Chapter 1

Finances of the State Government

Profile of the State

The State of Karnataka is the eighth largest State in terms of geographical area (1,91,791 Sq. Km) and the eighth largest by population. The State's population increased from 5.28 crore in 2001 to 6.11 crore in 2011, recording a decadal growth of about 16 *per cent*. The *percentage* of population below the poverty line was 21.90 compared to the All India Average of 29.50 during 2011-12. The State's Gross State Domestic Product (GSDP) in 2015-16 at market prices was ₹7,35,975 crore. The State's literacy rate increased from 66.64 *per cent* in 2001 to 75.36 *per cent* in 2011. The per-capita income of the state stands at ₹1,45,799 against the country average of ₹93,231 (As of March 2016 –Economic Survey 2015-16). General data relating to the State is given in **Appendix 1.1**

Gross State Domestic Product (GSDP)

GSDP is the market value of all officially recognized final goods and services produced within the State in a given period of time. The growth of GSDP of the State is an important indicator of the State's economy, as it indicates the standard of living of the State's population. The trends in the annual growth of the State, at current prices, are indicated in **Table 1.1**.

Table 1.1: GSDP at current prices

Year	2011-12	2012-13	2013-14 (QE)	2014-15 (AE)	2015-16 (RE)
State's GSDP* (₹in crore)	4,34,270	5,20,766	6,01,633	6,85,207	7,35,975
Growth rate of GSDP (*percentage*)	14.02	19.92	15.53	13.89	7.41

Source: MTFP 2016-20

(QE: Quick Estimates, AE: Advance Estimates, RE: Revised Estimates)

**GSDP figures for the years 2011-12 to 2015-16 have been worked out with the base year 2004-05 as per MTFP 2016-20.*

Comparison of the GSDP to that of national GDP has not been made as the GDP figures were worked out with base year 2011-12, whereas the State GSDP was made with base year 2004-05.

The growth rate of GSDP was 14.02 *per cent* during 2011-12, which increased to 19.92 *per cent* in 2012-13 and showed a reducing trend since then and was at 7.41 *per cent* during 2015-16.

1.1 Introduction

This chapter provides a broad perspective of the finances of the Government of Karnataka during 2015-16. It analyses important changes in the major fiscal indicators compared to the previous year, keeping in view the overall trends during the last five years. The analysis is based on the Finance Accounts and information obtained from the State Government. The structure of the

Government Accounts and the layout of the Finance Accounts have been explained in **Appendix 1.2**.

1.1.1 Summary of fiscal transactions in 2015-16

Table 1.2 and **Appendix 1.3** present the summary of the State Government's fiscal transactions during 2015-16 *vis-a-vis* the previous year (2014-15), while **Appendix 1.4** provides the details of receipts and disbursements as well as the overall fiscal position during the preceding four years.

Table 1.2 Summary of fiscal transactions in 2015-16

(₹ in crore)

Receipts			Disbursements				
	2014-15	2015-16		2014-15	2015-16		
Section-A Revenue				**Total**	**Non-Plan**	**Plan**	**Total**
Revenue Receipts	**1,04,142.15**	**1,18,817.31**	**Revenue Expenditure**	**1,03,614.29**	**77,018.84**	**40,009.74**	**1,17,028.58**
Tax revenue	70,180.21	75,550.18	General Services	28,265.27	30,574.06	225.22	30799.28
Non-tax revenue	4,688.24	5,355.04	Social Services	39,366.25	22,191.29	24,115.79	46307.08
Share of Union taxes/duties	14,654.25	23,983.34	Economic Services	29,971.31	20,383.68	13,463.49	33,846.17
Grants-in-aid and contributions from GOI	14,619.45	13,928.75	Grants-in-aid and contributions	6,011.46	3,870.81	2,205.24	6,076.05
Section-B: Capital and others:							
Misc. Capital receipts	**10.14**	**352.30**	**Capital Outlay**	**19,622.30**	**397.13**	**20,315.90**	**20,713.03**
			General Services	618.46	41.74	949.67	991.41
			Social Services	4,180.89	218.76	5,095.15	5,313.91
			Economic Services	14,822.95	136.63	14,271.08	14,407.71
Recoveries of Loans and Advances	**83.82**	**59.68**	**Loans and Advances disbursed**	**576.15**	**98.28**	**558.13**	**656.41**
Public debt receipts**	**21,874.63**	**21,072.33**	**Repayment of public debt****	**4,812.23**	**4,110.20**	**-**	**4,110.20**
Contingency Fund	**-**	**-**	**Contingency Fund**	**-**	**-**	**-**	**-**
Public Account Receipts	**1,40,229.39**	**1,60,518.76**	**Public Account disbursements**	**1,29,573.99**	**-**	**-**	**1,55,094.83**
Opening Cash Balance	**15,759.73**	**23,900.90**	**Closing Cash Balance**	**23,900.90**	**-**	**-**	**27,118.23**
Total	**2,82,099.86**	**3,24,721.28**	**Total**	**2,82,099.86**			**3,24,721.28**

Source: Finance Accounts 2015-16

*** Excluding net transactions under ways and means advances and overdraft.*

The following are the significant changes during 2015-16 over the previous year:

- Revenue receipts grew by ₹14,675.16 crore (14 *per cent*) due to increase in Share of Union Taxes/Duties (₹9,329.09 crore), Own Tax Revenue (₹5,369.97 crore), and Non-Tax Revenue (₹666.80 crore), offset by decrease in Grants-in-aid and contributions from Government of India (₹690.70 crore). The revenue receipts for the year 2015-16 were short of the projection made in the Medium Term Fiscal Plan (MTFP) 2012-16 by ₹5,675.69 crore.

- Revenue expenditure increased by ₹13,414.29 crore (13 *per cent*). Increase was under Social Services Sector (₹6,940.83 crore), Economic

Services Sector (₹3,874.86 crore), General Services Sector (₹2,534.01 crore), and Grants-in-Aid and Contributions (₹64.59 crore). It exceeded the MTFP 2012-16 projections for the year by ₹335.58 crore.

- Capital outlay increased by ₹1,090.73 crore (6 *per cent*). Increase was mainly under Social Services Sector (₹1,133.02 crore) and General Services Sector (₹372.95 crore) and offset by decrease under Economic Services (₹415.24 crore).

- Recoveries of Loans & Advances decreased by ₹24.14 crore (29 *per cent*) and Disbursement of Loans & Advances increased by ₹80.26 crore (14 *per cent*).

- Public debt receipts (excluding ways and means advances) decreased by ₹802.30 crore (4 *per cent*) while repayments decreased by ₹702.03 crore (15 *per cent*).

- Public Account receipts and disbursements increased by ₹20,289.37 crore (14 *per cent*) and ₹25,520.84 crore (20 *per cent*), respectively.

- Cash balance of the State Government increased by ₹3,217.33 crore (13 *per cent*).

1.1.2 Review of Fiscal situation

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 on the basis of broad parameters of the fiscal correction path laid down by the Eleventh Finance Commission (EFC). Towards this end, the Karnataka Fiscal Responsibility Act (KFRA) was enacted (September 2002), which became operational from 1 April 2003 and provided statutory backup to the MTFP.

The State Government had been on a fiscal consolidation path since passing of the KFRA and had maintained the guarantees within the limits prescribed under the Karnataka Ceiling on Government Guarantees Act, 1999. It had recorded revenue surplus since 2004-05 and the fiscal deficit was within the limit of 3 *per cent* of GSDP as prescribed under the Act. However, during 2008-09 and 2009-10, as per the directives of Government of India (GOI), the state deviated from the fiscal consolidation path and borrowed more money for public spending to tide over economic slowdown, by amending the Act.

By an amendment to the Act in February 2014, the scope of the total liabilities as defined under Section-2(g) was amplified to include the borrowings by Public Sector Undertakings (PSU) and Special Purpose Vehicles (SPVs) and other equivalent instruments, where the principal and/or interest are to be serviced out of the State Budget. The State Government had been amending its KFRA from time to time keeping in view the parameters prescribed by the successive Finance Commissions.

The XIV Finance Commission (XIV FC) has recommended a set of rules for the State relating to fiscal deficit targets and annual borrowing limits for the State.

- Fiscal deficit will be anchored to an annual limit of 3 *per cent* of GSDP. The State will be eligible for flexibility of 0.25 *per cent* over and above this for any given year for which the borrowing limits are to be fixed if their debt GSDP ratio is less than or equal to 25 *per cent* in the preceding year.

- Eligible for an additional borrowing limit of 0.25 *per cent* of GSDP in a given year for which the borrowing limits are to be fixed if the interest payments are less than or equal to 10 *per cent* of the revenue receipts in the preceding year.

- The two options under these flexibility provisions can be availed of by the State either separately, if any of the above criteria is fulfilled, or simultaneously if both the above state criteria are fulfilled. Thus, a State can have a maximum fiscal deficit-GSDP limit of 3.5 *per cent* in any given year.

- The flexibility in availing the additional limit will be available if there is no revenue deficit in the year in which borrowing limits are to be fixed and immediately preceding year.

- If the State is not able to fully utilize its sanctioned borrowing limit of 3 *per cent* of GSDP in any particular year during the first four years of award period (2015-16 to 2018-19), it will have the option of availing this unutilised borrowing amount only in the following year but within the award period.

However, the KFRA was not amended during the period to reflect the above recommendations. The MTFP placed before the Legislature also did not contain the reasons behind the non-amendment.

The ratio of outstanding debt (inclusive of off-budget borrowings) and fiscal deficit to GSDP (₹7,35,975 crore) during 2015-16 were 24.91 *per cent* and 2.60 *per cent*, respectively, which were within the prescribed limit of 25 *per cent* and 3 *per cent* respectively.

The Fiscal Management Review Committee (FMRC), headed by Chief Secretary to Government was constituted in July, 2011. The committee recommended remedial measures to be adopted to ensure adherence to the parameters stipulated in KFRA, which were as under.

- A thorough scrutiny of the State's liabilities to be taken up including the treatment of liabilities, especially the Reserve Funds, in the fiscal act.

- Writing back of large amount of unspent balances in the Local Body Funds in Public Account to create additional fiscal space.

- Continuing the practice of resorting to budgetary borrowings only in the 3rd and 4th quarters.

- Alternate budgetary framework may be evolved as Union budget is doing away with Plan and Non-Plan distinction from FY 2017-18.

- Rationalize existing Government schemes so as to have focused approach on the outcomes by avoiding thin spread of resources.

- Approve new initiatives and works requiring implementation over multiple years based on fiscal sustainability of the total expenditure, rather than expenditure during the year of approval only to avoid buildup of fiscal stress due to unfunded expenditure commitments.

- To make more & more resources available for developmental expenditure, regulation of creation of new posts and filling up of vacancies in non-core spheres has to be continued.

- Implementation of schemes and programs through bank and personal deposit accounts outside the Consolidated Fund should be minimized.

- Large projects particularly in Water Resources Department (WRD), Urban Development Department (UDD) and Rural Development and Panchayat Raj (RDPR) department should be accompanied by a financing plan.

- Follow up with departments for improving their non-tax revenues by regular revision of fees, user charges etc.

Scrutiny of certain high end transactions during 2015-16 revealed that the fiscal deficit and the liabilities in the Public Account were reduced more through certain accounting adjustments than through fiscal management. Such adjustments are discussed below in brief.

- Consolidated Fund expenditure of ₹1,118 crore towards Capital Expenditure on Roads and Bridges was adjusted to the Infrastructure Initiative Fund (IIF) maintained in Public Account, thereby compressing capital expenditure to that extent. The cumulative liability in Public Account also got reduced to that extent.

- An expenditure of ₹800 crore incurred on power projects was withdrawn and shown as expenditure met out of IIF maintained in Public Account, thus compressing the Capital Expenditure under the Consolidated Fund to that extent. The resultant liability in the Public Account also got reduced to the extent indicated. There were no investments under the fund.

- During 2015-16, Capital Expenditure of ₹500 crore incurred on projects related to Bengaluru City was withdrawn and shown as expenditure met out of IIF maintained in Public Account, thus compressing the Capital Expenditure under the Consolidated Fund to that extent. The resultant liability in the Public Account also got reduced to the extent indicated.

- During April 2015, the Chief Accounts Officer, Sarva Shiksha Abhiyan (SSA) remitted ₹213.41 crore to the Head of Account (HOA) '2202-01-Elementary Education' and accounted it as recovery of over payment. This was due to release of funds over and above the requirement during the previous years, which were kept in bank account, resulting in compression of expenditure to the extent cited and also a bearing on fiscal indicators.

- The grants to Panchayat Raj Institutions (PRIs) are released from functional heads under the Consolidated Fund and accounted under Public Account. The balances under the Zilla Panchayat (ZP) Fund II account and Taluk Panchayat (TP) Fund as the end of March every year should be written back to the Consolidated Fund in the next financial year. Write back of ₹188.50 crore for the year 2013-14 and ₹220.45 crore for the year 2014-15 under ZP Fund II and ₹10.15 crore under TP Fund was made during 2015-16 which has led to suppression of expenditure to the extent of ₹419.10 crore, treating the transaction as recoveries of over payments under revenue account. Write back of these amounts has overstated the Revenue Surplus and understated the Fiscal Deficit to this extent. Also the liabilities of the Government have reduced by the equivalent amount in Public Account.

- Any grants released by Government of India (GOI) on the recommendations of the XIII FC were required to be utilised before the award period i.e. 31 March 2015. A mention was made in the report on State Finances for the year ended March 2015 regarding non-utilisation of ₹9.00 crore of XIII FC grants relating to construction of Alternate Dispute Resolution (ADR) centers in 9 districts of the state under Improvement in Justice Delivery. During 2015-16, ₹8.46 crore relating to construction of ADR centers and ₹10.28 crore related to renovation of Heritage buildings released under XIII FC grants were remitted back to the Consolidated Fund of the State. The utilisation certificates for these released amounts have been sent to GOI as per the prescribed format giving the details of the amounts released to various authorities, which were treated as expenditure during those years on the Consolidated Fund of the State. These releases had the effect of overstatement of revenue expenditure and fiscal deficit of those years (during the award period of the XIII FC – 2010-11 to 2014-15). As the amount was remitted back in the current year to the Consolidated Fund, the expenditure stood compressed as also a bearing on the fiscal indicators. The remittance also resulted in the non-achievement of the purpose of the grants made by the Finance Commission.

Finance department clarified (October 2016) that reserve funds *viz.*, IIF and PRI funds by their very nature are expected to cushion fiscal dynamics. If the fiscal position in a year allowed all expenditure to be met from the resources of that fiscal year, then there would be no need to draw down from the Reserve Fund. The observations of the FD have been examined in audit and it is stated that any transfer of revenues to the reserve fund is treated as expenditure on the Consolidated Fund adding up to fiscal deficit. During the period of fiscal stimulus package, moneys were borrowed from the open market and the reserve funds were fed from General Revenues. This transaction created only liability in the Public Account as no investment was made to draw down on the reserves in the current year as stated by the Finance Department. Public Account transactions were utilised to justify the fiscal deficit and borrowings without actual utilisation of borrowed money.

1.1.3 Major Fiscal Variables

Major fiscal variables provided in the budget and targeted in the KFRA, are depicted in **Table 1.3**.

Table 1.3 Major Fiscal variables

	2015-16			
Fiscal variables	**Targets as prescribed in KFRA**	**Targets proposed in the budget**	**Projections made in MTFP (2012-16)**	**Actuals (2015-16)**
Revenue Deficit (-)/ Surplus (+) (₹ in crore)	-	910.64	7,800	1,789
Fiscal Deficit/GSDP (*per cent*)	3.00	2.75	3.00	2.60
Ratio of total outstanding debt of the Government to GSDP (*per cent*)	25.00	24.56	22.13	24.91

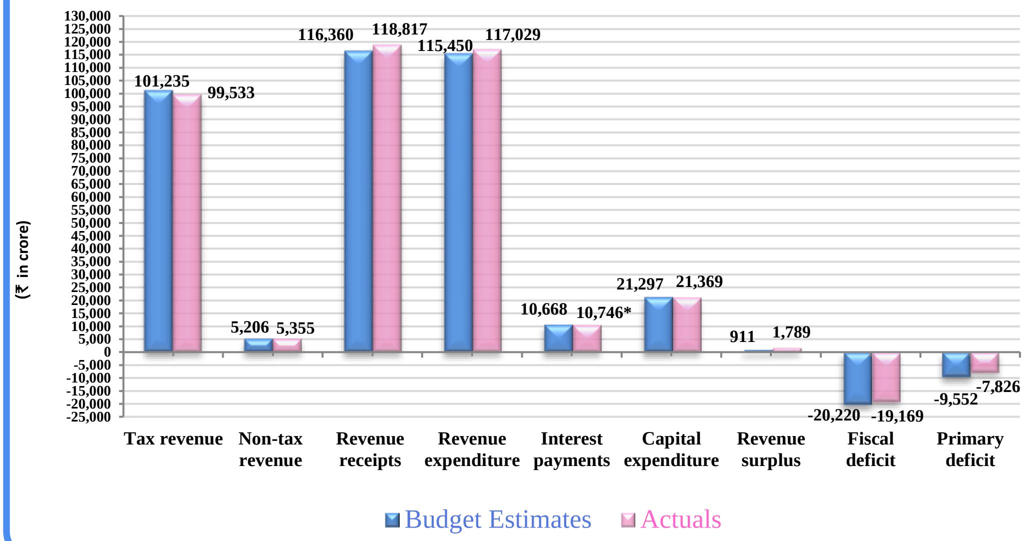
During 2015-16, there was a surplus on revenue account (₹1,789 crore) which exceeded budget projections by ₹878 crore and fell short of MTFP 2012-16 projections by ₹6,011 crore. The ratio of total outstanding debt to GSDP exceeded budget estimates by 0.35 *per cent* and ratio of fiscal deficit to GSDP was 2.60 *per cent*, which fell short of budget projections by 0.15 *per cent*. This was well within the prescribed target as per KFRA.

1.1.4 Budget Estimates and Actuals 2015-16

Budget papers presented by the State Government provide descriptions of projections or estimations of revenue and expenditure for a particular fiscal year. The importance of accuracy in the estimations of revenue and expenditure is widely accepted in the context of effective implementation of fiscal policies for overall economic management. Deviations from budget estimates are indicative of non-attainment/non-optimization of desired fiscal objectives, due to a variety of factors, some of which are within the control of the Government while some are beyond its control.

Chart 1.1 presents the budget estimates and actuals of some important fiscal parameters for the year 2015-16.

Chart 1.1: Selected fiscal parameters: Budget estimates *vis-a-vis* Actuals in 2015-16



Source: Annual Financial Statement and Finance Accounts

**The interest payments are exclusive of Off-budget borrowings.*

Audit observed that the actuals of various fiscal variables were very close to the estimated figures. However, there were substantial variances and savings in budgetary allocations which are explained in detail in **Chapter II**.

The budget estimates envisaged revenue receipts of ₹1,16,360 crore against which the actual realisation was ₹1,18,817 crore, an increase of ₹2,457 crore (2 *per cent*). The increase was mainly under grants-in-aid and contributions from GOI (₹4,010 crore) and Non-Tax revenue (₹149 crore), offset by decrease under Tax revenue (₹895 crore) and Central tax transfers (₹807 crore).

Revenue expenditure was estimated at ₹1,15,450 crore against which the actual expenditure was ₹1,17,029 crore, an increase of ₹1,579 crore (one *per cent*). The increase in the actuals was noticed under economic services (₹1,671 crore) and social services (₹579 crore), off-set by decrease in grant-in -aid and contributions (₹473 crore) and general services (₹198 crore). Further details are available in **Chapter-II** of this report.

Interest payments were estimated at ₹10,668 crore (excluding off-budget borrowings – Borrowings by PSUs and other SPVs from financial institutions, on Government guarantee, where the responsibility of servicing the debt solely lies on the Government) shown against Major Head 2049 - Interest payments. The actual payment was ₹11,816 crore, (exclusive of off-budget borrowings of ₹597 crore). According to the KFRA, 2002 (as amended on 28.02.2014), the interest on off-budget borrowings recorded below various service heads are also to be treated as the interest liability of the State.

Major source of revenue receipts had been the State's own tax revenue which constituted 64 *per cent*. Including the non-tax revenue, the State's own resources were around 68 *per cent* during 2015-16. The variations between budget estimates and actuals together with the reasons for the same under four major tax revenue heads and two non-tax revenue heads are brought out in **Table 1.4**.

Table 1.4: Variation between Budget and Actuals

(₹ in crore)

Source of revenue	Budget Estimate	Actuals	Increase (+) Decrease (-)	Reasons for variations according to MTFP 2016-20
Taxes on sales, trade etc.,	41,329	40,449	(-)880	The growth in tax revenue over the last few years is primarily attributable to the positive response of the tax payers to the extensive computerization programme by the department. However the moderation in growth during 2015-16 is mainly on account of fall in the crude oil prices internationally.
State Excise	15,200	15,333	133	The growth in revenue is from sale of Indian Made Foreign Liquor (IMFL).
Stamps and Registration fees	8,200	8,215	15	Under the Jawaharlal Nehru National Urban Renewal Mission (JnNURM) reforms, there was a commitment by the State to decrease stamp duty to 5 *per cent*. The decreased revenue on account of this move was expected to be made up by increased compliance in registering documents and revision of guidance values.
Motor vehicles tax	4,800	5,002	202	Increase was due to the collection of fees and tax, issue of driving licenses, vehicle registration and issue of permits, which have all been computerized.
Royalty on major and minor minerals	1,815	1,912	97	Due to delay in progress towards operationalisation of mines there was only a marginal increase in collections.
Interest receipts	754	1,293	539	Due to prudent cash management, the interest receipts out of excess cash balance invested in GOI's 91 day Treasury bills yielded more revenue.

Source: Budget documents-2015-16

1.1.5 Gender Budgeting

Gender budget of the State discloses the expenditure proposed to be incurred within the overall budget on schemes which are designed to benefit women fully or partly. The State had created the Gender Budget Cell (January 2007) and gender budgeting was introduced in 2007-08. The year-wise allocations in the gender budget document are detailed in **Table 1.5**.

