crore) was recovered during the year and at the close of the year ₹7,658 crore (Principal: ₹4,649 crore and interest: ₹3,009 crore) was due from 72 institutions as arrears in repayment of loan. Major defaulters were Kerala Water Authority (₹3,294 crore), Kerala State Electricity Board (₹1,729 crore), Kerala State Road Transport Corporation (₹649 crore) and Kerala State Cashew Development Corporation (₹296 crore). In spite of these arrears, ₹1,018 crore was released to 23 institutions/defaulters during 2013-14. Government should perform a risk assessment of the institutions and review the repaying capacity of the institutions before release of loans to statutory corporations/Government companies, to prevent the loan becoming liabilities to the State.

Debt Management: Fiscal liabilities of the State increased from ₹1,08,477 crore in April 2013 to ₹1,24,081 crore at the end of March 2014. Share of market loans in overall fiscal liabilities had increased and it was around 50 *per cent* of the outstanding fiscal liabilities at the end of March 2014. However, fiscal liabilities as a percentage of GSDP was 30.8 *per cent* which is almost in line with the target fixed in the Kerala Fiscal Responsibility (Amendment) Act, 2011.

As the non-debt receipts of the State were insufficient, some portion of the borrowed funds was used for bridging the revenue gap. After providing for principal and interest amount, the net availability of borrowed funds during 2013-14 was only ₹7350 crore. State was left with around 50 *per cent* of the borrowed funds (₹14342 crore) for development activities.

Deficit: All the key fiscal parameters, such as revenue, fiscal and primary deficits increased during 2013-14 also, since revenue realization was not as anticipated. Widening gap between revenue receipt and revenue expenditure and increasing ratio between revenue deficit and fiscal deficit indicates that main issue needs to be addressed by the State is increasing revenue deficit. The targets fixed as percentage of GSDP with respect to revenue and fiscal deficits (2.8 *per cent* and 4.2 *per cent*) were not achieved by the State and it was much higher than the targets fixed (0.54 *per cent* and 2.82 *per cent*) in the Medium Term Fiscal Plan for 2013-14 to 2015-16.

As per the Kerala Fiscal Responsibility (Amendment) Act, 2011 State needs to bring down revenue deficit as a percentage of GSDP to 'Nil' by the end of March 2015. In order to achieve this target, State Government has to make concerted efforts otherwise target is unlikely to be achieved.

Study report on selected topics:

Direct release of funds to the State implementing agencies: During the last five years, Government of India directly transferred ₹9,751 crore to the State implementing agencies. Short-release of State's matching contribution amounting to ₹84 crore was noticed in respect of three schemes test checked in Audit. Due to deficiency in monitoring process, implementing agencies furnished utilisation certificates for the funds lying unutilized with sub-level agencies. Appropriate control mechanism needs to be put in place to ensure proper accounting and timely utilisation of funds flowing directly to implementing agencies through off-budget route.

Implementation of New Pension Scheme: State Government introduced new pension scheme for All India Services officers who joined service on or after 1 April 2004. But, neither individual contribution nor matching contribution of State Government was credited to the pension account of the officials. The same pattern of pension scheme was also implemented among State Government employees, who joined service on or after 1 April 2013. Appropriate steps need to be taken to credit arrear contributions to individual's pension account, without further delay.

Management of Guarantee given by the State: The amount of outstanding guarantee at the end of March 2014 was ₹9763.36 crore. Guarantees were given on behalf of institutions without properly ascertaining their financial stability, which led to guarantees becoming liabilities of the Government. Government did not constitute the Guarantee Redemption Fund due to which the guarantee commission was not being credited into this fund. Instead, it was still being treated as part of non-tax revenue of the State for the last ten years.

Chapter II

Financial Management and Budgetary Control

During 2013-14, out of the total budget allocation of ₹80,661 crore, 19 *per cent* allocation (₹15,719 crore) remained unutilized. During test check, persistent savings were noticed in six Grants/Appropriations during the last three years. Of this, more than 50 *per cent* of the budget allocation remained unutilized in four Grants/ Appropriations during all the three years. Excess expenditure of ₹560.68 crore disclosed under six Grants and four appropriations requires regularization under Article 205 of the Constitution as summarized. Excess expenditure occurred for the years 2011-12 and 2012-13, under 27 Grants and three Appropriations amounting to ₹1,258.18 crore was to be regularized by the Public Accounts Committee.

Supplementary provisions obtained in 30 Grants/Appropriation (₹one crore or more in each case) during the year, proved unnecessary as the expenditure did not come up to the level of even the original provisions. In seven out of above 30 Grants/Appropriation, supplementary grants were obtained while more than 50 *per cent* of the original provision remained unutilized. Also, in 20 Grants/Appropriations the amounts surrendered (₹one or more in each case) was in excess of the actual savings. These instances indicate deficiency in appropriation control process by the departments.

Delay in completing the formalities for withdrawing from Consolidated Fund of the State, led to withdrawal of funds at the fag end of the financial year. In twenty out of forty test-checked cases, funds (₹57.64 crore) were withdrawn on the last working day of the financial year. In majority of the test checked cases, the amounts shown as expenditure under respective heads of accounts were only parked either in Treasury Savings Bank account or in other bank accounts.

Review of selected grant Grant No.XXII-Urban Development revealed that Budget allocations in the Grant were made in excess of annual requirements made by department/implementing agencies. Budget proposals were also made without considering the actual expenditure of the previous year, which led to inclusion of huge provision in the budget.

Budgetary controls need to be strengthened in all Government Departments, so that variations in budget estimates and actual expenditure can be minimized to the extent possible.

Chapter III

Financial Reporting

The Government's compliance with various rules, procedures and directives were lacking in some departments. Delayed submission or ignorance of the procedure in submission of utilisation certificates by the institutions were the main reasons for non-receipt of utilisation Certificate in the office of the Principal Accountant General (A&E). Twenty six autonomous bodies/authorities were required to submit their accounts in respect of grant-in-aid received by them during the year 2013-14. Finality has not been reached in long pending cases of misappropriation, defalcation, etc., involving Government money. Funds released for implementation of State/Central schemes were parked in Treasury Savings Bank accounts, without utilisation up to six years. Though there were instructions to penalize officers for keeping the funds outside Government account, departmental officers continue to do the same and no penalty was imposed on them. Inoperative PD accounts were seen retained without closing. Non-reconciliation of departmental balance with treasury balance caused difference between both the balances and no efforts were taken by departmental officers to reconcile them.