Table 1.5: Gender budgetary allocations during 2011-12 to 2015-16

(₹ in crore)

Year	Outlay			Expenditure			
	Category A*	Category B^	Total	Category A*	Category B^	Total	Demands covered
2011-12	854.54	30,228.05	31,082.59	1,454.15	34,923.16	36,377.31	27
2012-13	1,509.36	44,647.43	46,156.79	2,643.91	41,026.57	43,670.48	27
2013-14	1,915.30	55,032.21	56,947.51	2,541.78	47,679.24	50,221.02	28
2014-15	3,684.91	66,615.81	70,300.72	3,513.71	50,912.24	54,425.95	28
2015-16#	5,511.20	64,351.38	69,862.58	5,622.65	56,373.56	61,996.21	27

**Budgetary allocations to schemes designed for covering 100 per cent women beneficiaries.*

^Budgetary allocations to schemes designed for covering at least 30 per cent women beneficiaries.

#Figures for 2015-16 are Revised Estimate figures and not actuals.

The total number of schemes under Category A and B in 2015-16 were 774, of which 54 schemes were under Category A and 720 schemes were under Category B. The Gender Budget document also gives a brief explanatory note about the schemes indicating the objective of such schemes.

A review of some of the Category A schemes is brought out in the following paragraphs.

a) Issue of Free bus passes to wife/widows of Freedom Fighters

The scheme is being implemented by Department of Personnel and Administrative Reforms in collaboration with the Transport Department. Under the scheme wife/widows of freedom fighters are issued coupons for ₹2000 every year by Transport Corporations and the beneficiaries are entitled to travel in the State run Transport Corporation buses utilizing the coupons. It was observed that from the year 2009-10 to 2015-16, the budget allocation for the scheme was ₹3.01 crore and the related expenditure was ₹0.31crore. The sanction for the amount claimed towards subsidy by various corporations are being admitted based on the letter/ utilisation certificate, without any pre check.

b) Skill Development and Training for Minority Women

The scheme is being implemented by the Directorate of Minorities. The scheme is aimed at helping minority women to lead an independent life without depending on other training programmes under skill development. The physical targets, achievement and implementation of the scheme from its inception i.e. 2014-15 is brought out in **Table 1. 6** and **Table 1.7.**

Table 1.6: Physical target fixed and achieved

Year	Number of minority women to be trained	Number of minority women actually trained	Shortfall	Percentage of shortfall
2014-15	1,101	924	177	16
2015-16	2,123	1,873	250	12

Table 1.7: Minority women who have taken up employment/self-employment

Year	Number of minority women trained	Number of minority women who got employment after training	Number of minority women who are self-employed	Percentage of women who got employment after training
2014-15	924	340	-	37
2015-16	1,873	665	-	36

Even though the physical targets have been achieved to a large extent, the percentage of minority women who took up employment/self-employment after the skill development and training programme was very low. Concerted efforts need to be made to ensure that a larger percentage of women who successfully completed the training were employed.

1.1.6 Major policy initiatives of Budget 2015-16

The results of scrutiny of records of certain schemes which were proposed for implementation in 2015-16 and the action taken on such proposals in the Departments of Forest, Environment and Ecology and Home are brought out in **Table 1.8**.

Table 1.8: Budget assurances and audit analysis thereon

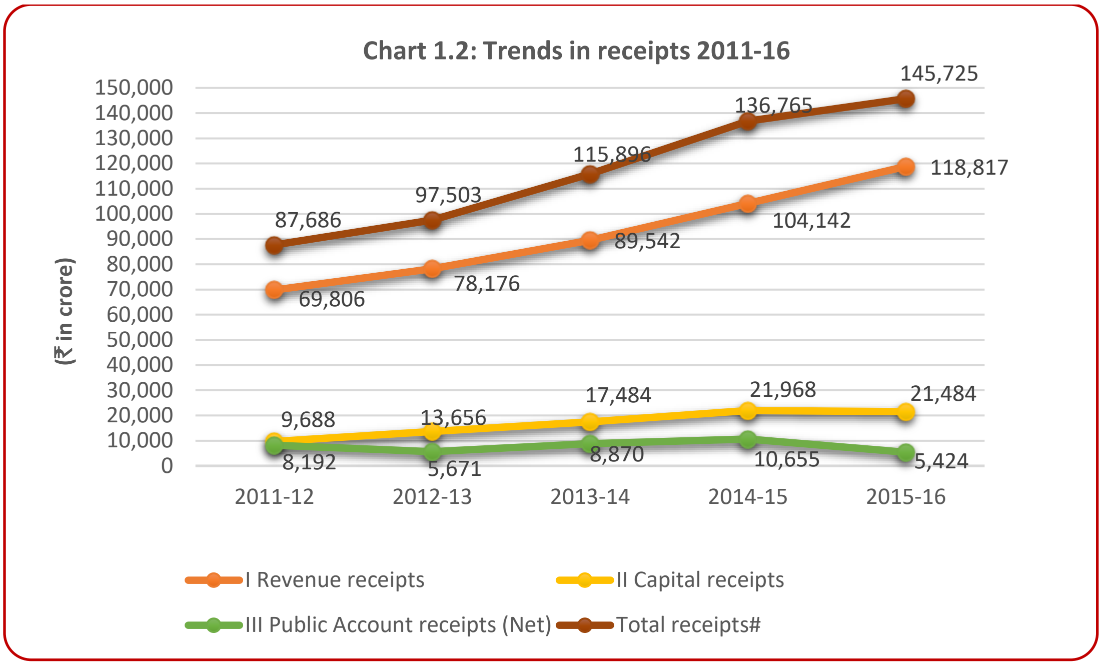
Budget Assurance	Action taken as per Action Taken Report	Audit Observations
It is proposed to establish Rehabilitation Cell to take up a programme of Relocation and Rehabilitation of forest dwellers of Tiger Reserve, Wildlife Sanctuaries and National Parks more effectively.	G.O.No: FEE 89 FAP 2015, dated: 15.07.2015 has been issued.	Proposals submitted by PCCF (February 2016) for the sanction of staff to the Rehabilitation Cell is still under the consideration of the Government (July 2016).
A grant of ₹5.56 crore is provided for the purpose of protection and development of lakes, enhancement of ground water and beautification of the lakes situated in metropolitan areas, by enacting Karnataka Lake Protection and Development Act.	G.O. No: FEE 116 ENV 2015, Dated: 19.01.2016 has been issued.	Out of ₹5.56 crore earmarked for the year 2015-16, the first tranche of ₹2.00 crore was released to Karnataka Lake Development Authority (KLDA) on 28.03.16 i.e. at the fag end of the financial year. The project work is yet to commence and amount remained unutilized with KLDA (July 2016). Reasons for release of money in advance were not available on record.
For the improvement of the health of the Police personnel in the State, ₹9.00 crore will be provided towards annual medical check-up at the rate of ₹1000/- for each personnel. In addition, for providing speedy treatment of Police personnel, the Government will establish 50 outpatient Police Health Centers in different units of the State.	1) G.O.No: HD 296 PoSeEe 2014, dated 15.07.2015 has been issued in this regard. 2) The proposal of establishing 50 Outpatient Police Health Centers is under examination in Administrative Department.	1) Orders have been issued (July 2015) for the provision of annual medical check-up at the rate of ₹1000/- for each police personnel. 2)The Health Department did not agree to the proposal of establishing 50 Outpatient Police Health Centers as the department is facing shortage of staff and also separate medical facilities cannot be provided to a particular class of people or their family.

Budget Assurance	Action taken as per Action Taken Report	Audit Observations
30 new Police Stations including 10 women police stations will be opened in the State for public safety and security.	Finance Department concurred to the proposal and issued endorsement in File No: HD 180 POP 2015, Dated 08.02.2016.	Out of 30 new Police Stations to be opened in the State, notifications were issued for the establishment of 15 new police stations (July 2016 to August 2016) which did not include any women police station.
CCTVs system in 20 district prisons, solar lighting system in 10 important district prisons and telemedicine system in 5 central prisons will be installed.	1) To provide solar lighting system in 10 district prisons, vide G.O. No: HD 347 PRA 2015, dated: 31.10.2015 has been issued. 2) For purchase of CCTV cameras for security arrangement of 20 district jails, proposal was submitted to obtain the approval of the Cabinet in consultation with the Finance Department. 3) The proposal of providing telemedicine system to 5 Central Jails has been decided to be dropped.	Solar lighting system was installed in 4 out of 10 district prisons (June 2016 to August 2016). 2) An amount of ₹400 lakh was released (March 2016) and deposited with Karnataka State Police Housing & Infrastructure Development Corporation (KSPHIDC) (June 2016). The tender process is under progress and the amount was yet to be utilized (August 2016). 3) Based on the report of the Health Department, the performance of the telemedicine system already established in Bengaluru and Belgaum Central jails would be reviewed before being implemented in other 5 Central Jails.
Facility of VAT reimbursement on purchases up to ₹3,000/- per month for each Police Constable will be given on purchases made from Police Canteens.	This proposal is under consideration in Finance Department.	Information regarding the quantity of material sold through police canteen, together with details thereof and the tax on such items were called for from the police department in June 2015. However, there was no information from the department for initiating further action in the matter (August 2016).

1.2 Resource of the State

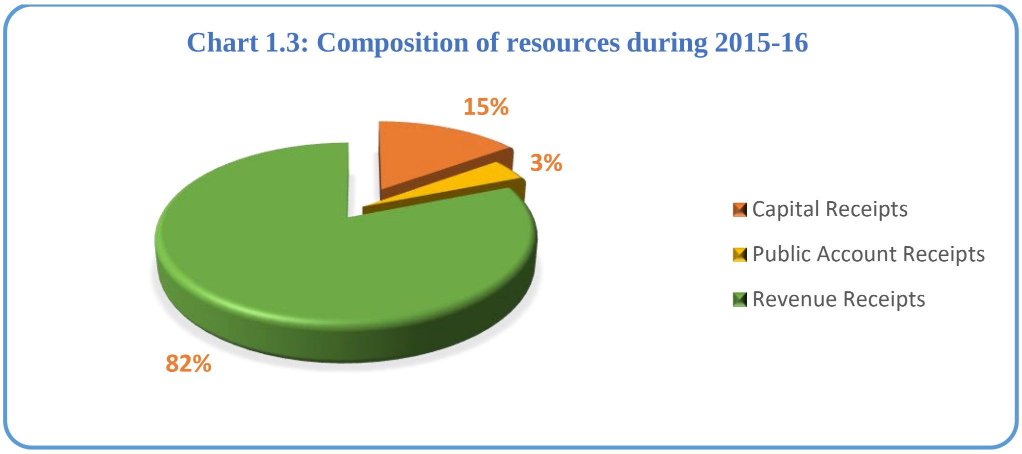
1.2.1 Resource of the State as per the Annual Finance Accounts

Revenue and Capital are the two streams of receipts that constitute the resources of the State Government. Revenue Receipts consist of tax revenues, non-tax revenues, States' share of Union taxes and duties and grants-in-aid and contributions from the GOI. Capital receipts comprise miscellaneous capital receipts such as proceeds from disinvestment, sale of assets, recoveries of loans and advances, debt receipts from internal sources (market loans, negotiated loans from financial institutions/commercial banks, National Small Savings Fund (NSSF) of the Central Government loans from RBI) and loans and advances from GOI. Besides, the net Public Account receipts are also utilised by the Government to finance its deficit. **Chart 1.2** depicts the trends in various components of receipts during 2011-12 to 2015-16.



#excluding Contingency Fund receipts

Chart 1.3 depicts the composition of resources of the State during 2015-16.



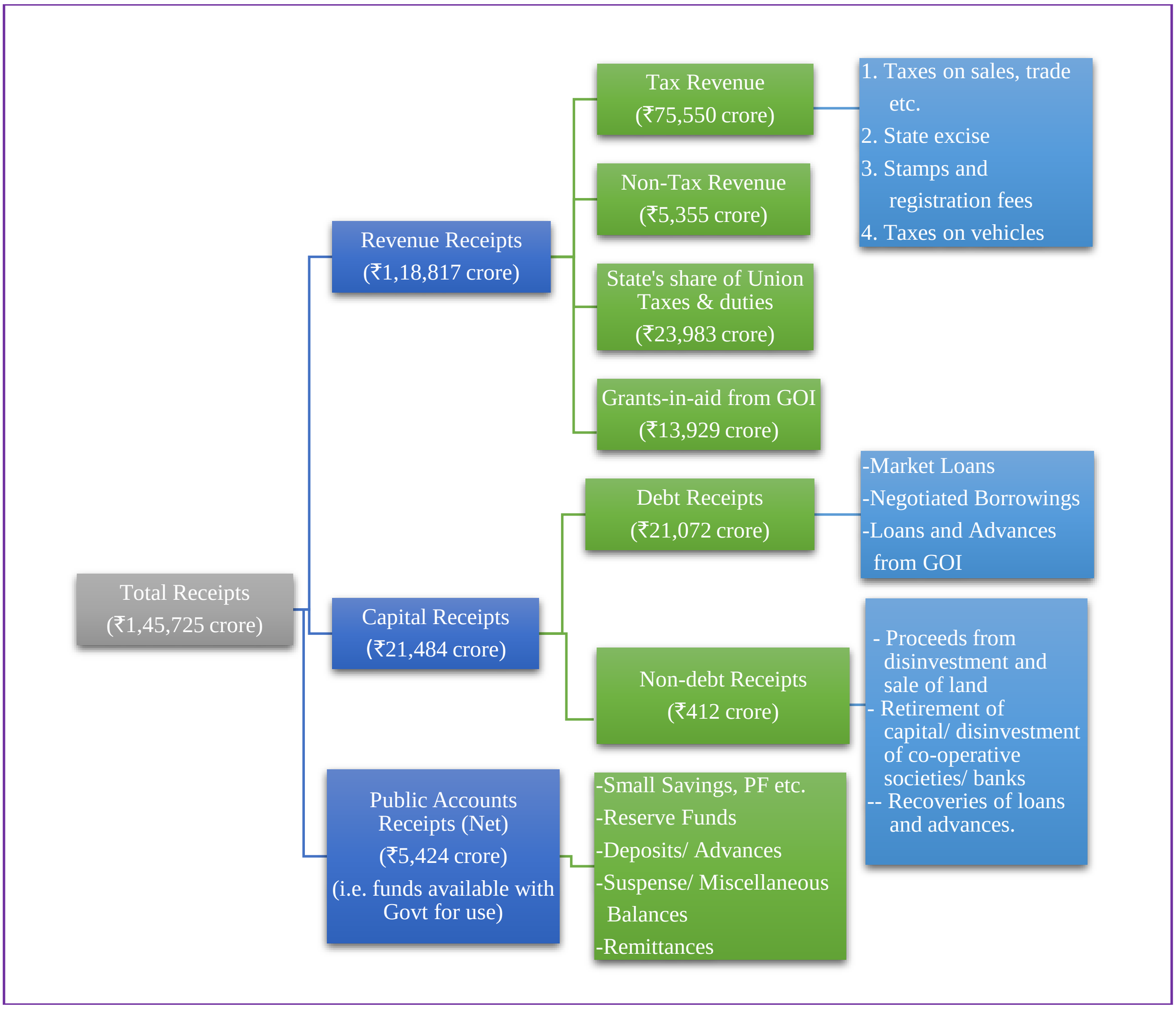
Total receipts (excluding Contingency Fund receipts) increased by 66 *per cent* from ₹87,686 crore in 2011 -12 to ₹1,45,725 crore in 2015 -16. Compared to the previous year, there was an increase by ₹8,960 crore (7 *per cent*) in the current year.

The share of revenue receipts in total receipts during 2015-16 was at 82 *per cent*. Further details are provided in **paragraph 1.3**.

Capital receipts increased by 122 *per cent* from ₹9,688 crore in 2011 -12 to ₹21,484 crore in 2015-16. During 2015-16, the capital receipts accounted for 15 *per cent* of total receipts. Debt receipts, the main constituent of capital receipts, decreased by ₹802 crore. Internal Debt and Loans & Advances from GOI are the two components of debt receipts whose share was 94 *per cent* (₹19,801 crore) and 6 *per cent* (₹1,271 crore) of the total debt receipts (₹21,072 crore) respectively.

Chart 1.4 depicts the components and sub-components of resources of the State during 2015-16.

Chart 1.4: Components and sub-components of Resources



Source: Finance Accounts

In 2015-16, there was a decrease in growth of 3 *per cent* in internal debt receipts. Loans and Advances decreased by 7 *per cent* over the previous year **(Appendix 1.4)**. Apart from debt receipts, capital receipts include non-debt receipts such as recovery of loans and advances and receipts through sale of land, miscellaneous capital receipts & retirement of capital/ disinvestment of co-operative societies/ banks etc. During 2015-16, non-debt capital receipts showed 338 *per cent* growth over the previous year.

Public Account receipts refer to those receipts for which the Government acts as a banker/trustee for the public money. On an average, it constituted 7 *per cent* of the total receipts during 2011-12 to 2015-16. Net Public Account receipts, which totalled to ₹8,192 crore in 2011-12, decreased to ₹5,424 crore in 2015-16.

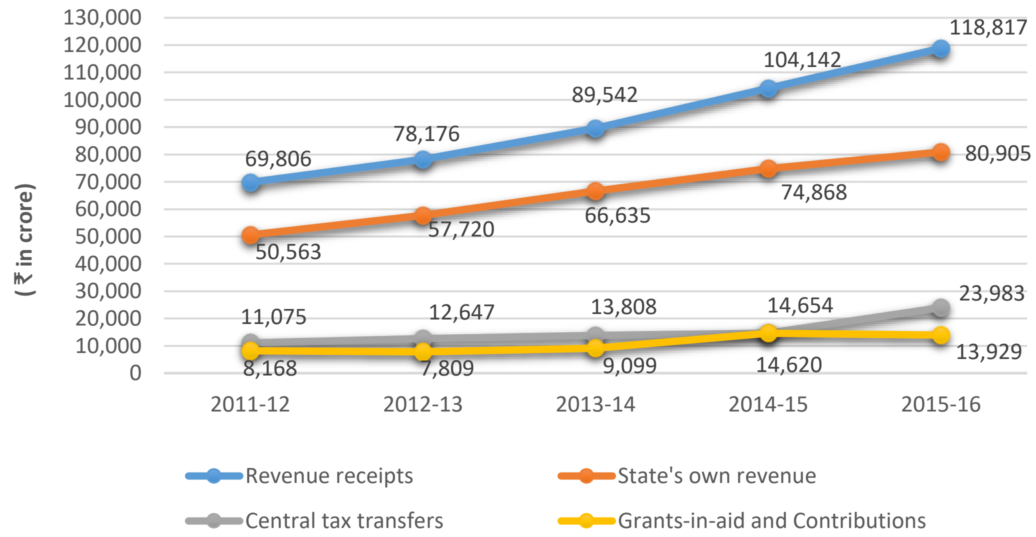
1.3 Revenue Receipts

The Government of Karnataka's fiscal position is largely influenced by the revenue side, as revenue receipts showed progressive increase from ₹69,806 crore in 2011-12 to ₹1,18,817 crore in 2015-16. On an average, 68 *per cent* of the revenue came from State's own resources during the period. The balance was transfers from GOI in the form of State's share of taxes and duties and grants-in-aid and contributions.

Simplification and rationalization of tax structure, along with simplification of process of filing tax returns like E-payment of taxes and anywhere registration has ensured effective mobilization of resources from various taxes which reflected consistent performance on the tax front. Though tax revenues have been consistently growing, Government of Karnataka has not improved revenues on the non-tax front, which hovered between 5 to 6 *per cent* during 2011-12 to 2015-16 which is discussed in detail in **paragraph 1.3.1.2**. The State's Fiscal Reforms and Budget Management Committee has recognized this issue and advised departments to improve their non-tax revenue by regular revision of fees, user charges etc.

Statement No.14 of the Finance Accounts projects the revenue receipts of the Government. The trends and composition of revenue receipts over the period 2011-12 to 2015-16 are presented in **Appendix 1.4** and are also depicted in **Chart 1.5**.

Chart 1.5: Trends in revenue receipts



Source: Finance Accounts

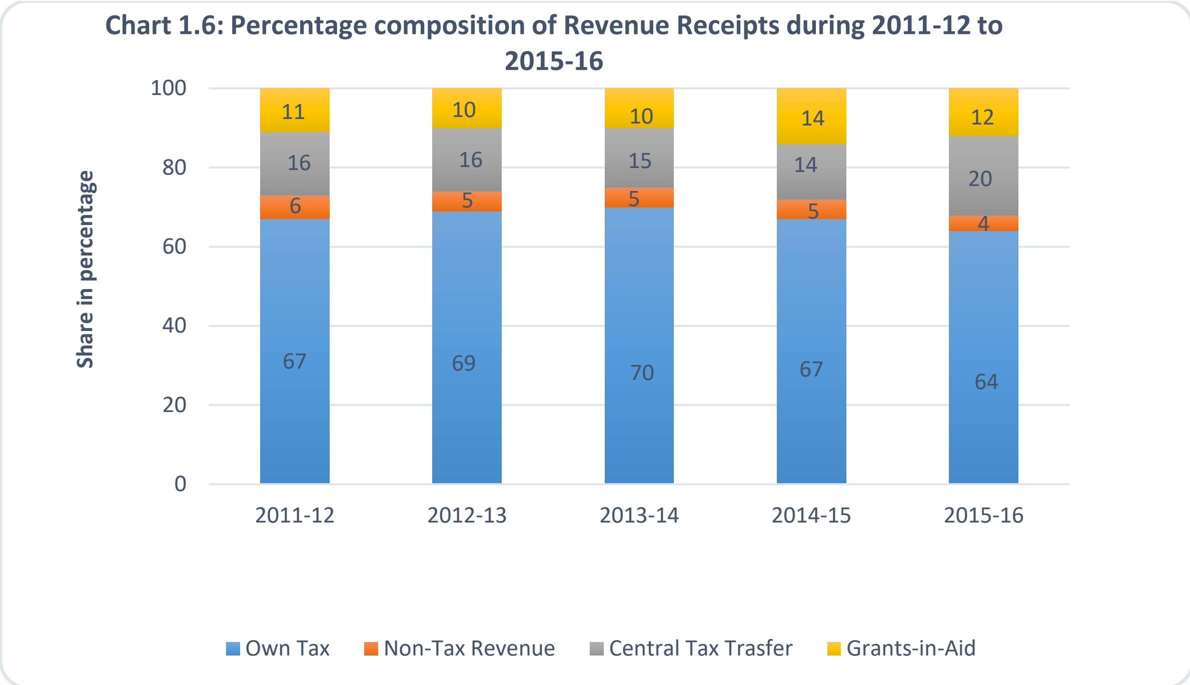


Chart 1.6 depicts that 68 *per cent* of revenue came from State's own resources during 2015-16 and the balance was from GOI in the form of State's share of taxes and Grants-in-aid. The share of own tax revenue increased from 67 *per cent* in 2011-12 to 70 *per cent* in 2013-14 and then decreased to 64 *per cent* in 2015-16. During 2015-16, there was a decrease under grants-in-aid and contributions from GOI. The trends in revenue receipts relative to GSDP are presented in **Table 1.9.**

Table 1.9: Trends in revenue receipts relative to GSDP

	2011-12	2012-13	2013-14	2014-15	2015-16
Revenue Receipts (RR) (₹ in crore)	69,806	78,176	89,542	1,04,142	1,18,817
Rate of growth of RR (*per cent*)	19.9	12.0	14.5	16.3	14.1
Rate of growth of State's own tax (*per cent*)	20.8	15.7	16.5	12.1	7.6
Own tax/GSDP (*per cent*)	10.7	10.3	10.4	10.2	10.3
Buoyancy ratios[1]					
RR/GSDP (*per cent*)	16.1	15.0	14.9	15.2	16.1
Revenue buoyancy w.r.t GSDP	1.4	0.6	0.9	1.2	1.9
State's own tax buoyancy w.r.t GSDP	1.5	0.8	1.1	0.9	1.0
Revenue buoyancy w.r.t States' own taxes	1.0	0.8	0.9	1.3	1.9
GSDP (₹ in crore)	4,34,270	5,20,766	6,01,633	6,85,207	7,35,975
Rate of growth of GSDP	14.0	19.9	15.5	13.9	7.4

Source: Finance Accounts, GSDP: MTFP 2016-20

In the Economic Survey for 2015-16, it was admitted that the ratio of non-tax revenue to total receipts has been continuously declining over the years. Further, the State has one of the lowest non-tax revenues to the GSDP ratios in the country **(Appendix 1.4)**. It hovered around the one *per cent* mark over the

[1]Buoyancy ratio indicates the elasticity or degree of responsiveness of a fiscal variable with respect to a given change in the base variable. For instance, revenue buoyancy at 0.4 implies that revenue receipts tend to increase by 0.4 *percentage* points, if the GSDP increases by one *per cent.*

past three years. This is due to the low recovery of costs. In many departments, the revision of user charges, fees & fines and other such non-tax receipts have not taken place for many years. Even with revision of rates and better collection mechanisms, increase in revenues from this avenue may not be large due to existing low base. Though Expenditure Reforms Commission has made a number of recommendations during 2010 to enhance revenues from user charges, the same has not been accomplished. In reply the Government stated that instructions have been issued (September 2016) to give information relating to user charges that are being collected.

1.3.1 State's own resources

The tax revenue of the State in 2015-16 was less than the projection made in MTFP by ₹5,607 crore and budget estimates by ₹895 crore. Non-tax revenue was significantly more than the MTFP projections (₹1,724 crore) and budget estimates by ₹149 crore, as detailed in **Table 1.10** below.

Table 1.10: Projections of Tax and Non-tax Revenue

(₹ in crore)

	Budget estimates	MTFP projections	Actual
Tax revenue	76,445	81,157	75,550
Non-tax revenue	5,206	3,631	5,355

1.3.1.1 Tax revenue

Taxes on sales, trade, etc., (54 *per cent*) were the main source of the State's tax revenue followed by State Excise (20 *per cent*), Stamps and Registration Fees (11 *per cent*) and Taxes on Vehicles (7 *per cent*) during 2015-16. The trends in the major constituents of tax revenue during the period 2011-12 to 2015-16 are shown in **Table1.11** and **Chart 1.7** below.

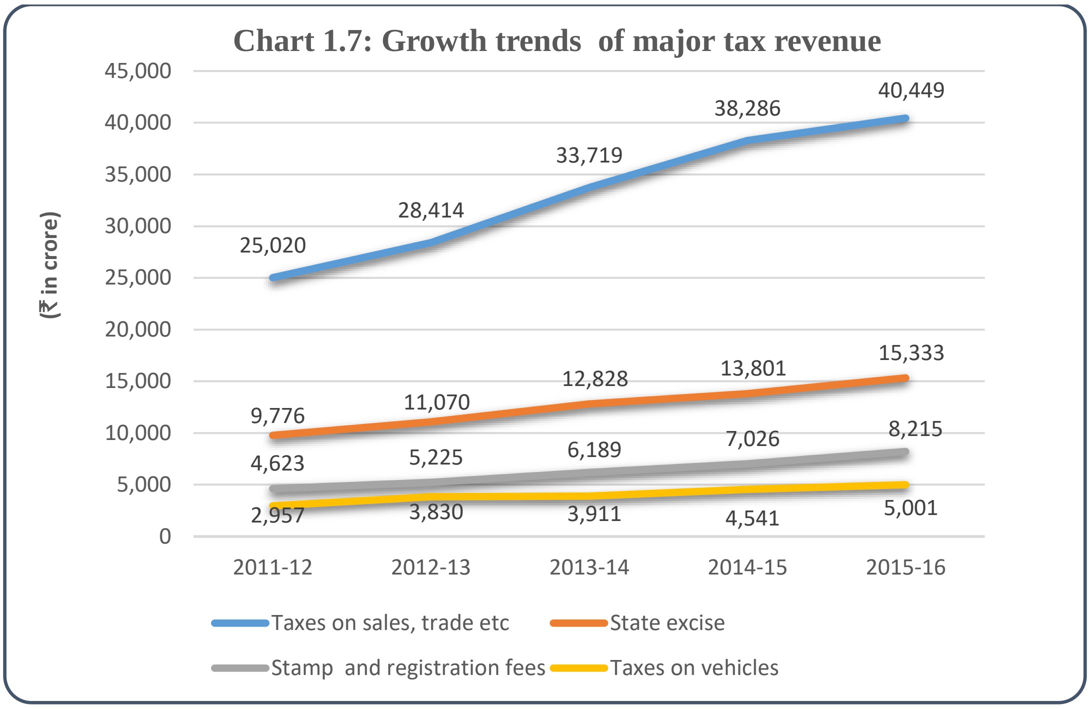
Table 1.11: Components of State's own tax revenue

(₹ in crore and growth rate in *per cent*)

Revenue Head	2011-12	2012-13	2013-14	2014-15	2015-16
Taxes on sales, trade etc.,	25,020	28,414	33,719	38,286	40,449
Rate of growth	23.65	13.57	18.67	13.54	5.65
State excise	9,776	11,070	12,828	13,801	15,333
Rate of growth	18.00	13.24	15.88	7.58	11.10
Stamp and Registration fees	4,623	5,225	6,189	7,026	8,215
Rate of growth	30.93	13.02	18.45	13.52	16.92
Taxes on vehicles	2,957	3,830	3,911	4,541	5,001
Rate of growth	15.96	29.52	2.11	16.11	10.13
Land revenue	215	205	199	186	181
Rate of growth	20.79	(-)4.65	(-)2.93	(-)6.53	(-)2.69
Taxes on goods and passengers	1,690	2,181	2,626	3,038	3,125
Rate of growth	10.75	29.05	20.40	15.69	2.86
Other taxes[2]	2,195	2,829	3,131	3,302	3,246
Rate of growth	1.2	28.88	10.68	5.46	(-)1.70
Total	**46,476**	**53,754**	**62,603**	**70,180**	**75,550**

Source: Finance Accounts of the respective years

[2]Other taxes include taxes on Agricultural Income, taxes and duties on Electricity, Other taxes on Income and Expenditure and other taxes and duties on Commodities and Services.



During the period 2011-12 to 2015-16, the rate of growth of taxes on sales, trade, etc., was between 5.65 *per cent* and 23.65 *per cent*. During 2015-16, the growth rate was 6 *per cent*. The moderation in growth rate was mainly on account of reduction in crude oil prices internationally.

State Excise, was the second largest contributor to State's own tax revenues. The strict enforcement of excise law and increased intensive patrolling and surveillance on manufacturing and selling units by the department has led to a healthy growth of revenue from sale of IMFL over the years. The growth rate was between 7.58 *per cent* and 18.00 *per cent* during 2011-12 to 2015-16.

Stamp and Registration fees also contributed to own tax revenues. There was a moderation in the growth rate during the years 2011-12 to 2015-16 due to decrease in the stamp duty to 5 *per cent.* During 2015-16, it stood at 16.92 *per cent* and efforts need to be made to ensure that collections are improved.

Motor vehicle taxes also contribute significantly to own tax revenues. The computerization in transport department has contributed towards better collection of fees and tax payment. The growth rate of revenue under the head was 2.11 *per cent* during 2013-14, which increased to 16.11 *per cent* during 2014-15 and was 10.13 *per cent* during 2015-16.

Cost of Collection

The gross collection of taxes on motor vehicles, taxes on sales, trade etc., stamp and registration fees and State excise, expenditure incurred on their collection and its percentage to gross collection during the years 2013-14 to 2015-16 along with their All-India average cost of collection for the respective previous years are indicated in the **Table 1.12.**

Table 1.12: Cost of collection

Receipt	Year	Gross collection	Expenditure on collection	Percentage of cost of collection to gross collection	All India average percentage for the preceding year
		(₹ in crore)			
Motor vehicles	2013-14	3,913.64	90.88	2.32	4.17
	2014-15	4,544.17	82.52	1.82	NA
	2015-16	5,004.35	83.18	1.66	NA
Taxes on sales, trade etc.,	2013-14	35,096.71	1,238.94	3.53	0.73
	2014-15	39,694.76	1,464.43	3.69	NA
	2015-16	41,891.72	250.47	0.60	NA
Stamp and registration fees	2013-14	6,240.21	86.92	1.39	3.25
	2014-15	7,063.35	68.28	0.96	NA
	2015-16	8,241.07	126.03	1.53	NA
State Excise	2013-14	12,833.71	110.57	0.86	2.96
	2014-15	13,805.75	130.11	0.94	NA
	2015-16	15,337.11	132.61	0.86	NA

The percentage of cost of collection to the gross collection was significantly less than the All India Average for the year 2013-14, except for 'taxes on sales, trade etc.'

Improper accounting and Non-Utilisation of Green Tax cess collections of ₹45.90 crore

Honourable Chief Minister in his Budget speech on 21 March 2002 for the year 2002-2003 proposed that "As a measure to contain air pollution, it is decided to levy 'Green Tax cess' on old vehicles at the rate of ₹250 for two wheelers and ₹500 for other Non-transport vehicles which have completed fifteen years at the time of renewal of Certificate of Registration. Further, ₹200 per annum will be collected in respect of transport vehicles which have completed seven years. Necessary amendments will be effected in the Karnataka Motor Vehicles Taxation Act, 1957. The amount will be earmarked for implementation of various pollution control measure."

Accordingly, The Karnataka Vehicles Taxation (Amendment) Act, 2002 was enacted (March 2002), wherein under section 3B of the said Act, the levy of a cess called 'Green Tax' at the rates mentioned above was proposed with effect from 01.04.2002.

During the Performance Audit on the 'Levy and collection of Motor Vehicles Taxes' by the Office of the AG (E&RSA), Karnataka, it was noticed on scrutiny of records in 20 RTOs/ARTOs that Green Tax cess collected is being accounted for under HOA '0041-00-102-0-01' ('Taxes on Motor Vehicles – Receipts under State Motor Vehicles Taxation Act' – 'Vehicles and Service Tax') while in a few cases, the revenue is being accounted for under the Head '0041-00-800-0-02' (Other Receipts) indicating non-uniformity in accounting of such transactions. The accounting mechanism did not distinguish green tax cess receipts from others, since there was no specific detailed head for accounting of the above cess and the budget documents did not show this element of revenue separately. In the absence of proper accounting mechanism, the department was not able to identify the total collection of Green Tax cess and its use for the intended purpose. Further, no rules were framed for administration and accounting of Green Tax cess so far. The year wise (2006-07 to 2014-15) Green Tax cess collected as furnished by the department (₹45.90 crore) is summarised in the **Table 1.13.** The information for the year 2015-16 was not furnished till date (December 2016).

Table 1.13: Green Tax cess collections

(₹ in crore)

Year	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	Total
Green Tax collected	3.65	3.81	3.95	4.30	5.17	5.73	5.92	6.59	6.78	**45.90**

In its reply, the Transport Department had stated (July 2016) that a separate HOA'0041-00-102-0-11' Green Tax cess has been opened as of 2016-17 to account for green tax cess collections and utilized for prevention of air pollution through various programmes. The reply of the department is not satisfactory as there was no data relating to its collection/expenditure for the period from 2002-03 to 2005-06 and a separate HOA was created after a lapse of 13 years. The expenditure incurred was meagre which ranged from 0.25 *per cent* to 3.31 *per cent* of the total green tax collected during 2008-09 to 2014-15. Also no concrete action plan had been made for utilisation of the funds towards air pollution control measures.

Finance Department in its reply (December 2016) stated that the accounting procedure is being put in place by opening a separate fund head in Public Account to account for the green tax cess. It was also stated that the expenditure heads and the contra debit head have also been identified for incurring expenditure and its eventual shifting to the fund head and that orders in that regard were being issued.

1.3.1.2 Non-tax revenue

Non-tax receipts (fees, user charges, interest receipts, etc.) are generally raised through non-statutory mandates and usually a reciprocal benefit accrues to the citizens from whom such receipts are collected. The sources of non-tax receipts included receipts from fiscal services like interest receipts from outstanding advances, dividends and profits from equity investments, royalty fees for allowing use of assets held as custodian like minerals, forests and wild life, or other such services and user charges for various social and economic services provided through the apparatus of the Government. The trend in collection of non-tax revenue under certain important heads of accounts is given in **Table 1.14.**

Table 1.14: Trends in collections of non-tax revenues

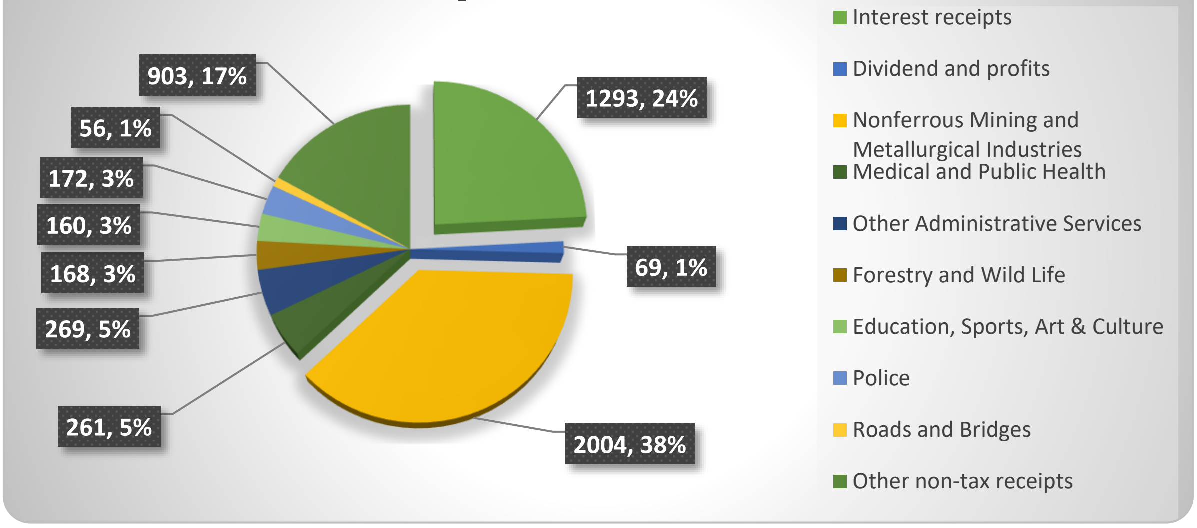
(₹ in crore)

Revenue Head	2011-12	2012-13	2013-14	2014-15	2015-16	% increase (+)/ decrease (-) over previous year
Interest receipts	434.23	778.55	693.17	874.74	1,292.63	47.77
Dividend and profits	60.56	56.29	55.49	74.84	69.40	(-)7.27
Nonferrous Mining and Metallurgical Industries	1,326.84	1,496.49	1,474.49	1,931.10	2,003.80	3.76
Medical and Public Health	87.82	100.70	207.54	224.00	260.74	16.40
Other Administrative Services	117.79	123.37	181.66	179.23	269.08	50.13
Forestry and Wild Life	168.32	171.54	161.14	178.21	168.15	(-)5.65
Education, Sports and Culture	130.58	148.73	120.09	154.96	159.72	3.07
Police	118.26	110.84	150.71	152.07	171.87	13.02
Roads and Bridges	95.60	119.49	120.14	118.38	56.11	(-)52.60
Other non-tax receipts	1,546.86	860.11	867.47	800.71	903.54	12.84
Total	**4,086.86**	**3,966.11**	**4,031.90**	**4,688.24**	**5,355.04**	**14.22**

Source: Finance Accounts

The components of non-tax revenue for the year 2015-16 are presented in **Chart 1.8**.

Chart 1.8: Components of non-tax revenue in 2015-16



Interest receipts, Dividends and Profits

Apart from the regular source of interest receipts on account of repayment of loans, the other major source is interest proceeds out of investment of surplus cash balance of the State. As per RBI's regulations, the cash balance maintained by the State is invested in GOI's 14 day Treasury Bills (TBs). To improve cash management, excess cash balance (beyond the immediate requirement) is invested in GOI's 91 day TBs. Against the budgeted estimate of ₹754 crore during 2015-16, the revenue realized was ₹1,028.15 crore, of which 14 day TBs yielded ₹330.65 crore and 91 day TBs yielded ₹697.50 crore.

The interest realized on loans and advances given by the Government to its Companies/Corporations etc. stood at ₹263.68 crore, working out to 2 *per cent* of the outstanding balances of loans at the end of the year. The receipts also included ₹0.83 crore, being the interest on capital of departmentally run commercial undertakings, such as Silk Filatures, the adjustments of which were made through book transfer.

The return on investment in the form of dividends declared by the Companies/Corporations and credited to Government account during 2015-16 was ₹69.40 crore. Considering the magnitude of Government investment (₹61,356 crore), the return works out to a meager 0.11 *per cent*.

Other Non-tax receipts

The other major non-tax revenue is royalty on major and minor minerals. Against the Budget estimates of ₹1,815 crore, the actual realization was ₹1,912 crore.

1.3.2 Grants-in-aid from GOI

Grants-in-aid and Contributions from GOI increased from ₹8,168 crore in 2011-12 to ₹13,929 crore in 2015-16 as shown in **Table 1.15**.

Table 1.15: Grants-in-aid from GOI

(₹ in crore)

Particulars	2011-12	2012-13	2013-14	2014-15	2015-16
Non-Plan grants	2,129.42	2,455.43	3,139.79	3,634.58	5,547.34
Grants for State Plan schemes	3,626.00	2,908.74	3,341.15	9,096.87	8,105.31
Grants for Central Plan schemes	76.14	124.59	191.70	158.52	138.90
Grants for Centrally sponsored schemes	2,336.85	2,320.66	2,426.18	1,729.48	137.20
Grants for special plan schemes	-	-	-	-	-
Total	**8,168.41**	**7,809.42**	**9,098.82**	**14,619.45**	**13,928.75**
% of increase/decrease over previous year	18.93	(-) 4.39	16.51	60.67	(-)4.72
Total grants as % of revenue receipts	11.70	10.00	10.16	14.04	11.72

Source: Finance Accounts

As compared to the previous year, there was a decrease of ₹691 crore during 2015-16. This was on account of decrease in Grants for State Plan Schemes (₹992 crore), Grants for Central Plan schemes (₹20 crore) and Centrally

Sponsored Schemes (CSS) (₹1,592 crore), offset by increase in receipts under Non-plan grants (₹1,913 crore).

Due to transfer of central share of Centrally Sponsored Schemes directly to the Consolidated Fund of the State, these central shares were also available under State Budget.

1.3.3 Central tax transfers

The XIV FC had recommended that the State's share of Central Taxes be increased to 42 *per cent* from 32 *per cent* as recommended by XIII FC. The State's share in the net proceeds of Central Taxes (excluding Service Tax) and net proceeds of Service Tax had been fixed at 4.713 and 4.822 *per cent*, respectively. The share of Union taxes received during 2015-16 was ₹23,983 crore. There is an increase of ₹9,329 crore over the previous year under Corporation Tax (₹2,430 crore), Service Tax (₹1,993 crore), Union Excise duties (₹1,844 crore), Taxes on Income other than Corporation Tax (₹1,598 crore), Customs Duty (₹1,460 crore), Other taxes and duties on Commodities and Services (₹16.13 crore), Other taxes on Income and Expenditure (₹0.03 crore), offset by decrease in share of Wealth Tax (₹12.16 crore).

1.3.4 Optimization of XIV Finance Commission (XIV FC) Grants

1.3.4.1 Introduction

The XIV FC was constituted by the President under Article 280 of the Constitution on 2 January 2013 to make recommendations on specified aspects of Centre State Fiscal relations for the period from 2015-16 to 2019-20 (award period). As per the terms of reference, the commission shall make recommendations in the matter of distribution of net proceeds of taxes between the Union and the States, principles which should govern the grants-in-aid of the revenues of the States and measures needed to augment the Consolidated Fund of the State to supplement the resources of the Panchayat and Municipalities in the State.

1.3.4.2 Comparison of Devolution of Union Taxes and duties

The XIII FC had recommended that the State's share of net proceeds of all shareable Union Taxes and Duties be increased to 32 *per cent* from 30.50 *per cent* as recommended by the XII FC during its award period of 2010-11 to 2014-15 and the State's share in the net proceeds of Central Taxes (excluding Service Tax) and net proceeds of Service Tax had been fixed at 4.33 and 4.40 *per cent* respectively. The recommendations of the XIV FC with regard to the devolution of Union Taxes and duties are discussed in **paragraph 1.3.3** above. A comparison of the devolution of Union Taxes and duties during the last year of award period of XIII FC and first year of award period of XIV FC is brought out in the **Table 1.16.**

Table 1.16: Share of net proceeds of Union Taxes and Duties during 2014-15 and 2015-16

(₹ in crore)

Nature of Tax	2014-15	2015-16	Difference	Increase (+)/ decrease(-) in *per cent*
Corporation Tax	5,117.21	7,547.57	2,430.36	(+)47
Taxes on Income other than Corporation Tax	3,654.18	5,252.47	1,598.29	(+)44
Service Tax	2,160.75	4,153.56	1,992.81	(+)92
Taxes on Wealth	13.81	1.65	(-)12.16	(-)88
Customs	2,369.95	3,830.22	1,460.27	(+)62
Union Excise Duties	1,338.24	3,181.60	1,843.36	(+)138
Other Taxes and Duties on Commodities and Services	(-)0.01	16.12	16.13	-
Other Taxes on Income and Expenditure	0.12	0.15	0.03	(+)25
Total	**14,654.25**	**23,983.34**	**9,329.09**	**(+)64**

There had been a significant increase in the State's share in the net proceeds of Union Taxes and duties under Union Excise duties (138 *per cent*), Service Tax (92 *per cent*) and Customs duty (62 *per cent*) during the first year of the award period of the XIV FC as compared to the last year of the award period of the previous Finance Commission.

1.3.4.3 Release of Grants

The State Government had received ₹1,741.44 crore during 2015-16 as transfer to the State and a comparison of the grants released during the last year of award period (2014-15) of XIII FC is indicated in **Table 1.17.**

Table 1.17: Comparison of release of grants during 2014-15 and 2015-16

(₹ in crore)

Sl. No.	Transfers	Release as per XIII FC during 2014-15	Recommendation of XIV FC	Release as per XIV FC during 2015-16	Increase/ Decrease over previous year	Percentage of increase(+)/ decrease(-)
1	Local Bodies					
(a)	Basic Grants to PRIs	753.04	1002.85	972.36	219.32	29
(b)	Basic Grants to ULBs	333.02	562.08	562.08	229.06	69
2	Disaster Relief	146.74	249.00	207.00	60.26	41
	Total	**1,232.80**	**1,813.93**	**1,741.44**	**508.64**	**41**

As of March 2016, the State Government received ₹972.36 crore of Basic Grants for PRIs against the recommendation of ₹1,002.85 crore which is ₹219.32 crore (29 *per cent*) more over the previous year. Basic grants to ULBs showed an increase of ₹229.06 crore over the previous year, an increase of 69 *per cent*. The release of Performance Grants to PRIs and ULBs will commence from the 2nd year of award period i.e. 2016-17. The State Government (RDPR department and UDD) has issued guidelines to arrive at entitlement of the PRIs and ULBs with regard to the operational criteria to obtain Performance Grants under XIV Finance Commission.

Similarly, against the recommended amount of ₹249 crore towards State Disaster Relief Fund (SDRF), only ₹207 crore was released, an increase of ₹60.26 crore (41 *per cent*) over the previous year. The contributions from GOI together with the State's contribution are transferred to the SDRF account in Public Account of the State. An equivalent amount is also shown as expenditure met out of the Fund during the award period. However, the expenditure shown as incurred out of the fund, is not the real expenditure, but these releases were made to the Deputy Commissioners (DCs) of the districts to meet subsequent expenditure. The unspent balances remaining with the DCs are not readily ascertainable as the transactions under the calamity fund maintained by the DCs take place in the deposit account in Public Account. Audit observed that in respect of 9 Deputy Commissioners from whom the details were obtained, there remained ₹144.29 crore unspent balance under the calamity fund. Thus the charging of entire expenditure to the fund expenditure lacks transparency.

During 2015-16, the XIV FC has not recommended for release of any Improving Outcome Grants, State Specific Grants or grants towards Elementary Education, Roads and Bridges and Environment related funds. The XIV Finance Commission in its recommendation stated that health, education, drinking water and sanitation are considered as public services of national importance, having significant inter-state externalities. Therefore, the grants to these sectors should be carefully designed and implemented and an effective monitoring mechanism put in place with the involvement of the Union Government, State Governments and domain experts. As such the commission has desisted from recommending specific-purpose grants and suggested that a separate institutional arrangement be introduced for the purpose.

Finance Department replied (December 2016) that since there was no cash support for improving outcome grants etc., institutional arrangements for the purpose have not been implemented. It was further stated that the departments have their own regular monitoring system for their programmes.

1.3.5 Foregone revenue

As per the requirements under Section 5(2) (c) of the KFRA, additional statements are brought out in the MTFP 2016-20 detailing the tax expenditure/revenue foregone by exemption or deferment of VAT, CST and Entry Tax. The details of such exemptions/revenue foregone during the years 2014-15 to 2015-16 are indicated in **Table 1.18**.

Table 1.18: Details of exemptions/revenue foregone

(₹ in crore)

Particulars	2014-15	2015-16#
Tax expenditure/revenue foregone under deferment of purchase tax on sugarcane	34.19	19.32
Exemption/deferment/re-imbursement of tax	652.57	423.33
Total	**686.76**	**442.65**

Source: MTFP 2016-20

#for the first three quarters of 2015-16

Though the Public Accounts Committee (PAC) in its 13th Report, while recommending a system to oversee the collection of revenue had suggested to the State Government to discontinue the practice of giving discounts, waivers and exemptions while collecting taxes, the State Government had failed to adhere to the same.

However, Government contended that the tax concessions in the form of waiver/discount/exemptions are conscious decisions taken by the State as a matter of policy for promoting certain sectors of the economy. Such concessions are provided with the objective of enabling a conducive environment to attract more industries to the State. It has other benefits of providing employment to locals and boosting the economy. It is expected that it will ultimately compensate the revenue foregone by way of improvements in overall tax collection and faster growth of GSDP.

1.4 Capital Receipts

Capital receipts of the State Government include non-debt and debt receipts, whose composition has been discussed in **paragraph 1.2.1**. The Public Debt receipts during 2015-16 (₹21,072 crore) comprised internal debt of ₹19,801 crore (94 *per cent*) and Loans and Advances from GOI ₹1,271 crore (6 *per cent*). Market borrowings had a predominant share under internal debt, comprising 82 *per cent* followed by NSSF loans (14 *per cent*) and negotiated loans (4 *per cent*). Loans from GOI comprised Plan loans only. The trends in composition of capital receipts during the period 2011-12 to 2015-16 are indicated in **Table 1.19**.

Table 1.19: Trends in growth and composition of capital receipts

(₹ in crore and growth rate in *per cent*)

Sources of State Capital receipts	2011-12	2012-13	2013-14	2014-15	2015-16
Capital Receipts (CR)	9,688	13,656	17,484	21,968	21,484
Misc. Capital Receipts	89	33	88	10	352
Recovery of Loans and Advances	241	158	109	84	60
Public Debt receipts	9,358	13,465	17,287	21,874	21,072
Rate of growth of debt capital receipts	39.38	43.89	28.38	26.53	(-)3.67
Rate of growth of non-debt capital receipts	41.63	(-) 42.12	3.14	(-) 52.28	338.30
Rate of growth of GSDP	14.02	19.92	15.53	13.89	7.41
Rate of growth of capital receipts (%)	39.46	40.96	28.03	25.65	(-)2.20

Overall, capital receipts increased from ₹9,688 crore in 2011-12 to ₹21,484 crore in 2015-16. Debt receipts had a predominant share in capital receipts which were between 97 and 98 *per cent* during 2011-12 to 2015-16. The recovery towards loans and advances was very meager during the period. Recovery amounted to less than one *per cent* of the outstanding loans and advances as at the end of 2015-16. It also included book adjustment of ₹15.18 crore being the dues of Electricity Supply Companies (ESCOMs), treated as subsidy on revenue account.

1.5 Public Account Receipts

Receipts and disbursements in respect of certain transactions, such as Small Savings, Provident Fund, Reserve Funds, Deposits, Suspense, Remittances etc., which do not form part of the Consolidated Fund are kept in the Public Account set up under Article 266(2) of the Constitution and are not subject to vote by the State Legislature. Here, the Government acts as a banker/trustee for custody of public money, since these transactions are mere pass through transactions. The net transactions under Public Account covering the period 2011-12 to 2015-16 are indicated in **Table 1.20**.

Table 1.20: Net transactions under Public Account

(₹ in crore)

Resources under sectors of Public Account (Net)	2011-12	2012-13	2013-14	2014-15	2015-16
I. Small Saving, PF etc.,	1,398	1,732	3,107	2,156	2,086
J. Reserve Funds	2,761	1,362	1,264	1,547	2,081
K. Deposits and Advances	1,410	2,511	2,840	3,702	284
L. Suspense and Misc.	2,634	98	2,671	3,282	990
M. Remittances	(-) 11	(-) 32	(-) 12	(-) 32	(-)17
Total	**8,192**	**5,671**	**8,870**	**10,655**	**5,424**

The net receipts from Public Account decreased from ₹8,192 crore in 2011-12 to ₹5,424 crore (34 *per cent*) in 2015-16. Net availability of funds under Small Savings, Provident Fund, and Reserve Funds had a predominant share in financing the fiscal deficit. Under Suspense and Miscellaneous, there was decrease in transactions relating to un-encashed cheques which amounted to ₹996 crore during 2015-16. An analysis of the transaction is brought out in **paragraph 1.8.6**.

1.6 Application of resources

Analysis of the allocation of expenditure at the State Government level assumes significance since major expenditure responsibilities 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 the expenditure directed towards development of social and economic sectors.

Prudent fiscal management should aim at creating savings by raising revenue receipts in excess of revenue expenditures. The revenue balance is called Government's saving, which is used to finance capital expenditure. Use of borrowed funds for either directly revenue yielding activities or indirectly productive uses creates returns by way of tax or non-tax revenues which can be used for debt servicing and repayment of loans.

1.6.1 Growth and composition of expenditure

The basic parameters of total expenditure, growth rate and comparison with GSDP etc., are furnished in the **Table 1.21**.

Table 1.21: Total expenditure – Basic parameters

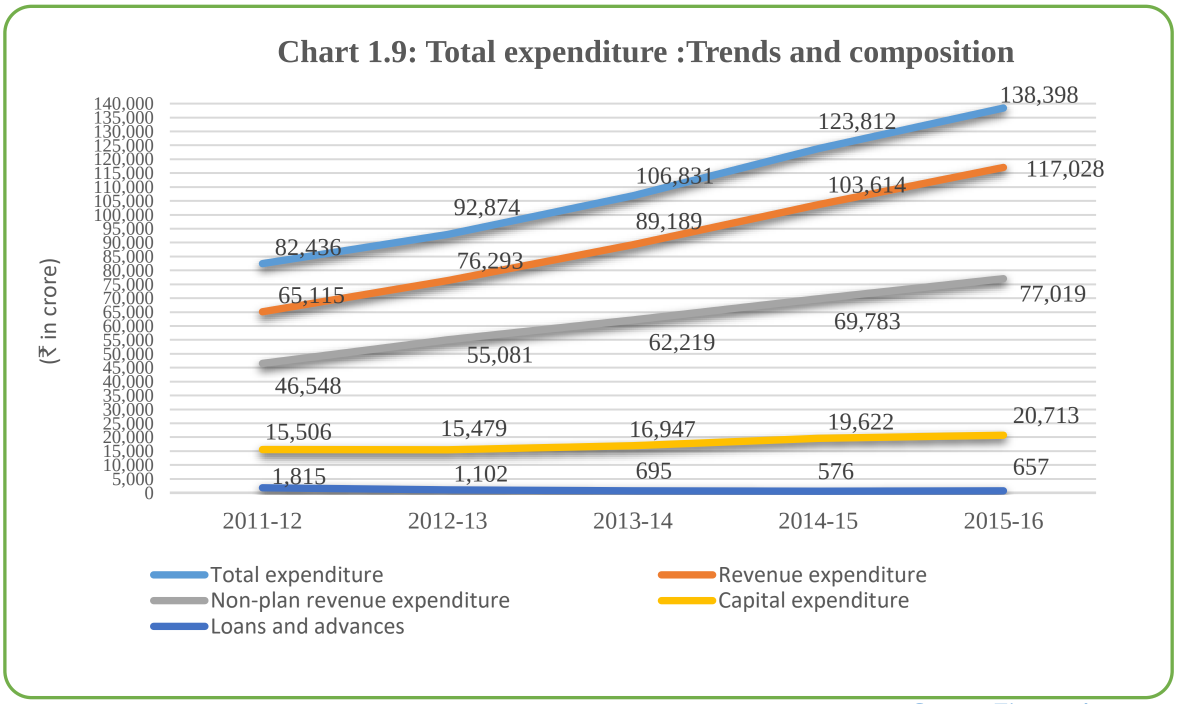
(₹ in crore and growth rate in *per cent*)

	2011-12	2012-13	2013-14	2014-15	2015-16
Total Expenditure (TE)*	82,436	92,874	1,06,831	1,23,812	1,38,398
Rate of growth	19.2	12.7	15.0	15.9	11.8
GSDP	4,34,270	5,20,766	6,01,633	6,85,207	7,35,975
Rate of growth	14.02	19.92	15.53	13.89	7.41
TE/GSDP	18.98	17.83	17.76	18.07	18.80
Revenue receipts/TE	84.7	84.2	83.8	84.11	85.85
Revenue expenditure	65,115	76,293	89,189	1,03,614	1,17,028
Rate of growth	20.5	17.2	16.9	16.2	12.9
Capital expenditure (including loans and advances)	17,321	16,581	17,642	20,198	21,370
Rate of growth	14.8	(-) 4.3	6.4	14.5	5.8
Buoyancy of total expenditure with GSDP					
GSDP	1.4	0.6	1.0	1.1	1.6
Revenue receipts	1.0	1.1	1.0	1.0	0.8
Buoyancy of revenue expenditure with					
GSDP	1.5	1.0	1.1	1.2	1.7
Revenue receipts	1.0	1.4	1.2	1.0	1.0

Source: Finance Accounts

**Total expenditure includes revenue expenditure, capital expenditure including loans and advances*

Chart 1.9 presents the trends in total expenditure over a period of five years (2011-12 to 2015-16) and its composition under revenue, capital and loans and advances.



Source: Finance Accounts

Total expenditure increased by 68 *per cent* from ₹82,436 crore in 2011-12 to ₹1,38,398 crore in 2015-16 due to increase in revenue expenditure (₹51,913 crore), capital outlay (₹5,207 crore), offset by decrease in disbursement of loans and advances (₹1,158 crore).

During the period 2011-12 to 2015-16, on an average, 83 *per cent* of the total expenditure was on revenue account. During 2015-16, it was 85 *per cent*. The share of capital expenditure (including loans and advances) was 15 *per cent*.

The share of Revenue Expenditure, Capital Expenditure and Loans and Advances for the years 2011-12 to 2015-16 is given in **Table 1.22.**

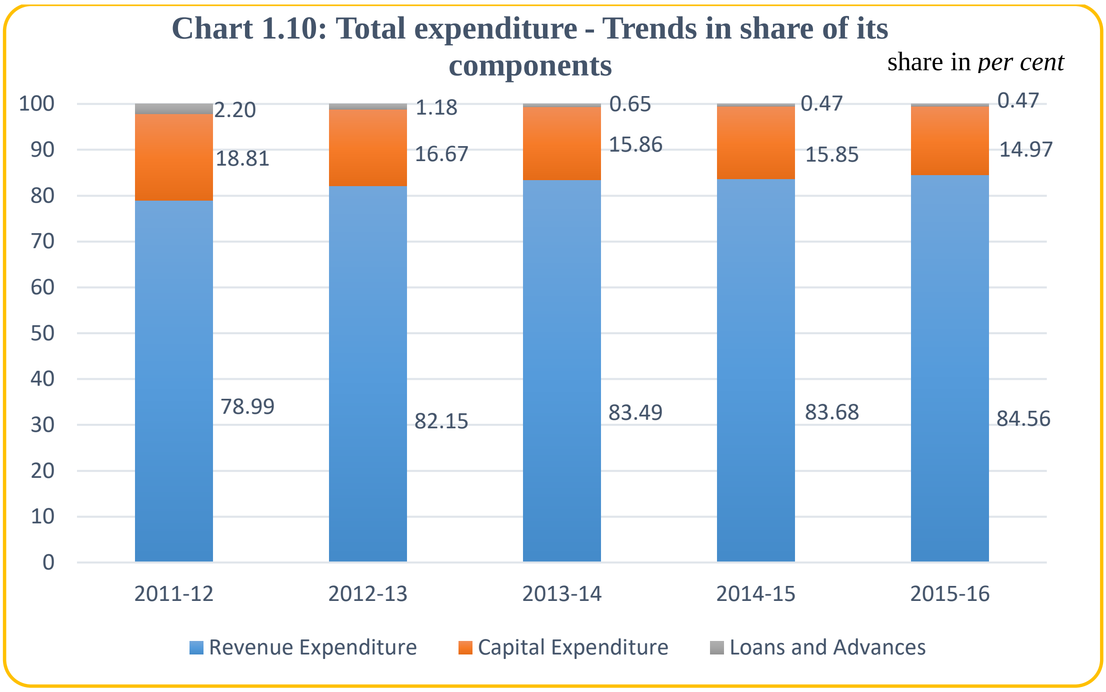
Table 1.22: Total Expenditure – Trends of Share of its components

(figures in *per cent*)

	2011-12	2012-13	2013-14	2014-15	2015-16
Revenue Expenditure	78.99	82.15	83.49	83.68	84.56
Capital Expenditure	18.81	16.67	15.86	15.85	14.97
Loans and Advances	2.20	1.18	0.65	0.47	0.47

Source: Finance Accounts of respective years

Chart 1.10 presents composition of total expenditure over a period of five years (2011-12 to 2015-16).



Revenue expenditure had a predominant share in total expenditure as around 80 *per cent* of the expenditure was committed expenditure thus leaving little scope for increase in capital expenditure. The trends of total expenditure by activities under General, Social, Economic, Loans and Advances and Grants-in-aid are given in **Table 1.23.**

Table 1.23: Total Expenditure – Trends by activities

(Share in *per cent*)

	2011-12	2012-13	2013-14	2014-15	2015-16
General Services	20.71	22.36	23.83	23.33	22.97
Social Services	33.80	35.89	33.39	35.17	37.30
Economic Services	38.02	36.23	37.43	36.17	34.87
Loans and Advances	2.20	1.18	0.65	0.47	0.47
Grants-in-aid	5.27	4.34	4.70	4.86	4.39

Source: Finance Accounts of the respective years

The movement of relative share of these components exhibited relative stability during the period from 2011-12 to 2015-16 with marginal inter year variations. The share of both General and Social services increased marginally while the share of Economic Services decreased slightly in 2015-16. The share of loans and advances declined sharply from 2011-12 to 2015-16.

The Expenditure Reforms Commission (ERC) in its first report (February 2010) had recommended capital investments to be stepped up and protected from fiscal uncertainties through prudent allocations. It had also recommended maintaining the capital expenditure (excluding debt servicing) at 5 *per cent* of GSDP. The ratio of capital expenditure to GSDP which was at 4 *per cent* during 2011-12, however, dropped to 3 *per cent* during the remaining period of 2012-13 to 2015-16.

1.6.2 Revenue Expenditure

Revenue expenditure comprises of day-to-day expenditure of the Government, wages and salaries, pensions, interest payments, expenditure on operation and maintenance of capital works, subsidies and transfers to local bodies, co-operatives, Non-Government Organisations (NGO) and others. Expenditure can also be classified into various functional categories such as administrative services, social services and economic services. Expenditure on social and economic services is incurred to create physical infrastructure and human resource development and, therefore, is considered productive, whereas expenditure on general administration and debt servicing are considered unproductive.

Revenue expenditure increased from ₹65,115 crore in 2011-12 to ₹1,17,028 crore in 2015-16, an increase of 80 *per cent*. The revenue expenditure buoyancy during 2015-16 was 1.7 times compared to GSDP. Compared to the previous year, the increase was 13 *per cent*, due to increase in salary expenditure (₹822 crore), interest payments (₹1,539 crore), pensions (₹1,133 crore) and devolution to local bodies (₹1,211 crore) etc.

The revenue expenditure during 2015-16 also included ₹1,185.31 crore provided as Guarantee Commission[3] (₹56.96 crore), waiver of penalty on Coffee seeds (₹1.60 crore), settlement of statutory dues of MySugar Company Ltd (₹38.95 crore), ESCOMs (₹1,087 crore) being the dues of electricity tax etc., treated as subsidy and adjustment of interest on Capital invested in Government Commercial Undertakings (GCU's) (₹0.80 crore) through book adjustment.

1.6.3 Committed Expenditure

Most of the revenue expenditure is in the nature of committed expenditure on salaries, pension, interest, subsidy etc., which affects the maneuverability of the State in prioritizing expenditure and in meeting capital investments to meet growing needs of social and economic infrastructure. The expenditure on these components and also certain other expenses such as pensions under social

[3] Rajiv Gandhi Rural Housing Corporation Ltd., (₹40.26 crore), Karnataka Slum Development Board (₹0.29 crore), Mines and Geology (₹0.70 crore), Karnataka Power Transmission Corporation Limited (₹14.03 crore), Mysore Lamps Works Limited (₹0.14 crore) and Karnataka State Industrial Investment and Development Corporation (KSIIDC) (₹1.54 crore).

security schemes, Grant-in-aid & Other Financial Assistance, administrative expenses, implicit subsidies arising under various schemes of the Government, devolution to local bodies etc., which are treated as committed expenditure in the MTFP 2014-18 covering the period 2011-12 to 2015-16 is depicted in **Table 1.24** and **Chart 1.11**.

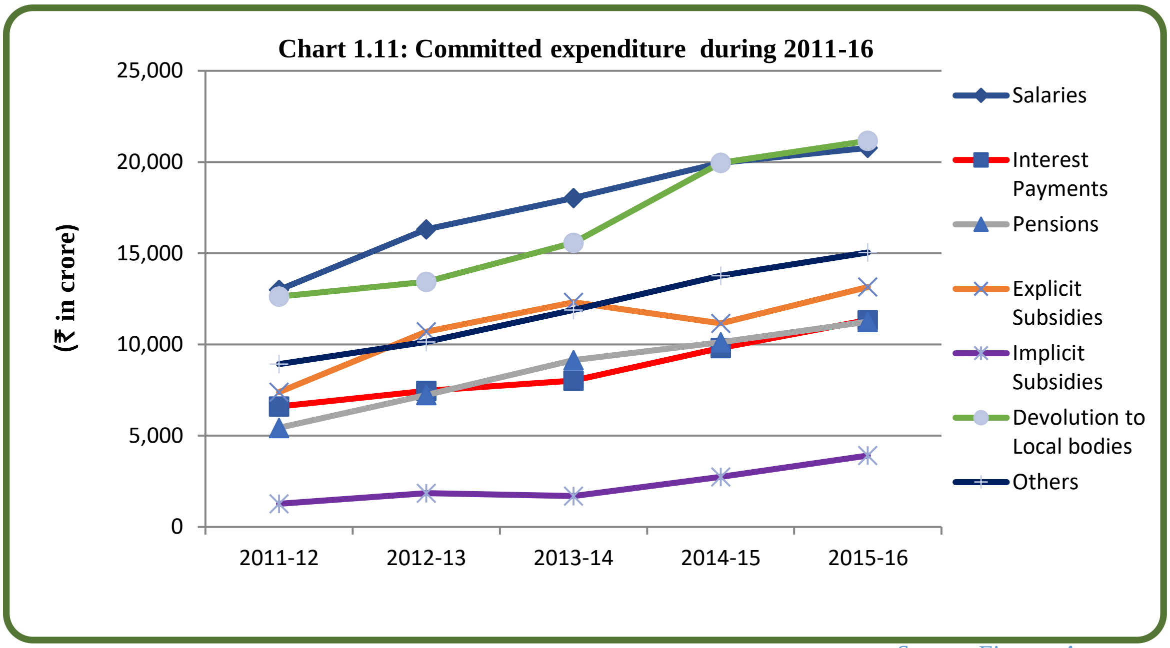
Table 1.24: Trends in committed expenditure

(₹ in crore)

Sl. No	Particulars	2011-12	2012-13	2013-14	2014-15	2015-16	
						BE	Actuals
1	Salaries* of which	12,996	16,308	18,027	19,952	22,576	20,774
	Non-Plan head	11,446	8,324	15,211	16,733		17,342
	Plan head**	1,550	7,984	2,816	3,219		3,432
2	Interest payments[#]	6,604	7,454	8,027	9,804	10,668[@]	11,343
3	Expenditure on pensions	5,436	7,227	9,152	10,118	10,714	11,251
4	Social Security Pensions	2,244	1,880	1,870	2,322	3,547	2,247
5	Subsidies of which						
	Explicit	7,390	10,709	13,323	11,153	18,480	13,149
	Implicit	1,270	1,849	1,690	2,973		3,913[^]
6	Grants-in-aid and financial assistance	5,652	6,898	8,471	9,737	7,717	10,840
7	Administrative Expenses	1,029	1,358	1,549	1,708	2,331	1,958
8	Devolution of Local Bodies	12,628	13,445	15,570	19,952	20,813	21,163
9	**Total Committed Expenditure**	**55,249**	**67,128**	**77,679**	**87,719**	**96,846**	**96,638**
10	**Revenue receipts**	**69,806**	**78,176**	**89,542**	**1,04,142**	**1,16,360**	**1,18,817**
11	Revenue receipts of which committed expenditure as % of revenue receipts **(9/10)**	79	86	87	84	83	81

** Includes salaries paid out of grants-in-aid released to PRIs and others*
*** Includes the salaries paid under centrally sponsored schemes.*
 # Includes interest on off-budget borrowings
@ includes interest pertaining to 2049 only
^ Excludes subsidy under Indira Awas Yojana, which was released as financial assistance

The ratio of committed expenditure to revenue receipts has been steadily increasing from 2011-12 to 2013-14 and there was decreasing trend from 2014-15 onwards. The high percentage of committed expenditure to revenue receipts indicates that the State has limited flexibility in allocation of its resources for new schemes. Medium term correction on the expenditure side is required to moderate such committed expenditure. There is also increasing demand on the public resources in the light of statutory legislation like Right to Education, Food Security Act and Employment Guarantee measures. These emerging concerns necessitate a review of public resources as a whole to assess their allocative and technical efficiency.



Source: Finance Accounts

Expenditure on salaries

Expenditure on salaries increased from ₹12,996 crore in 2011-12 to ₹20,774 crore in 2015-16. It grew by 4 *per cent* over the previous year. It was noticed that the Finance Accounts captured data on salaries only in respect of State Sector, whereas the salary expenditure in case of PRIs (to the tune of ₹11,608 crore) was not captured. Since the salaries in respect of PRIs are released as grant-in-aid, the total salary expenditure is not reflected in the accounts. The salary expenditure excluding the salary grant relating to Urban Local Bodies (ULBs) of the State was 22 *per cent* of the revenue expenditure net of interest payment and pensions, which was within the norm of 35 *per cent* fixed by the TFC.

FD replied (November 2014) that grants to PRIs/ULBs are released as lump sum grants as per constitutional requirement. Further, scheme wise breakup of salary and non-salary items is available in the link volumes. As such, the information is already being captured as part of PRI/ULB accounts.

The PAC in its 5th Report (July 2015) reiterated its recommendation that the data of the district sector, relating to details of salary be consolidated for exhibition in the Appendix of Finance Accounts.

Also, the salary expenditure relating to the employees of ULBs overlapped with those under the State sector (Constitutional dignitaries). This has been discussed in **paragraph 2.4.1.7** of this report**.**

Misclassification of salary expenditure under capital section amounting to ₹6.73 crore instead of under revenue during 2015-16 is discussed in **paragraph 2.4.1.**

Pension Payments

The expenditure on pension (₹11,251 crore) during 2015-16 exceeded MTFP (2012-16) projections by ₹991 crore. Increase of ₹1,133 crore in expenditure over the previous year was on account of increase in retirement of employees.

Defined Contribution Pension Scheme known as New Pension Scheme (NPS), for all employees who joined the State Government service on or after 01 April 2006, became fully operational from 01 April 2010. A dedicated NPS Cell has been created under the Directorate of Treasuries to operationalise the NPS in the State. The State Government has adopted the NPS architecture designed by the Pension Fund Regulatory Development Authority (PFRDA) and has appointed the National Securities Depository Limited (NSDL) as the Central Record Keeping Agency (CRA) for NPS. Bank of India is the Trustee Bank in charge of operation of Pension Funds. The security of investment of the pension corpus is also given primacy by mandating that 85 *per cent* of corpus be invested in bonds and fixed maturity investments and the remaining 15 *per cent* in equity and equity related instruments. The employees are given an option to pay their backlog either in lump sum outside salary or in multiple installments through salary deductions.

The New Pension Implementation Cell (NPIC) stated that (May 2016) there were 1,57,719 officials registered in the State and allotted Permanent Retirement Account Number (PRAN) as on 31 March 2016. An amount of ₹388.33 crore was contributed towards the scheme by the Government through revenue account. Employees' contribution of ₹439.02 crore for the current year was also accounted against the scheme. The employee recoveries and backlog[4] contribution as on 31 March 2016 is ₹1,673.20 crore and the matching contributions made by State Government since inception of the scheme is ₹1,625.97 crore.

An amount of ₹791.55 crore was transferred to NSDL/Trustee bank from Fund balance, leaving net balance of ₹16.01 crore (Employees' contribution, Government's contribution and Backlog/Interest) under Major Head 8342 and Minor head 117- Defined Contribution Pension Scheme for Government Employees. The discrepancy is due to misclassification by the Director of Treasuries and needs to be reconciled. Un-transferred amounts with accrued interest represent outstanding liabilities of the Government. During 2015-16, ₹3.50 crore has been paid from the Consolidated Fund as 'New Contributory Pension Schemes – Extension of benefit to the cases of Persons/Families who retire/died while in service' and are covered under NPS.

Vide correction slip No 793 effective from 2015-16 issued to the List of Major and Minor Head (LMMH) a new minor head '119' below the functional Major head "2071 – Pension & Retirement benefits" has been opened to account the expenditure towards service charges paid to NSDL. Accordingly, for the year 2015-16, ₹6.12 crore had been paid to NSDL towards service charges under NPS and accounted under HOA'2071-01-119-0-01-NP'.

[4]Refers to the contribution the employee has to make from the date of his entry into service to the date of implementation of the scheme.

Government in its GO dated 31.01.2014 had issued the detailed procedure for effecting NPS deductions of Government employees on foreign services to Boards/ Corporations/ Societies/ Universities/ State Aided Institutions/ State Autonomous Bodies under all Ministries and Departments of State Government. For effecting the NPS deductions, NPS cell allocated a unique Non-Treasury PAO/DDO code to 28 organisations, of which 11 organisations have been registered by CRA as on 31.03.2016 and allotted PAO registration numbers and DDO numbers. As such there were 276 subscribers coming under the purview of NPS in these organizations.

The payment of pension and other retirement benefits to All India Service officers prior to 01 April 2008, was a liability to be borne by the State Government. The liability on account of pension payments that are to be borne by the GOI (from April 2008), are to be booked under suspense head - 8658 and a demand raised for reimbursement. In this regard a sum of ₹9.12 crore (March 2016) was outstanding for settlement, implying that the State Government was yet to receive amount due to it.

Interest Payments

Interest payments increased by ₹4,739 crore from ₹6,604 crore in 2011-12 to ₹11,343 crore in 2015-16. Interest payments during 2015-16 constituted interest on internal debt (₹8,222 crore), interest on small savings, provident fund etc., (₹1,844 crore), interest on loans and advances from the Central Government (₹680 crore) and interest on off-budget borrowings (₹597 crore).

The interest on internal debt increased by 17 *per cent* from ₹7,024 crore in 2014-15 to ₹8,222 crore in 2015-16 on account of increase in payment of interest on market loans by ₹1,138 crore (24 *per cent*), interest on special securities by ₹41 crore (2 *per cent*) issued to NSSF of the Central Government by the State Government, interest on other internal debt by ₹11 crore (2 *per cent*) and management of debt by ₹8 crore (113 *per cent*).

The interest on small savings, provident funds etc. increased by ₹178 crore (11 *per cent*) from ₹1,666 crore during 2014-15 to ₹1,844 crore in 2015-16, mainly on account of increase in interest on State provident funds and insurance and pension funds by 10 and 12 *per cent*, respectively, relating to the previous year.

Interest on off-budget borrowings

The ratio of interest payments to revenue receipts (IP/RR) determines the debt sustainability of the State. During 2015-16, the ratio of interest payments to total revenue receipts of the State was 10 *per cent*, which was well within the TFC norm of 15 *per cent*. During 2011-12 to 2015-16 the ratio hovered between 9 and 10 *per cent* on account of buoyancy in revenue receipts. By an amendment to the KFRA in February 2014, the scope of the total liabilities was amplified to include the borrowings by PSU and SPVs and other equivalent instruments, where the principal and/or interest are to be serviced out of the State Budget. Thus the off-budget borrowings (OBB) are part of the State’s own liabilities for working out the Total Liabilities of the State.

The State Government in its MTFP 2016-20 on the ratio of IP/RR had included the interest payments serviced under the HOA 2049 only. But the interest on OBBs which are serviced through other heads of account is not part of this ratio of IP/RR. Even though the ratio of IP/RR are within the norms, the inclusion of interest on OBBs should also be considered for working out this ratio, in the MTFP by the State Government.

Payment of interest on Compensation Bonds

The interest payments by the Government is on the financial liabilities brought out in Government Accounts. These liabilities inter alia comprise borrowings under Public Debt and Liabilities on Public Account. The borrowings under compensation bonds forms a part under Public Debt.

Sanction was accorded by Finance department (January 2015) for payment of ₹1,45,765 to Reserve Bank of India, Banking Department, Bangalore towards the interest on Compensation Bonds, the transactions of which are reflected under the functional minor head 200-Interest on other Internal Debts. Finance department instructed RBI to take out this transaction from its books and afford equivalent credit to Government books.

However, audit observed that Office of Accountant General (A&E) [AG (A&E)] in their letter (March 2016) stated that the balance amount of Compensation bonds had already been adjusted to the 2075-'Miscellaneous Government Accounts' during 1996-97 in terms of instructions contained under Note (3) below 6003-Internal Debt of the State Government in the LMMH.

The State Government is paying interest on Compensation Bonds even though the bonds are not outstanding in the Government books. The un-redeemed bonds to the extent of ₹39.81 lakh are still shown as outstanding as per the books of RBI even though office of the AG (A&E) has clearly stated (March 2016) that the compensations bonds have been adjusted during 1996-97 itself. As there exists an anomaly between the figures of RBI and AG (A&E), early action is necessary to set right the discrepancy.

Delay in release of grants to PRIs and ULBs –Payment of Interest

A mention was made in the report on State Finances for the year ending March 2015 regarding delay in release of XIII FC grants to PRIs and ULBs wherein it was stated that the grants to the PRIs and ULBs should be released by the Rural Development Department within 05 days from the date of receipt of grant from Government of India. In the event of delay in release of grants, the State Government was liable to release the installment with interest at the bank rate of Reserve Bank of India for the number of days of delay. Accordingly, for the delay in release of General Basic Grants and Performance Grants for the year 2013-14, ₹5.03 crore in respect of PRIs and ₹1.92 crore in respect of ULBs has been paid as interest during 2015-16. Similarly, there has been delay in release of first installment of XIV FC grants during 2015-16 to Gram Panchayats (GP) for which the Government had to pay interest of ₹1.43 crore. The grants to GP were required to be released within 15 days of receipt from Central Government. The reasons for the delay in release of grants to PRIs and ULBs is not forthcoming. Appropriate procedures may be put in place to ensure timely releases in future.

Subsidies

Subsidy expenditure increased from ₹7,390 crore in 2011-12 to ₹13,149 crore during 2015-16, which was 11 *per cent* of revenue receipts.

Explicit Subsidies

In MTFP (2013-17), the Government had stated that subsidies provided by the State could be of two kinds – explicit and implicit subsidies. Explicit subsidy is that which provides for expenditure in the form of a subsidy or interest subvention for certain schemes of the Government. It was stressed that the challenge lies in ensuring that these subsidies do not become a permanent source of additional support and thereby deter these sectors from undertaking reforms. The three largest explicit subsidy outgoes for the State were power subsidy provided for supply of free electricity to farmers for usage of agricultural pump sets, food subsidy and interest subsidy for crop loans. Finance Accounts (Appendix-II) showed an explicit subsidy of ₹13,149 crore during 2015-16 which was ₹1,996 crore more than the previous year. The increase was 18 *per cent* over the previous year. The details are given below.

Power

During 2015-16, subsidy to the power sector (₹8,693 crore) accounted for 66 *per cent* of the total subsidy (₹13,149 crore). It included financial assistance to electricity supply companies towards subsidy for supply to Irrigation Pump (IP) sets, Bhagya Jyothi (BJ)/ Kutira Jyothi (KJ)(₹8,143 crore) and pension contribution to the employees of Karnataka Power Transmission Corporation Limited (KPTCL) (₹550 crore). The power subsidy included book adjustment of ₹1,101.39 crore of which ₹1,029.86 crore was the tax dues retained by ESCOMs against power subsidy due.

Though Government stated (November 2007) that the KPTCL would be reflected as an off-budget entity in the budget documents, this was not complied with. Also subsidy of ₹19.19 crore given to the KPTCL for meeting its debt servicing obligations to the Power Finance Corporation (PFC) and Rural Electrification Corporation (REC), was not captured under revenue account.

Release of subsidy to ESCOMS

Government is providing subsidy to ESCOMs for supply of IP Sets, BJ/ KJ consumers. For the years from 2007-08 to 2014-15, the accepted subsidy dues to ESCOMS were ₹1,537.36 crore which were cleared during 2015-16. Postponing the expenditure of earlier years and making payment during the current year had the effect of altering the fiscal indicators of those years.

Food

Food subsidy to meet the differential cost of food grains in 2015-16 is ₹2,196 crore which includes subsidy towards Annabhagya for BPL beneficiaries towards subsidies for Food Grains (₹1,761 crore), Annabhagya for BPL beneficiaries towards subsidies for other items (₹429 crore) and Annabhagya for APL beneficiaries towards subsidies for food grains (₹5 crore) and Sugar (₹0.92 crore).

Co-operation

Subsidy in the co-operative sector predominantly represented waiver of overdue loans (principal as well as interest) given to farmers. Such waiver of loans and interest aggregated to ₹5,863 crore (₹447 crore in 2011-12, ₹1,323 crore in 2012-13, ₹2,704 crore in 2013-14, ₹624 crore in 2014-15 and ₹765 crore in 2015-16).

According to the Vaidyanathan Committee Report (March 2008), and as reiterated by the PAC, the Governments both at the Centre and in the States should desist from the practice of waiver of recovery of loans and interest to prevent deterioration of the health of the co-operative credit system.

Transport

Transport subsidy had increased from ₹651 crore in 2014-15 to ₹748 crore in 2015-16. This subsidy was mainly towards fare concession extended to students, freedom fighters, physically challenged, etc. It also included book adjustment of ₹328.43 crore being the motor vehicle tax dues of transport corporations, adjusted as subsidy towards concession value of bus passes issued to students, senior citizens, blind, handicapped and free bus passes provided to ex-MLAs and MLCs.

Implicit Subsidies

Implicit subsidies inter alia arise when the Government is unable to recover the costs it incurs on the provision of social and economic goods/services, even though sometimes these may have extended benefits. They can be indirect, in kind or take the shape of tax concessions. Some of the implicit subsidies extended during 2015-16 are detailed in **Appendix 1.5**.

The implicit subsidies increased from ₹1,270 crore in 2011-12 to ₹3,913 crore during 2015-16. They mainly include financial assistance for supply of seeds, weaver's package, Ashraya scheme, micro/drip irrigation, minimum floor price scheme, housing for weaker sections, house site for landless etc.

During 2015-16, the subsidy under Indira Awas Yojana (₹1,020 crore) was accounted for under HOA '2216-80-198-6-02-300(P)' as financial assistance/ block grant to ZPs instead of for under HOA '2216-80-103-0-21' (Indira Awas Yojana) &'2216-80-800-0-04' (Indira Awas Yojana – State share).

1.6.4 Financial assistance to local bodies and other Institutions

The quantum of assistance provided by way of grants to local bodies and other institutions during 2015-16, relative to the previous years, is presented in **Table 1.25**.

Table 1.25: Financial assistance to local bodies and other institutions

(₹ in crore)

	2011-12	2012-13	2013-14	2014-15	2015-16
Panchayat Raj Institutions	15,211.83	18,532.58	20,512.71	24,991.27	26,694.94
Urban Local Bodies*	4,343.96	4,018.42	5,020.43	6,011.45	6,076.05
Educational Institutions (including Universities)	630.47	738.69	961.62	1,145.04	1,406.50
Co-operative societies and co-operative institutions	357.79	47.04	849.85	818.09	1,023.13
Other institutions and bodies (including statutory bodies)	2,486.31	3,850.11	5,267.90	5,782.63	4,820.87
Assistance as a percentage of revenue expenditure	37	36	37	37	34
Total	**24,030.36**	**27,186.84**	**32,612.51**	**38,748.48**	**40,021.49**

Source: Finance Accounts

**the figures under assistance to Urban Local Bodies differs from those shown in the earlier reports on account of inclusion of devolutions under the Minor Head 200 – Other compensations and assignment.*

As a sequel to the recommendations of the Eleventh Finance Commission, grants are released to PRIs under three distinct programme minor heads namely 196, 197 and 198. The assistance to PRIs increased from ₹15,212 crore in 2011-12 to ₹26,695 crore in 2015-16, while the assistance to ULBs increased from ₹4,344 crore in 2011-12 to ₹6,076 crore in 2015-16.

Out of the total devolution of ₹26,695 crore to PRIs during 2015-16, ₹11,608 crore (43 *per cent*) was towards salaries as the State Government's functions viz., education, water supply and sanitation, housing, health and family welfare etc., were transferred to PRIs. It also included the XIV FC grants released to the State Government (₹972.36 crore).

Audit observed that in case of a CSS viz. Indira Awas Yojana, funds were being released to the M/s Rajiv Gandhi Rural Housing Corporation Ltd. for construction of houses under the State Sector. During 2015-16, ₹1,019.20 crore were released to the said company for the above purpose under District sector instead of State sector, to project increased devolutions to PRIs.

The assistance to ULBs increased by ₹65 crore and to Co-operatives by ₹205 crore respectively, as compared to the previous year. It increased for educational institutions by ₹261 crore and decreased by ₹962 crore during 2015-16 for other institutions. The assistance to ULBs included ₹2,972 crore towards creation of capital assets. It also included the XIV FC grants released to the State Government (₹562.08 crore).

Assistance to other institutions (₹4,821 crore) included assistance to Development Authorities (₹748 crore), NGOs (₹1,721 crore), PSUs (₹26 crore) and others (₹2,326 crore).

1.7 Quality of expenditure

The availability of better social and physical infrastructure in the State generally reflects the quality of its expenditure. The 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, and its effectiveness.

1.7.1 Adequacy of public expenditure

The expenditure responsibilities relating to the social sector and 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 category to aggregate expenditure) can be stated to have been attached to a particular sector if the priority given to that particular head of expenditure is below the General Category States' (GCS) average for that year.

Table 1.26 analyses the fiscal priority of the State Government with regard to development expenditure, social expenditure and capital expenditure relative to GCS in 2012-13 and the current year 2015-16.

Table 1.26: Fiscal priority of the State in 2012-13 and 2015-16

Fiscal priority by the State	AE/ GSDP	DE#/ AE	SSE/ AE	CE/ AE	Education/ AE	Health/ AE
*General Category States Average (Ratio) 2012-13	14.14	70.03	38.47	13.70	17.72	4.72
Karnataka State's Average (Ratio) 2012-13	17.83	73.29	36.77	17.85	16.14	4.23
*General Category States Average (Ratio) 2015-16	16.05	70.03	36.29	14.89	15.63	4.45
Karnataka State's Average (Ratio) 2015-16	18.80	72.57	37.54	15.44	14.05	4.21

AE: Aggregate 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.
Source: For GSDP, data is as per the Government of India conveyed figures, adopted by the State Government in its budget documents.
**refer note in Appendix 1.1.*

Comparative analysis reveals the following:

- The State's spending ratio of aggregate expenditure to GSDP moderated marginally during 2015-16 compared to 2012-13.
- Development expenditure as a proportion of aggregate expenditure in the State has been higher than the GCS average. Development expenditure consists of both economic and social service sector expenditure. The social sector expenditure as a proportion of aggregate expenditure in the State, was lower than that of the GCS in 2012-13 and higher in 2015-16. As observed from the **Table 1.26**, adequate priority needs to be given to both education and health

sectors as the ratio under both these sectors is well below the GCS average during 2012-13 and 2015-16.

- Priority has been given by the State Government to capital expenditure in 2012-13 and 2015-16, as the ratio of capital expenditure to aggregate expenditure has been higher than the average ratio of GCS.

1.7.2 Efficiency of expenditure

In view of the importance of public expenditure on social and economic development, it is imperative for the State Government to take appropriate expenditure rationalization measures with more emphasis on development expenditure[5]. The higher the ratio of these components to total expenditure, the better would be the quality of expenditure. **Table 1.27** presents the trends in development expenditure relative to the aggregate expenditure of the State during 2015-16 *vis-à-vis* that of previous years.

Table 1.27: Development expenditure

(₹ in crore)

	2011-12	2012-13	2013-14	2014-15	2015-16
Development Expenditure (DE)	60,930	68,067	76,328	88,904	1,00,441
Percentage of DE to total expenditure	74	73	71	72	73
Components of DE					
Revenue	44,326 (73)	52,094 (76)	59,215 (77)	69,337 (78)	80,153 (80)
Capital	14,880 (24)	14,889 (22)	16,446 (22)	19,004 (21)	19,722 (20)
Loans and Advances	1,724(3)	1,084(2)	667(1)	563(1)	566(-)*

Source: Finance Accounts

Figures in brackets indicate percentage to development expenditure.
**differs from those shown in appendix due to rounding.*

Development expenditure increased from ₹60,930 crore in 2011-12 to ₹1,00,441 crore in 2015-16. As a percentage of total expenditure, it decreased from 74 in 2011-12 to 71 in 2013-14 and thereafter increased to 73 *per cent* during 2015-16. On an average, 77 *per cent* of the development expenditure was on revenue account while capital expenditure, including loans and advances accounted for the balance during 2011-12 to 2015-16. In 2015-16, expenditure on salary (₹15,500 crore) and subsidy (₹13,106 crore) formed two major components of development revenue expenditure.

Table 1.28 provides the details of capital expenditure and the components of revenue expenditure incurred on salaries and maintenance of the selected social and economic services.

[5]The analysis of expenditure data is segregated into development and non-development expenditure. All expenditure relating to revenue account, capital outlay and loans and advances is categorized into social, economic and general services. Broadly, the social and economic services constitute development expenditure, while expenditure on general services is treated as non-developmental expenditure.

Table 1.28: Efficiency of expenditure in selected social and economic services

(ratio in *per cent*)

Sector	2014-15			2015-16		
		Revenue expenditure			Revenue expenditure	
	Ratio of capital expenditure to total expenditure	Salaries and wages	Operation and Maintenance	Ratio of capital expenditure to total expenditure	Salaries and wages	Operation and Maintenance
Social Services						
Education, sports, art and culture	0.26	9.37	0.02	0.52	8.68	0.01
Health and family welfare	0.64	2.09	0.01	0.59	1.96	0.01
Water Supply, sanitation, housing and urban development	1.64	0.05	0.11	1.42	0.08	0.12
Others	1.14	0.62	0.02	1.55	0.55	0.02
Total (SS)	**3.68**	**12.13**	**0.16**	**4.08**	**11.27**	**0.16**
Economic Services						
Agriculture and allied activities	0.22	1.15	0.05	0.14	1.04	0.04
Irrigation and flood control	6.28	0.16	0.23	5.02	0.12	0.29
Power and energy	0.25	-	-	0.06	-	-
Transport	4.16	0.07	0.89	3.90	0.07	0.62
Others	1.22	0.78	0.03	1.46	0.74	0.02
Total (ES)	**12.13**	**2.16**	**1.20**	**10.58**	**1.97**	**0.97**
Total (SS+ES)	**15.80**	**14.29**	**1.36**	**14.66**	**13.24**	**1.13**

Source: Finance Accounts

Expenditure on Social Services

Capital expenditure on social services increased from ₹4,551 crore in 2014-15 to ₹5,641 crore in 2015-16 and the ratio of capital expenditure to total expenditure increased from 3.68 *per cent* in 2014-15 to 4.08 *per cent* in 2015-16. The share of salary expenditure (under social services) in total revenue expenditure was 11 *per cent* in 2015-16 (**Table 1.28**).

Expenditure on Economic Services

Capital expenditure on economic services decreased from ₹15,016 crore in 2014-15 to ₹14,647 crore in 2015-16. The share of salary expenditure (under economic services) in total revenue expenditure was 2 *per cent* during 2015-16 (**Table 1.28**).

The priority sectors identified by the Government in respect of economic services were agriculture, rural development, irrigation and flood control, transport, industries and minerals. In 2015-16, capital outlay was higher by ₹350 crore, ₹253 crore and ₹99 crore under industries and minerals, transport and special areas programmes respectively, while under irrigation and flood control, energy, agriculture and rural development it was lower by ₹824 crore, ₹203 crore, ₹84 crore and ₹7 crore respectively compared to the previous year.

1.8 Financial Analysis of Government expenditure and investments

In the post KFRA framework, the Government is expected to keep its fiscal deficit (borrowing) at low levels and still meet its capital expenditure/investment (including loans and advances) requirements. In addition, the State Government needs to initiate measures to earn adequate return on its investments rather than bearing the same in the form of implicit subsidy, recover cost of borrowed funds and 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 2015-16 *vis-à-vis* previous years.

1.8.1 Incomplete projects

Locking up of funds in incomplete works, which includes works stopped due to reasons like litigation, etc., impinge negatively on the quality of expenditure. The department-wise information pertaining to incomplete projects as of 31 March 2016 is given in **Table 1.29**.

Table 1.29: Incomplete projects

(₹ in crore)

Department	Incomplete Projects*				Cumulative expenditure as of March 2016
	Number	Budgeted cost	Cost over run		
			Number	Amount	
Public Works					
Buildings	77	315.92	7	14.47	260.66
Roads & Bridges	212	1,243.18	47	14.30	1,155.70
Irrigation	57	99.90	7	0.88	78.87
Total	**346**	**1,659.00**	**61**	**29.65**	**1,495.23**

Source: Finance Accounts

**Projects scheduled to be completed on or before 31 March 2016 have been included*

Against the initial budgeted cost of ₹1,659 crore in respect of 346 works, stipulated to be completed on or before March 2016, the progressive expenditure was ₹1,495.23 crore as of 31 March 2016, out of which, in 61 cases, the cost overrun aggregated ₹29.65 crore. No reasons for delay in completion of the works was given by the Public Works and Irrigation Departments.

1.8.2 Investment and returns

The investment of the Government in the share capital of Companies/Corporations etc., as brought out in Finance Accounts include the expenditure under the heads of account 4225-107 - Investment in Credit Co-operatives, 4225-108 - Investment in other Co-operatives, 4405-00-191 - Fishermen Co-operatives, and 4851-00-108-01 - Share Capital Assistance to Power Loom Co-operative Societies and the minor heads 190 – Investments in Public Sector and Other undertakings and 195 - Investment in Co-operatives under the various Capital Outlay heads.

Sick / non-working PSUs/Departmentally managed organizations

As of 31 March 2016, the Government had invested ₹61,356 crore, in 84 Government Companies (₹56,229 crore including investment of ₹68 crore in 16 non-working Government Companies), Nine Statutory Corporations (₹2,445 crore), 43 Joint Stock Companies (₹2,299 crore), and Co-operative Institutions, Local bodies and Regional Rural Banks (₹382 crore). The return from investment was negligible (**Table 1.30**).

Table 1.30: Return on investment

	2011-12	2012-13	2013-14	2014-15	2015-16
Investment at the end of the year (₹ in crore)	44,294.86	49,463.80	55,048.00	61,726.92	61,355.89
Return (₹ in crore)	60.56	56.29	55.49	74.84	69.40
Return (*per cent*)	0.1	0.1	0.1	0.1	0.1
Average rate of interest on Government borrowings (*per cent*)	6.6	6.6	6.2	6.5	6.5
Difference between interest rate and return (*per cent*)	6.5	6.5	6.1	6.4	6.4

Source: Finance Accounts

Though the State Government had accepted that the return on these investments was meager, it stated that it would not shy away from investing in social infrastructure involving long gestation and pay back periods. The Government further stated that efforts would be made to ensure due returns. Audit found that the MTFPs placed before the Legislatures did not contain a road map for ensuring proper return on investments.

In addition, investment of ₹388.47 crore in respect of five[6] Companies/ Corporations has been lying in Public Account as at the end of March 2016 without actual utilisation by the institutions. This has resulted in locking up of funds in the Public Account. Efforts should be made for proper utilization of these funds and a system should be put in place for scrutiny of proposals received from the Companies seeking funds before releasing further money from the Consolidated Fund.

With regard to large sums remaining unutilised by certain entities, the Finance Department replied (October 2015) that a committee called Off Budget Borrowing Monitoring Committee (OMC) has been constituted under the chairmanship of the Principal Secretary to Government, Finance Department, that has the power to review the status of the existing loan or bond and suggest action as may be required in the overall interest of the finances of the Board / Corporation. The FD also stated (October 2015) that before releasing the amount towards payment of principal and interest, the utilisation of previous year's principal repayment and interest is also being ensured.

Out of the total investment of ₹61,356 crore up to the end of March 2016, ₹58,494 crore (95 *per cent*) were invested in 60 Government Companies and Statutory Corporations under irrigation sector (₹36,779 crore), transport sector (₹2,399 crore), infrastructure sector (₹3,686 crore), power sector (₹9,508 crore), industries sector (₹806 crore), housing sector (₹1,451 crore), financing sector (₹2,841 crore), construction sector (₹2 crore) and social sector (₹1,022 crore). The investment included ₹25,002 crore (41 *per cent*) in the following Companies/Corporations, which were running perennial losses and where the investments were substantial (**Table 1.31**).

[6]Krishna Bhagya Jala Nigam (₹128.71 crore), Karnataka Urban Infrastructure Development and Finance Corporation (₹191.09 crore), Karnataka Neeravari Nigam Limited (₹0.33 crore), Karnataka Rural Infrastructure Corporation Limited (₹61.21 crore), Karnataka Slum Development Board (₹7.13 crore).

Table 1.31: Investment in Companies/Corporations under perennial loss

(₹ in crore)

Company/Corporation	Investment up to 2015-16	Cumulative loss	Cumulative loss to the end of
North Western Karnataka Road Transport Corporation	266.85	562.17	2014-15
North Eastern Karnataka Road Transport Corporation	183.43	432.74	2014-15
The Karnataka Minorities Development Corporation Limited, Bengaluru	437.80	23.55	2013-14
Rajiv Gandhi Rural Housing Corporation Limited, Bengaluru	96.11	74.29	2014-15
Krishna Bhagya Jala Nigam Limited	23,745.34	511.78	2014-15
The Mysore Sugar Company Limited, Bengaluru	272.34	289.42	2012-13
Total	**25,001.87**	**1,893.95**	

Source: Finance Accounts

During 2015-16, the Government invested ₹122 crore in these Companies and the cumulative loss had increased by ₹213 crore over the previous year.

Krishna Bhagya Jala Nigam Limited was established (in 1994) as a wholly owned Government Company under the provisions of the Companies Act, 1956, mainly for execution, operation and maintenance of the Upper Krishna Project works in the Krishna River Basin and such other projects allocated to it by the Government from time to time. The cumulative loss of the company at the end of 2014-15 was ₹512 crore.

The transactions under investment account includes certain non-cash transactions like conversion of dues into equity and reconciling the investment of the Government with the books of the Companies. Outstanding Government dues amounting to ₹83.82 crore held by Karnataka State Industrial and Infrastructure Development Corporation Limited (KSIIDC) were converted into equity in order to increase the capital base of the Company.

The investment account was reduced Proforma on account of the following transactions:

1. Investments in 'Karnataka Road Development Corporation Limited', decreased' by ₹2,669.19 crore due to conversion of equity into capital grants under MH 5054-800-Other expenditure. Change in classification of expenditure of earlier years was done by correction of progressive balance under relevant heads without affecting the disbursement transactions for the year 2015-16.

2. Investments in 'Rajiv Gandhi Rural Housing Corporation Limited' decreased by ₹127.29 crore due to conversion of equity as capital grants under MH 4216-190 – Investments in Public Sector and Other Undertakings to minor head 800-Other Expenditure.

3. Progressive capital expenditure under 4425-Capital Outlay on Co-operation', decreased by ₹1.70 crore, due to retirement of Government investments in share capital of co-operative institutions,

proceeds of which stands accounted under 'Miscellaneous Capital Receipts' in 2015-16.

4. Government Investments in KSIIDC was increased by ₹15.00 crore due to conversion of capital releases into share capital.

During 2015-16, the Government invested ₹1,689.49 crore, in Statutory Corporations (₹75.00 crore), Government Companies (working) (₹1,570.35 crore) and co-operative institutions (₹44.14 crore).

Non-approval for establishment of company – Bangalore Bioinnovation Centre

A new company by name "The Bangalore Bioinnovation Centre" (BBC) has been incorporated on 10 April 2015 under the Administrative Control of Department of Information Technology/Bio-Technology & Science & Technology of Government of Karnataka as a Government of Karnataka undertaking. The company has been formed with Certificate of Incorporation by Registrar of Companies, Memorandum and Articles of Association, appointment of first directors and investment in the form of share capital by the Government.

Under the Karnataka Government (Transaction of Business) Rules, 1977, Rule 16 (i) of the First Schedule "creation of new corporations or companies either wholly owned or partially financed by the State Government or by a Public Sector Undertaking" shall be brought before the Cabinet. In the instant case the company was formed without the approval of the Cabinet which is against the rules. However, investment of ₹0.01 crore was made in this company.

1.8.3 Investment in Public Private Partnership (PPP) Projects

Recourse to the PPP mode for project financing is encouraged because it frees valuable fiscal space for the provision of public goods in areas where such financing may not be forthcoming. PPP projects are in the sectors of transport, agri-infrastructure, education, health, tourism, urban and municipal infrastructure and energy. The Infrastructure Development Department was established to play a significant role in the areas of developing air, train and maritime connectivity for the State and in promoting increased private investment in public infrastructure through PPP.

The summary of PPP projects that are completed, under implementation/ construction and in operation/ planning/ pipeline as on 31 March 2016 are detailed in **Table 1.32**.

Table 1.32: Sector and stage-wise status of PPP projects in the State

(₹ in crore)

Sector	Completed		Under implementation/ construction		Under planning/Pipeline		Grand Total	
	No	Cost	No	Cost	No	Cost	No	Cost
Agri-Infrastructure	-	-	1	105.90	13	6,739.00	14	6,844.90
Education	-	-	-	-	-	-	-	-

Sector	Completed		Under implementation/ construction		Under planning/Pipeline		Grand Total	
	No	Cost	No	Cost	No	Cost	No	Cost
Energy	-	-	-	-	4	10,520.00	4	10,520.00
Health	-	-	-	-	1	-	1	-
Industrial Infrastructure	-	-	-	-	10	61,851.50	10	61,851.50
Roads & Bridges	5	793.18	4	1,275.51	28	49,588.00	37	51,656.69
Tourism	1	32.00	1	108.00	20	1,982.00	22	2,122.00
Transportation & Logistics excluding roads and bridges	2	2,763.29	3	60.82	19	21,753.00	24	24,577.11
Urban and Municipal Infrastructure	7	325.00	1	40.00	54	34,084.00	62	34,449.00
Total	**15**	**3,913.47**	**10**	**1,590.23**	**149**	**1,86,517.50**	**174**	**1,92,021.20**

Source: PPP Cell of Infrastructure Development Department

From the table it is seen that as on 31 March 2016, 15 projects were completed at a cost of ₹3,913 crore. Another 10 projects of ₹1,590 crore are under implementation and 149 projects of ₹1,86,518 crore were under pipeline/planning indicating that 94 *per cent* of the projects are yet to materialize. The details are furnished in **Appendix 1.6.**

1.8.4 Departmental Undertakings

Nineteen undertakings of certain Government departments performed activities of a quasi-commercial nature. According to the latest accounts furnished by six undertakings, the State Government's investment in these undertakings was ₹10.04 crore. The total loss incurred by these undertakings was ₹6.24 crore. Details are furnished in **Appendix 1.7.**

In view of the continued losses sustained by these undertakings, there is a need for reviewing their working so as to wipe out their losses in the short term and make them self-sustaining in the medium to long term.

State Government assured the PAC in December 2013 that the departments would be advised to expedite the conduct of review on the working of these undertakings and submit the findings of the review to the FD and PAC. The outcome of the review is yet to be received.

1.8.5 Loans and advances by the State Government

In addition to investments in Companies, Corporations and Co-operative Institutions, the Government also provided loans and advances to many institutions. **Table 1.33** presents the position of outstanding loans and advances as of 31 March 2016 and interest receipts *vis-à-vis* interest payments during the last five years.

Table 1.33: Average interest received on loans advanced by the State Government

(₹ in crore)

	2011-12	2012-13	2013-14	2014-15	2015-16
Opening balance	9,623	11,198	12,142	12,724*	13,216
Amount advanced during the	1,816	1,102	695	576	657

	2011-12	2012-13	2013-14	2014-15	2015-16
year					
Amount repaid during the year	241	158	109	84	60
Closing balance	11,198	12,142	12,729	13,216	13,813
Net addition	1,575	944	586	492	597
Interest receipts	52	247	235	127	264
Interest receipts as *per cent* to outstanding loans and advances	0.5	2.2	1.9	1.0	1.9
Interest payments as *per cent* to outstanding fiscal liabilities of the State Government	6.3	6.2	5.8	6.0	6.2
Difference between interest receipts and interest	-5.8	-4.0	-3.9	-5.0	-4.3

Source: Finance Accounts

**Differs by ₹5 crore on account of conversion of outstanding loans into equity in respect of M/s MSIL during 2014-15.*

Loans outstanding as of 31 March 2016 aggregated to ₹13,813 crore. Interest spread of Government borrowings was negative during 2011-12 to 2015-16, which meant that the State's borrowings were more expensive than the loans advanced by it.

The amount advanced during 2015-16 was ₹657 crore. Repayment of loans during 2015-16 aggregated ₹60 crore.

Detailed accounts of recovery of loans which are maintained in the office of the AG (A&E) indicated that arrears in recovery of loans and advances aggregating ₹6,270 crore (Principal: ₹3,763 crore and Interest: ₹2,507 crore) were overdue as of 31 March 2016 from 21 institutions (**Appendix 1.8**).

The transaction during 2015-16 included a sum of ₹0.87 crore, being loan drawn by Silk Growers & Reelers under Indo-Dutch scheme written off through book adjustments. The book adjustment was made by booking the expenditure under '2851-00-792-0-01-100- Village and Small Industries' and crediting HOA '6851-00-107-1-07- Loans and Small Industries'.

Information in respect of overdue principal and interest contained in Statement No.7 of Finance Accounts is incomplete, as only 22 out of 842 institutions in respect of whom the detailed accounts are maintained by the Heads of Departments /Chief Controlling Officers of the Government of Karnataka, have furnished the required information. Indian Government Accounting Standards (IGAS)-3 requires disclosure of loans that were sanctioned without specific terms and conditions governing such loans. Out of the 185 loans valued at ₹656.42 crore sanctioned by the State Government in 2015-16, 24 loans valued at ₹504.98 crore were sanctioned without specifying any terms and conditions. Details are available as additional disclosures under Statement No.18 of the Finance Accounts.

The Finance Department had stated (November 2014) that the department of Treasuries will be directed to categorically check whether GOs pertaining to release of loan amounts adhere to the instructions delineated in general loan GO issued by the FD in November 2013. It was observed in audit that even after the issue of instructions, compliance was poor.

1.8.6 Cash balances and investment of cash balances

Table 1.34 depicts the cash balances and investments made by the State Government during 2015-16.

Table 1.34: Cash balances and their investments

(₹ in crore)

	Opening Balance on 01-04-2015	Closing Balance on 31-03-2016	Increase (+)/ Decrease(-)
a)General cash balance			
Cash in treasuries	-	-	-
Deposits with RBI	4.84	(-)74.90	(-) 79.74
Deposits with other banks	-	-	-
Remittance in transit-Local	0.01	0.01	-
Sub Total	4.85	(-)74.89	(-)79.74
Investments held in cash balance Investment account	17,962.31	16,917.13	(-)1,045.18
Total (a)	17,967.16	16,842.24	(-)1,124.92
(b)Other cash balances and investments			
Cash with departmental officers viz. PWD officers, Forest Department, DCs	2.09	2.09	-
Permanent Advances for contingent expenditure with departmental officers	1.69	1.69	-
Investment of earmarked funds	5,929.96	10,272.21	4,342.25
Total (b)	5,933.74	10,275.99	4.342.25
Grand Total (a+b)	23,900.90	27,118.23	3,217.33

Source: Finance Accounts

Claims against Government are settled by preferring bills at treasuries, against which cheques are issued (by debit to the Consolidated Fund) to the claimants. The Major Head 8670 – Cheques and Bills is credited with the amount of each cheque and paired off with its encashment at the Agency Banks. Thus, credit balances under this head indicate the value of cheques that remained un-encashed. Article 75(1) of the Karnataka Financial Code, 1958, prescribes that the Treasury Officer should propose an Alteration Memorandum for the value of cheques outstanding for more than 12 months from the date of issue on the 15th of May each year. Due to non-compliance with these instructions by the treasury officers, the credit balance under this head increased from ₹12,758 crore in 2014-15 to ₹13,754 crore during 2015-16, which includes un-encashed cheques issued during January to March 2016.

Audit observed that the net credit under the account during 2015-16 was ₹996 crore. Action is required to be taken for analysis of data for cleaning up of the balances.

The cash balance of the State at the end of the year was ₹27,118 crore. The increase in the cash balance was 13 *per cent* over the previous year. The surplus cash was on account of release of funds by the Government of India to the State Government during 2015-16, which remained un-utilised and were released during 2016-17 through supplementary estimates to the extent of ₹60.40 crore.

Surplus cash balance was mainly due to market borrowings of ₹16,188 crore raised during 2015-16. There was a decrease of ₹1,045 crore in the investments held in cash balance investment account with RBI at the end of the year.

The surplus cash balance was invested partly in 14-day intermediate Treasury Bills of RBI with an average interest rate of 4.09 *per cent* per annum and partly in 91-day intermediate Treasury Bills of RBI with an average interest rate of 7.41 *per cent* against an average rate of 8.24 *per cent* per annum at which the borrowings were made. The interest received from investment in 91-day Treasury Bills during 2015-16 was ₹697.50 crore.

1.9 Assets and Liabilities

1.9.1 Growth and composition of assets and liabilities

In the existing Government accounting system, comprehensive accounting of fixed assets like lands and buildings owned by the Government is not done. However, Government accounts do capture the financial liabilities of the Government and the assets created out of the expenditure incurred. **Appendix 1.9** gives an abstract of such liabilities and assets as on 31 March 2016 compared with the corresponding position as on 31 March 2015.

Total liabilities, as defined in the KFRA, 2002 are the liabilities under the Consolidated Fund and the Public Account of the State. By an amendment to section 2(g) of the KFRA, 2002 brought out in February 2014, the scope of the total liabilities was enlarged to include borrowings by PSUs and Special Purpose Vehicles (SPVs) and other equivalent instruments where the principal and /or interest are to be serviced out of the budget of the Government of Karnataka.

The internal debt includes market loans, special securities issued to RBI and other negotiated loans. The Public Account liability includes small savings, provident funds etc., reserve funds and other deposits. The liabilities of the State as depicted in Finance Accounts, however, did not include pension, other retirement benefits payable to retired/retiring State Government employees/ guarantees/letters of comfort issued by the State Government and borrowings through SPVs, termed off-budget borrowings.

Assets comprise assets under the Consolidated Fund and cash. The assets under the Consolidated Fund consist of capital outlay on fixed assets – investments in shares of Companies and Corporations and loans and advances, which consist of loans for power projects and other development loans. The growth rate of components of assets and liabilities is summarized in **Table 1.35**.

Table 1.35: Summarized position of Assets and Liabilities

(₹ in crore)

Liabilities				Assets			
	2014-15	2015-16	*per cent*		2014-15	2015-16	*per cent*
Consolidated Fund	**1,05,585**	**1,22,547**	**16**	***Consolidated Fund***	**1,69,258**	**1,90,566**	**13**
a. Internal Debt	92,904	1,09,545	18	Capital outlay	1,56,042	1,76,753	13

Liabilities				Assets			
b. Loans and advances from GOI	12,681	13,002	2	Loans and advances	13,216	13,813	5
Off-budget borrowings	5,727	7,699	34	**Cash**	**23,901**	**27,118**	**13**
Public Account*	52,967	53,076	-				
a. Small savings, Provident Funds etc.,	20,176	22,262	10				
b. Reserve Funds	12,632	10,371	(-)18				
c. Deposits	20,159	20,443	1				

Source: Finance Accounts

**The liabilities are on net basis. It does not include investments from earmarked funds of ₹5,930 crore (2014-15) and ₹10,272 crore (2015-16)*

The growth rate of assets remained same at 13 *per cent* during 2014-15 and 2015-16, while that of liabilities inclusive of off-budget borrowings, decreased from 19 *per cent* in 2014-15 to 16 *per cent* in 2015-16.

The Finance Accounts reflected an amount of ₹1,09,545 crore as internal debt outstanding at the end of 2015-16 after taking into account the difference of ₹2,284.08 crore in the accounts of LIC, GIC, NABARD, NCDC etc. Further, the Reserve Bank of India (RBI) in its quarterly statement of outstanding balances of the Government of Karnataka as on 31 March 2016 reflected closing balance of Market Loans – not bearing interest as ₹0.15 crore. However, the Finance Accounts reflected an amount of ₹0.70 crore, indicating that reconciliation of loan balances (capital account) was required. It was also observed that certain loan balances which figure in the Finance Accounts had not been reckoned in the RBI books (two cases). In respect of six cases, there were differences which require reconciliation. In respect of five cases, the balances as per the books of accounts of the AG (A&E) tallied with those of RBI. Further, as per the communication from the Reserve Bank, there still exists a balance of ₹0.40 crore to be discharged in respect of Compensation bonds, the transactions of which are accounted under the minor head 106. However, these loans do not figure in the outstanding balances in the Finance Accounts. The loans and advances from the GOI reflected an amount of ₹13,002 crore as at the end of 2015-16.

In the furtherance of the recommendations of the XIII FC, the Ministry of Finance, GOI, in a series of orders, dated 29 February 2012, wrote off loans advanced to the State Government by various Ministries (except those advanced by the Ministry of Finance itself) as on 31 March 2010 (limited to current balances outstanding in the records of the Ministries) towards Central Plan and Centrally Sponsored Schemes. The Ministry of Finance permitted the State Governments to adjust the excess repayments of principal and interest made from the effective date of the order (31 March 2010) and its implementation against future repayments to the Ministry of Finance. In respect of the Government of Karnataka, this excess payment amounted to ₹68.66 crore, of which, the Ministry of Finance had adjusted ₹17.32 crore (June 2013) against the dues payable to the Ministry of Finance by end of

March 2013 and ₹5.48 crore (May 2014) against the dues payable by end of March 2014. The balance amount pending for adjustment was ₹45.87 crore (Principal ₹23.66 crore and Interest ₹22.21 crore). This had resulted in adverse balance (net debit) of ₹23.66 crore against the loans of the Ministries other than the Ministry of Finance in the books of the State Government.

The assets shown in the Finance Accounts (Statement No. 1 - Investment from earmarked funds - ₹10,272.21 crore) were understated to the extent of ₹142.86 crore. This is on account of the interest accrued on the investment of Consolidated Sinking Fund account made during 2012-13 which had not passed through the Government books.

Variation in Debt Servicing of Negotiated Loans and adverse balances of NCDC

The borrowings and the repayments in respect of negotiated loans (LIC, GIC, NABARD etc.,) reflected in the Finance Accounts are based on the departmental figures, as the office of the AG (A&E) does not keep scheme wise details of transactions in respect of these loans. The maturity profile in respect of these borrowings are furnished by the Finance Department which are brought in the Finance Accounts of the State Government.

The Budget Estimates of debt servicing of these negotiated loans for the year 2015-16 should be as depicted in Finance Accounts of 2014-15. From the Budget Estimates and the actual repayments made during 2015-16 and Finance Accounts for the year 2014-15 in respect of the negotiated loans, it was observed that there are variations in respect of principal repayments which are brought out in the maturity profile and the actual repayments made, the details of which are discussed in **paragraph 2.4.1.8** of this report. As regards the variations in the budget and the maturity profile so prepared being pointed in audit, Finance Department replied (July 2016) that the Budget was obtained inadvertently in respect of LIC loan and that in respect of GIC loan it was admitted that the provision made for the purpose was excessive.

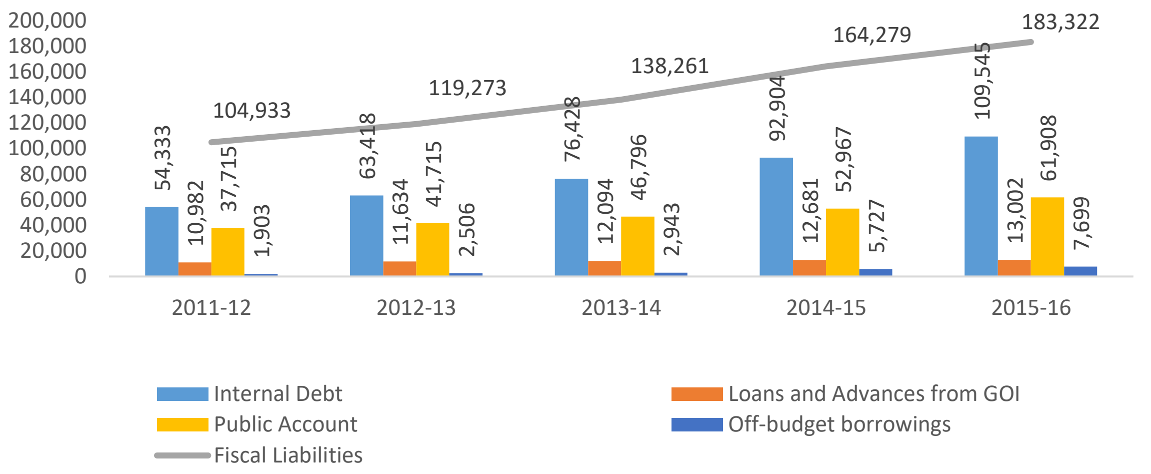
Further, in respect of HOA '6003-00-108-0-01-240-NCDC loans', the balances to the end of 31 March 2016 are (-) ₹117.63 crore. These adverse balances are due to the repayment of loans without routing the initial loans released by National Co-operative Development Corporation (NCDC) through the Consolidated Fund of the Government. Even though the adverse balances of NCDC loans in the Finance Accounts are being pointed by audit since 2008-09, Government is yet to clear these adverse balances.

The responsibility of clearing adverse balances rests with the Government as the initial and detailed accounts are being maintained by the departments of the Government. Public Accounts Committee also discussed (2010-11) the adverse balances of NCDC loans and recommended vide paragraph XVIII of the 13th Report of PAC on Report of Comptroller and Auditor General of India on State Finances (2009-10) for reconciliation of these adverse balances within six months.

1.9.2 Fiscal Liabilities

The trends in outstanding fiscal liabilities of the State are presented in **Appendix 1.4**. The composition of fiscal liabilities during the year 2011-12 to 2015-16 is presented in **Chart 1.12**.

Chart 1.12: Composition of outstanding Fiscal Liabilities (₹ in crore)



Source: Finance Accounts

The Fiscal liabilities of the State, their rate of growth, ratio of these liabilities to GSDP, revenue receipts and own resources as well as buoyancy of fiscal liabilities with respect to these parameters are brought out in **Table 1.36**.

Table 1.36: Fiscal Liabilities – basic parameters

	2011-12	2012-13	2013-14	2014-15	2015-16
Fiscal Liabilities (₹ in crore)	1,04,933	1,19,273	1,38,261	1,64,279	1,83,322
Rate of growth (*per cent*)	11.6	13.7	15.9	18.8	11.6
Ratio of fiscal liabilities to					
GSDP	0.24	0.23	0.23	0.24	0.25
Revenue Receipts	1.50	1.53	1.54	1.58	1.54
Own resources	2.08	2.07	2.07	2.19	2.27
Buoyancy ratio of fiscal liabilities to					
GSDP	0.83	0.69	1.02	1.35	1.57
Revenue Receipts	0.58	1.14	1.10	1.15	0.82
Own resources	0.56	0.96	1.03	1.52	1.44

Source: Finance Accounts

The Fiscal liabilities of the State increased by 75 *per cent* from ₹1,04,933 crore in 2011-12 to ₹1,83,322 crore in 2015-16 comprising Consolidated Fund liabilities (₹1,22,547 crore), Public Account liabilities (₹53,076 crore) and off-budget borrowings (₹7,699 crore). In 2014-15 and 2015-16, due to increased borrowings, the growth rate of fiscal liabilities was 19 *per cent* and 12 *per cent* respectively. Further, the ratio of fiscal liabilities to GSDP during 2015-16 remained at 24.91 *per cent* and the buoyancy of fiscal liabilities to revenue receipts was at 1.15 *per cent* and 0.82 *per cent* in 2014-15 and 2015-16 respectively. Also, the buoyancy ratio of fiscal liabilities to own resources gradually increased from 0.56 *per cent* in 2011-12 to 1.44 *per cent* in 2015-16.

1.9.3 Off-budget borrowings

The borrowings of the State Government are governed by Article 293 (1) of the Constitution of India. The State stood as guarantor for loans availed by Government Companies/ Corporations/ Societies. These Companies/ Corporations/ Societies borrowed funds from the market/financial institutions for implementation of various State plan programmes projected outside the State budget. The borrowings of these concerns ultimately turn out to be the liabilities of the State Government termed 'off-budget borrowings' and the Government had been repaying the loans availed of by these Companies/Corporations/Societies including interest through regular budget provision under capital account.

During 2015-16, capital expenditure of ₹20,713 crore included ₹399.73 crore towards servicing of principal amount of off-budget borrowings. However, the accounts of the entities for the year show disbursement as ₹401.70 crore towards off budget borrowings. **Table 1.37** captures the trend in the off-budget borrowings of the State during 2011-12 to 2015-16 while **Table 1.38** gives the entity-wise position of borrowings to the end of 2015-16.

Table 1.37: Trend in off-budget borrowings

(₹ in crore)

Year	2011-12	2012-13	2013-14	2014-15	2015-16
Amount as furnished by entities*	512	18.16	1,914.50	3,081.50	2,372.00

Source: As reported by the concerned entities

**Figures are yet to be reconciled with those indicated in Budget Overview*

Table 1.38: Entity-wise position of off-budget borrowings

(₹ in crore)

Company/Corporation/Board	Outstanding Off-budget borrowings*	Borrowings during 2015-16	Repayment during 2015-16	
			Principal	Interest
Krishna Bhagya Jala Nigam Limited	2,512.00	1,370.00	1.15*	270.81
Karnataka Neeravari Nigam Limited	1,051.16	610.00	98.84	127.56
Karnataka Road Development Corporation Limited	168.96	57.00	43.60*	17.72
Rajiv Gandhi Rural Housing Corporation Limited	1,392.33	-	207.01*	128.31
Karnataka Slum Development Board	13.73	-	8.02*	1.18
Karnataka Rural Infrastructure Development Limited	8.75	-	8.75	0.36
Karnataka State Police Housing and Infrastructure Development Corporation	69.71	-	24.81	7.07
Cauvery Neeravari Nigam Limited	500.00	335.00	-	38.17
Karnataka Residential Educational Institutions Society	3.82	-	3.82	0.22
Karnataka State Industrial Infrastructure Development Corporation Limited	5.53	-	5.53	0.71
Karnataka Power Transmission Corporation Limited	0.26	-	0.17	0.02
Total	**5,726.25**	**2,372.00**	**401.70**	**592.13**

**as there were differences in the closing balances of these entities (2014-15), the principal repayments have been adjusted to bring them in concordance with the closing balances of 2015-16.*

Taking into account the off-budget borrowings of the State, the total liabilities at the end of March 2016 worked out to ₹1,83,322 crore. The ratio of fiscal liabilities (inclusive of off-budget borrowings) to GSDP thus worked out to 24.91 *per cent* at the end of the year.

1.9.4 Transactions under Reserve Fund

Reserves and Reserve Funds are created for specific and well defined purposes under the Sector 'J' in the accounts of the State Government (Public Account). These funds are fed by contributions or grants from the Consolidated Fund of India or State or from outside agencies. The contributions are treated as expenditure under the Consolidated Fund. The expenditure relating to the fund is initially accounted for under the Consolidated Fund itself for which the vote of the Legislature is obtained. At the end of the year, at the time of closure of accounts, the expenditure relating to the fund is transferred to Public Account. The funds may further be classified as 'Funds carrying interest' or 'Funds not carrying interest'. Generally, the Reserve Funds are classified under the following three categories based on the sources from which they are fed.

- Funds accumulated from grants made by another Government and at times aided by public.
- Funds accumulated from sums set aside by the Union/State from the Consolidated Fund of India or Consolidated Fund of State, as the case may be, to provide reserves for expenditure to be incurred by them for particular purposes, e.g., Depreciation Fund.
- Funds accumulated from contributions made by outside agencies to the State Government.

As given in 'Notes to Accounts' for the year, out of the total outstanding balance of ₹20,643.36 crore available in various reserve funds as on 31 March 2016, the Government of Karnataka invested ₹10,272.20 crore (49.76 *per cent*). In addition, AG (A&E) had requested (June 2011) the State Government to review the necessity to continue two reserve funds, namely

- State Renewable Fund which has not recorded any transaction under it since 1999-2000 and,
- Guarantee Reserve Fund which needs to be replaced by Guarantee Redemption Fund in the light of recommendations of the TFC.

The operation of certain major reserve funds having a bearing on the liability position of the Government, its funding and expenditure are brought out below.

a) Consolidated Sinking Fund : The Government of Karnataka constituted a Consolidated Sinking Fund (CSF) in 2012-13 for the amortization of all loans as recommended by the Twelfth Finance Commission and transferred ₹1,000 crore towards its corpus in 2012-13. The fund is administered by the Reserve Bank of India which has invested the corpus in Government of India Securities. As per Government notification (February 2013), the State Government is required to make minimum annual contributions to the Fund at 0.50 *per cent* of the outstanding liabilities at the end of the previous financial year. During 2015-16, against the requirement of ₹792.76 crore, the State Government has contributed ₹1,070 crore to the fund. The balance under the fund at the end of the year was ₹2,070 crore. However, the interest of ₹142.86 crore accrued (2015-16) on re-investment made by the RBI from the fund did not pass through the accounts.

b) Delay in transfer of Environment Protection Fees (EPF) to Fund Account

Government of Karnataka imposed (February 2009) Environment Protection Fee at the rate of ₹84,000 per hectare on the non-forest land/ patta land/ Revenue land permitted to be used for mining/ quarrying. The order was effective for both ongoing as well as fresh mining/ quarrying leases. The receipts under Environment Protection Fee were required to be accounted under the functional major head 0853- Mines and Geology, as this function is vested with them. However, the receipts were accounted under the functional major head 0406 –Forestry and Wild Life, which was not in order.

Further in the Government Order dated 11.05.2015, the Government advised the department to create a Reserve Fund for EPF in the Public Account of the State by transferring the receipts collected under it till the end of 2014-15 and that future receipts may be accounted for under the departmental receipts of Mines and Geology under the HOA '0853-00-800-0-02-EPF'. Also, the entire process of collection, implementation, enforcement and expenditure management had to be carried out by the Department of Mines. However, the EPF receipts continue to be accounted for under the HOA '0406-01-800-0-11'.

During the supplementary budget of 2015-16, an amount of ₹75.00 crore was provided under HOA '2853-00-797-0-01' for transferring the EPF collected up to 2013-14 to the Reserve Fund and a deduct entry for ₹20.00 crore was made to adjust the related expenditure incurred from EPF under Demand No 18 – Industries and Commerce. Further a Government Order was issued (March 2016) to carry out the adjustment in accounts during 2015-16 for transfer of receipts of ₹75.00 crore into the fund and expenditure of ₹9.94 crore out of the fund.

It was noticed that though levy and collection of EPF was introduced in February 2009, it took seven years to create a fund. The amount collected was not utilized till 2014-15. Further, non-transfer of revenues to the fund account during those years had the effect of distorting the fiscal indicators of the relevant years. During the period from 2009-10 to 2015-16, though an amount of ₹102.39 crore was collected as revenues, only an amount of ₹75.00 crore was transferred to the fund account. Thus, short transfer of ₹27.39 crore to the fund account from the Consolidated Fund during 2015-16 resulted in overstatement of revenue surplus to that extent.

Finance Department stated (December 2016) that the balance of ₹27.39 crore has been proposed for transfer by obtaining Supplementary demand during 2016-17 for that purpose.

Inoperative Reserve Funds

Out of 76 reserve funds, 20 funds with balance of ₹11.01 crore under Major HOA '8115-Depreciation/Renewal Reserve Fund' and 14 funds with balance of ₹35.25 crore under Major HOA '8229 – Development and Welfare Funds' were liquidated during 2014-15 as per the directions of the State Government. During 2015-16, 22 funds were active with a balance of ₹7,915.75 crore and 21 funds remained inoperative with a balance of ₹2,455.24 crore.

1.9.5 Contingent liabilities

1.9.5.1 Status of guarantees

Guarantees are contingent liabilities on the Consolidated Fund of the State in case of default by the borrower for whom the guarantee was extended. The details of last five years are given in **Table 1.39.**

Table 1.39: Guarantees given by the State Government

(₹ in crore)

	2011-12	2012-13	2013-14	2014-15	2015-16
Maximum amount guaranteed	13,262	14,306	16,145	16,869	18,358
Outstanding amount of guarantees as at 1 April (including interest)	6,515	6,688	7,783	11,033	11,327
Percentage of outstanding amount guaranteed to total revenue receipts of the second preceding year	13	11	11	14	13

Source: Finance Accounts

The Karnataka Ceiling on Government Guarantees Act, 1999 provides for a cap on outstanding guarantees extended by the Government at the end of any year at 80 *per cent* of the State's revenue receipts of the second preceding year. The outstanding guarantees on 1st April of each year were within the prescribed limit.

The outstanding guarantees amounting to ₹13,324 crore at the end of the year 2015-16 (principal + interest) included guarantees extended to 169 institutions/ companies under irrigation (₹6,278 crore), co-operative (₹1,805 crore), finance (₹1,552 crore), power (₹560 crore), housing (₹2,250 crore), transport (₹184 crore) and other sectors (₹695 crore).

Against the total estimated guarantee commission of ₹376.97 crore receivable as reported by the State Government, only ₹138.37 crore was received during 2015-16. The guarantee commission received includes book adjustment made by the State Government towards the guarantee commission payable to it by KSIIDC (₹2.24 crore), Karnataka Slum Development Board (₹0.29 crore), Rajiv Gandhi Rural Housing Corporation Ltd. (₹40.26 crore), Mysore Lamps Works Ltd. (₹0.14 crore) and Karnataka Power Transmission Corporation Ltd. (₹14.03 crore) by way of subsidies / grants-in-aid. Consequently, the net shortfall in guarantee commission received was ₹295.56 crore (₹376.97 crore minus ₹81.41 crore, excluding book adjustment of ₹56.96 crore).

In the MTFPs (2015-19 and 2016-20) presented before the Legislatures, the Government had been stating that since the guarantees result in increase in contingent liability, they should be examined in the same manner as a proposal for a loan, taking into account, inter alia, the credit-worthiness of the borrower, the amount and risks sought to be covered by a sovereign guarantee, the terms of the borrowing, the justification and public purpose to be served, probabilities that various commitments will become due and possible costs of such liabilities, etc. The utility of having a functional Guarantee Reserve Fund and Guarantee Policy is under consideration with the State Government.

PAC also recommended (July 2015) that suitable efforts should be made to operate and continue the Guarantee Reserve Fund.

1.9.5.2 Incomplete Database on Guarantees

Karnataka Ceiling on Government Guarantees Act, 1999 came into force with effect from April 29, 1999 to fix the limits of Government Guarantees issued on behalf of Government Departments, Public Sector Undertakings, Local Authorities, Statutory Boards, and Corporations etc., for promoting fiscal discipline in the State. The act prescribes for a minimum guarantee fee at the rate of one *per cent*.

The responsibility for monitoring of guarantees was entrusted to the Directorate of Pensions, Small Savings and Asset-Liability Monitoring (ALM) section (April 2010). The existence of complete database about guarantees is a prequisite for effective monitoring of guarantees. The information furnished by the Finance Department is reckoned for the preparation of Statement No 20 (previously Statement No 9) of Finance Accounts.

During 2015-16 in the Supplementary Demand I, a sum of ₹632.89 lakh was provided to M/s Mysore Lamp Works Limited for various activities. Out of the amount so provided, ₹20.32 lakh was made through book adjustments which included the adjustment of Guarantee Commission dues of ₹14.19 lakh. A perusal of the Guarantee Statement No. 20 of Finance Accounts (previously Statement No. 9) revealed that, M/s Mysore Lamp Works Limited did not figure in the Statement on Guarantees.

Thus a book adjustment proposed in respect of an entity not figuring in the statement clearly showed that the database on guarantees was incomplete, not updated at regular intervals or cross checked at the time of finalisation of the Statements, thus lacking accuracy of disclosure on guarantees.

Finance department in its reply (July 2016) stated that the due from this entity had been inadvertently left out from the statement furnished by the department.

Adjustment of Guarantee Commission of Companies/ Corporations/ Public Sector Under takings (PSUs) under off budget borrowings

Majority of the Guarantee Commission dues receivable from Companies/ Corporations/ PSUs under off budget borrowings are through book adjustments. These adjustments are related to receipts from Companies/ Corporations/ PSUs, adjusted as guarantee fee received on the Consolidated Fund on one side, with an equivalent amount being provided as grants etc., out of the Consolidated Fund with the approval of the Legislature. These adjustments, though not made in cash are accounted as cash transactions for working out borrowing requirements of the Government. These book adjustments were being resorted to due to the fact that these Companies/ Corporations/ PSUs were not in a position to pay guarantee commission dues and it was being done merely to clean up the guarantee revenues due to Government as also the balance of the concerned Companies. The Government Accounts being carried out on cash basis, the book adjustment of guarantee commission dues, though revenue neutral, inflate revenues/expenditure of those years artificially. Government may consider amending the "Karnataka Ceiling on Government Guarantees Act, 1999" suitably to bring in a provision that all those Companies/ Corporations/ PSUs to whom Government is providing grants be excluded from the purview of the Act.

1.10 Debt Management

1.10.1 Debt Profile

The revenues of the Government are of two type's viz. current revenues which are termed as revenue receipts, realised through administration of taxes, user charges and grants received from GOI and capital receipts that comprise of borrowings, non-debt receipts and surplus from Public Account. For working out the borrowings, certain book adjustments are also reckoned as if these are cash transactions. Such transactions are in the nature of subsidy dues of electricity supply companies, student/elderly concession passes etc., which on one side are shown as expenditure and on the other, as revenues, under relevant receipt heads (tax/non-tax). Such accounting amounted to ₹1,598 crore during 2015-16. These transactions had the impact of showing the tax/non-tax revenues without actual cash flow. Such revenue, adjusted through book adjustment was ₹1,400 crore (tax revenues) and ₹163 crore (non-tax revenues) constituting 1.3 *per cent* of revenue receipts.

Table 1.40 gives details of outstanding fiscal liabilities of the Government under Consolidated Fund and Public Account compared with the per capita liability.

Table 1.40: Debt Profile of the State

(₹ in crore)

Borrowings through	2011-12	2012-13	2013-14	2014-15	2015-16
Open Market loans	30,770	39,920	53,326	69,419	84,334
Negotiated loans	2,972	3,425	3,372	3,318	3,482
NSSF loans	20,591	20,074	19,730	20,167	21,729
GOI loans	10,982	11,634	12,094	12,681	13,002

Borrowings through	2011-12	2012-13	2013-14	2014-15	2015-16
Public Account borrowings	37,715	41,714	46,796	52,968	53,076
Off budget borrowings	1,903	2,506	2,943	5,726	7,699
Total Fiscal Liabilities	1,04,933	1,19,273	1,38,261	1,64,279	1,83,322
Population (in crore)	6.11	6.11	6.11	6.11	6.11
Per capita debt ratio (in ₹)	17,174	19,521	22,629	26,887	30,004

Source: Finance Accounts

The per capita debt ratio has significantly increased from ₹17,174 in 2011-12 to ₹30,004 in 2015-16, an increase of 75 *per cent*.

1.10.2 Debt Sustainability

Apart from the magnitude of the debt of the State Government, it is important to analyse various indicators that determine the debt sustainability of the State. 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. This section assesses the sustainability of debt of the State Government in terms of debt as a percentage of GSDP, rate of growth of outstanding debt, interest payments/revenue receipts ratio and net debt available to the State. **Table 1.41** analyses the debt sustainability of the State according to these indicators for the period from 2011-12 to 2015-16.

Table 1.41: Debt sustainability indicators and trends

(in *per cent*)

Debt sustainability indicators	2011-12	2012-13	2013-14	2014-15	2015-16
Debt*/GSDP	15.04	14.41	14.71	15.41	16.65
Rate of growth of Outstanding Debt*	10.19	14.91	17.95	19.28	16.06
Rate of growth of GSDP	14.02	19.92	15.53	13.89	7.41
Average Interest rate of Outstanding Debt (Interest payments/(opening balance of Public debt + closing balance of Public Debt/2)	10.60	10.62	9.81	10.10	9.94
Interest/Revenue Receipts	9.5	9.5	9.0	9.4	9.6
Debt Repayment/Debt Receipts	35.48	27.68	22.08	22.00	19.50
Net Debt available to the State (₹in crore)	6,038	9,738	13,470	17,062	16,962

Source: Finance Accounts

**Excluding Public Account liabilities and Off Budget Borrowings.*

- The rate of growth of outstanding debt was 16.06 *per cent* during 2015-16, being 6 *per cent* increase over the year 2011-12 (10.19 *per cent*).
- Interest payments on debt and other liabilities totalling ₹11,343 crore constituted 9.6 *per cent* of revenue receipts during 2015-16, being 0.20 *per cent* increase over previous year. Though the decrease in growth rate of outstanding debt was marginal (3.22 *per cent*), the increase in interest payment/Revenue Receipt ratio from 9.4 in 2014-15 to 9.6 in 2015-16 was due to increased interest payments (by 15.70 *per cent*) as compared to revenue receipts (14.10 *per cent*) during 2015-16.
- The decrease in Debt Repayment/Debt Receipts ratio was mainly due to decrease in total debt receipts by ₹802 crore as compared to debt repayment made during 2015-16 which decreased by ₹702 crore.

- Decrease in net debt available to the state was mainly due to decrease in receipt under internal debt from ₹20,509 crore in 2014-15 to ₹19,801 crore in 2015-16 (**Appendix 1.4**) and by ₹94 crore under Loans and Advances from Government of India.

1.10.3 Debt stability

Fiscal liabilities are considered sustainable if the Government is able to service these liabilities over the foreseeable future and the debt-GSDP ratio does not grow to unmanageable proportions. A necessary condition for stability is that if the rate of growth of economy exceeds the cost of borrowings, the debt-GSDP ratio is likely to be stable provided primary balances are positive/ zero/ moderately negative. Primary revenue balance is the difference between revenue receipts and primary revenue expenditure and indicates whether the balance of revenue receipts left out after meeting current revenue expenditure is sufficient for meeting the interest expenditure. During 2011-12 to 2015-16, the primary revenue balance was positive and sufficient to meet incremental interest expenditure.

1.10.4 Sufficiency of incremental non-debt receipts

Another indicator of debt sustainability is the adequacy of incremental non-debt receipts of the State to cover the incremental interest liabilities and incremental primary expenditure. Debt sustainability is facilitated if the incremental non-debt receipts meet the incremental interest burden and the incremental primary expenditure. Negative resource gap indicates non-sustainability of debt while positive resource gap indicates sustainability of debt. The details for the last five years have been indicated in **Table 1.42**.

Table 1.42: Sufficiency of incremental non-debit receipts

(₹ in crore)

Sl. No.		2011-12	2012-13	2013-14	2014-15	2015-16
1	Incremental non-debt receipts	11,697	8,231	11,372	14,497	14,993
2	Incremental Interest Payments	963	850	573	1,777	1,539
3	Incremental Primary Expenditure	12,346	9,588	13,384	15,204	13,047
	Resource gap	(-)1,612	(-)2,207	(-)2,585	(-)2,484	407

The resource gap, which was negative from 2011-12 to 2014-15 turned positive during 2015-16. This was mainly on account of high growth of revenue receipts compared to the growth of total expenditure. It is observed that during 2015-16, the State could meet the incremental interest payments and incremental primary expenditure from its own resources.

1.10.5 Net availability of borrowed funds

Debt sustainability also depends on the ratio of debt redemption (principal plus interest payments) to total debt receipts and application of available borrowed funds. The ratio of debt redemption to debt receipts indicates the extent to which the debt receipts are used in debt redemption indicating the net availability of borrowed funds for capital spending. The debt redemption to debt receipts ranged between 19.5 *per cent* and 35.5 *per cent* during 2011-12 to 2015-16. During 2015-16, the debt redemption ratio dropped by 2.5 *per cent* points compared to the previous year.

1.10.6 Inordinate delay in remittance of Borrowings to Government Account – resultant loss of Interest

The negotiated Loans borrowed from various financial institutions form part of Internal Debt of the State Government. The borrowings are made from financial institutions like LIC, GIC, NABARD and NCDC etc. and the Budget provisions for these borrowings are made in the detailed estimates of revenue and other receipts which are placed before the Legislature along with the Budget documents. The borrowings [Rural Infrastructure Development Fund (RIDF) loans] from NABARD for the year 2014-15 were estimated at ₹1,170.33 crore against which the actual borrowings accounted for were ₹558.42 crore (HOA '6003-105').

Rule 4 (a) of Karnataka Financial Code, 1958 envisages that all transactions to which any Government servant in his official capacity is a party must, without any reservation, be brought to account and all moneys received should be paid in full within two days, into a Government treasury, to be credited to the appropriate account and made part of the general treasury balance. The receipts are to be accounted for within a reasonable time as the delay would have implication on the interest foregone.

A scrutiny of transactions for the year 2015-16 showed that in one case, NABARD had remitted ₹48.61 crore (25/26.03.2015) to the agency bank i.e. State Bank of Mysore (SBM) in the current account (No 64040265974) through RTGS. In ideal circumstances the amount should have been brought to accounts during 2014-15 itself. However, the SBM has transferred the funds to Government account in May 2015, thus affecting the net borrowings under E-Public debt. During 2015-16, it was noticed that there was delayed accounting of the borrowings of ₹525.42 crore due to delay in remittances which ranged between 1 day to 739 days resulting in loss of revenue (interest) to the extent of ₹2.98 crore approximately as shown in **Appendix 1.10.**

Non-remittance of Government money in time to the Consolidated Fund resulted in understatement of Public Debt receipts and fiscal indicator such as fiscal deficit of the concerned year besides being in contravention of Rule 4 (a) of KFC.

Finance department in its (September 2016) reply stated that the SBM had remitted ₹2.98 crore to the State Government Account under HOA'0049-04-190-0-12-Interest receipt' on account of delayed remittance of NABARD RIDF Loan.

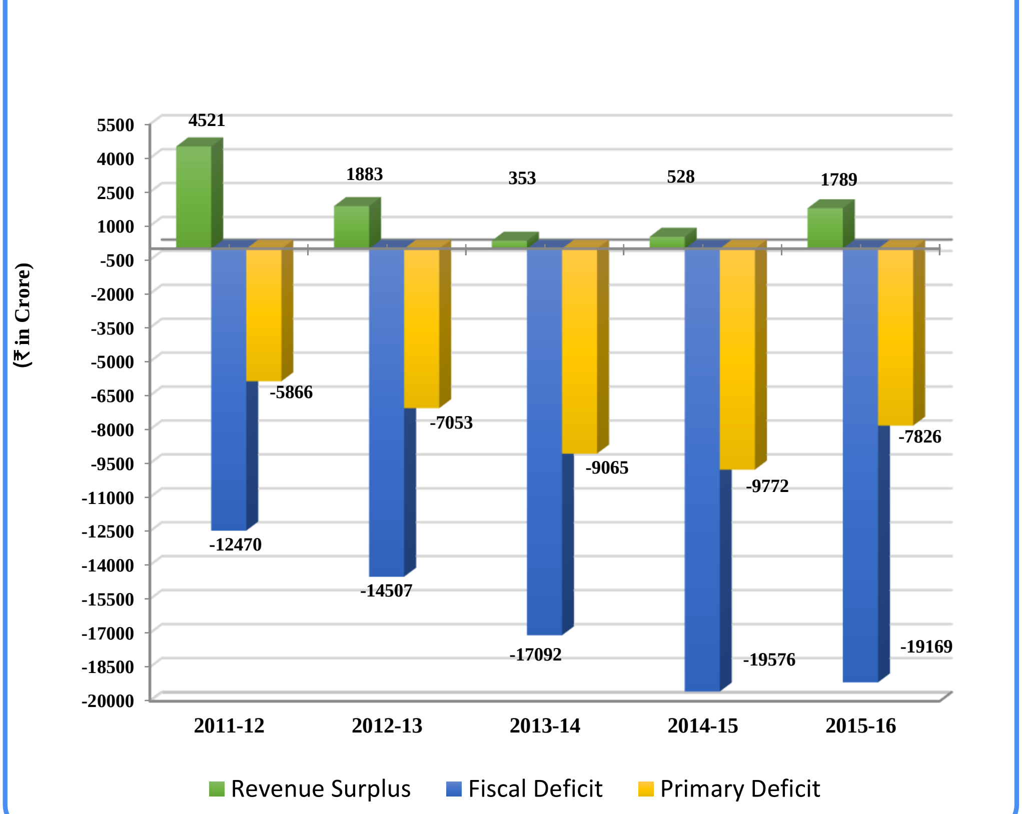
1.11 Fiscal Imbalances

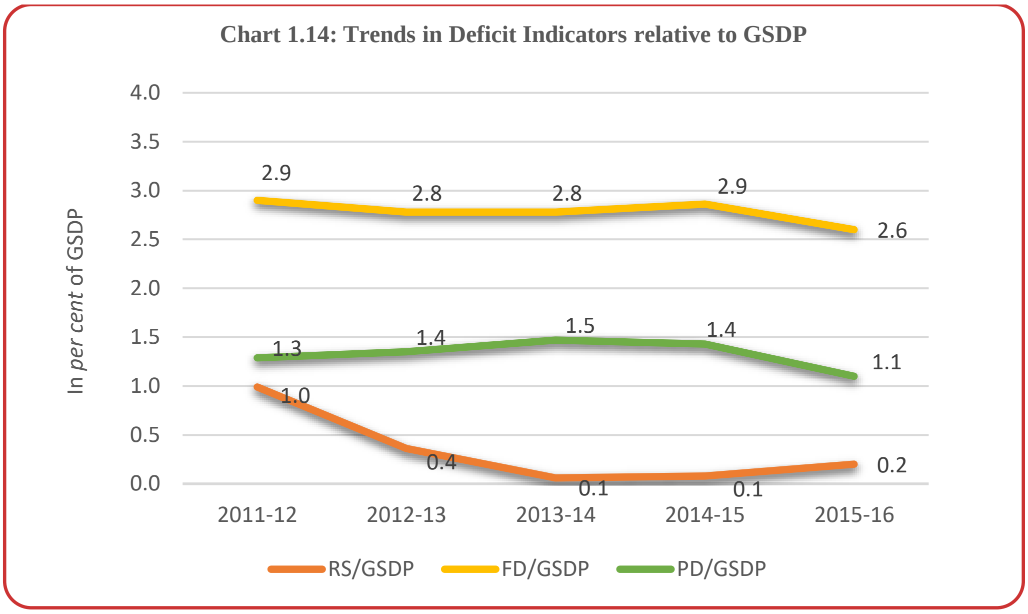
Three key fiscal parameters – revenue, fiscal and primary deficits – indicate the extent of overall fiscal imbalances in the Finances of the State Government during a specified period. The deficit in the Government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the Government. Further the ways in which the deficit is financed and the application of resources raised are important pointers to its fiscal health. This section presents trends, nature and 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 KFRA for the financial year 2015-16.

1.11.1 Trends in deficits

Chart 1.13 and **Chart 1.14** presents the trends in deficit indicators over the period 2011-12 to 2015-16.

Chart 1.13: Trends in Fiscal Indicators





The targets for revenue and fiscal deficits set for XIII FC along with their actual levels are given in **Table 1.43**.

Table 1.43: Outcome *vis-à-vis* targets under KFRA

Period	Revenue Deficit/Surplus		Fiscal Deficit (in *per cent*)	
	Targets as per KFRA	Actual	Targets as per KFRA	Actual
XIII FC (2010-15)				
2011-12	Maintain Revenue Surplus	Achieved the target	3.00	2.74
2012-13			3.00	2.78
2013-14			3.00	2.78
2014-15			3.00	2.86
XIV FC (2015-20)				
2015-16	Maintain Revenue Surplus	Maintained Revenue Surplus	3.00	2.60

The Government was able to maintain revenue surplus during 2011-12 to 2015-16. The fiscal target of wiping out revenue deficit by March 2006, as laid down in KFRA, was achieved by the State one year ahead in 2004-05, which was appreciable. Thereafter, the State maintained revenue surplus till 2015-16 with inter-year variations. In 2014-15, the revenue surplus increased by ₹175 crore over previous year and was ₹528 crore. However, during 2015-16 there was a substantial increase and revenue surplus was ₹1,789 crore.

The KFRA target of reducing fiscal deficit to GSDP ratio to less than three per cent was also achieved. Moreover, the capital expenditure was also compressed to the extent of ₹500 crore on account of adjustment of the debit to the Infrastructure Initiative Fund in Public Account.

In 2015-16, there was a moderate decrease in the ratio of fiscal deficit to GSDP as compared to the previous year and was 2.60 *per cent* considering the figure of GSDP as communicated by the State Government (₹7,35,975 crore) which was well within the target of 3 *per cent*.

Revenue Surplus

Revenue surplus represents the difference between revenue receipts and revenue expenditure. Revenue surplus helps to decrease the borrowings. The revenue surplus had drastically reduced from ₹4,521 crore in 2011-12 to ₹353 crore in 2013-14, on account of increased expenditure (committed) on revenue account under salaries, pensions, interest, subsidies and devolutions affecting the fiscal space, but increased by ₹1,261 crore to ₹1,789 crore during 2015-16, due to increase in net proceeds of state share of Union Taxes and duties and increase in respect of devolutions to local bodies (₹508.64 crore) which helped the Government to maintain surplus.

The growth rate of revenue receipts and revenue expenditure was 14 *per cent* and 13 *per cent* respectively during 2015-16, as a result of which there was considerable increase in revenue surplus. The factors responsible for the surplus on revenue account have been discussed in **paragraph 1.1.2.**

The State Government in MTFP (2016-20) had stated that 'the high percentage of committed revenue expenditure reduces maneuverability around expenditure decisions by the State and that the State has limited revenue space available after accounting for its committed expenditure needs'. Hence, the State Government needs to make medium term corrections on the expenditure side to moderate such committed expenditures and streamlining revenue collections.

Fiscal Deficit

Fiscal deficit represents the net incremental liabilities of the Government or its additional borrowings. The shortfall could be met either by additional public debt (internal or external) or by the use of surplus funds from Public Account. Fiscal deficit trends along with the trends of the deficit relative to key components are indicated in **Table 1.44.**

Table 1.44: Fiscal deficit and its parameters

(₹ in crore)

Period	Non-debit Receipts	Total expenditure	Fiscal deficit	Fiscal Deficit as *per cent* of		
				GSDP	Non-debt receipts	Total expenditure
2011-12	70,136	82,436	12,470	2.87	17.78	15.13
2012-13	78,367	92,874	14,507	2.79	18.51	15.62
2013-14	89,739	1,06,831	17,092	2.84	19.50	16.00
2014-15	1,04,236	1,23,812	19,576	2.86	18.78	15.81
2015-16	1,19,229	1,38,398	19,169	2.60	16.08	13.85

Source: Finance Accounts

During 2011-12 to 2015-16, fiscal deficit as a percentage of GSDP decreased gradually from 2.87 *per cent* to 2.60 *per cent*, with marginal variations in between. The fiscal deficit as *per cent* of GSDP, Non-debt receipts and Total expenditure decreased during 2015-16 over the previous year, on account of increased revenue surplus.

Primary Deficit

While fiscal deficit represents the need for additional resources in general, a part of such resources may be needed to finance interest payments in respect of States having deficit on revenue account. Interest payments represent the expenditure of past obligations and are independent of ongoing expenditure. To look at the imbalances of current nature, these payments need to be separated and deducted from the total imbalances. The primary deficit and its parameters for the last five years are indicated in **Table 1.45**.

Table 1.45: Primary deficit and its parameters

(₹ in crore)

Period	Fiscal Deficit	Interest Payments	Primary Deficit
2011-12	12,470	6,604*	5,866
2012-13	14,507	7,454*	7,053
2013-14	17,092	8,027*	9,065
2014-15	19,576	9,804*	9,772
2015-16	19,169	11,343*	7,826

Source: Finance Accounts

**includes interest payments of ₹542 crore, ₹621 crore, ₹190 crore, ₹400 crore and ₹597 crore towards off-budget borrowings during 2011-12, 2012-13, 2013-14, 2014-15 and 2015-16 respectively.*

During 2011-12 to 2015-16, the fiscal deficit was almost twice the amount of interest payments. Containing the committed expenditure, which constitutes the major chunk of the revenue expenditure, would enable the State Government to attain surplus on revenue account to a considerable extent. Since the costs of salary, pension and interest are inflexible, the expenditure on subsidies and grants-in-aid other than to local bodies, which are increasing steadily, requires utmost attention from the State Government.

1.11.2 Composition of fiscal deficit and its financing pattern

The financing pattern of fiscal deficit has undergone a compositional shift as reflected in the **Table 1.46**. Breakdown of fiscal deficit reveals the extent of various borrowings resorted to by the State to meet its requirement of funds over and above revenue and non-debt receipts.

Table 1.46: Components of fiscal deficit and its financing pattern

(₹ in crore)

Breakdown of fiscal deficit		2011-12		2012-13		2013-14		2014-15		2015-16	
		Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP
		(-)12,470	**2.87**	**(-)14,507**	**2.79**	**(-)17,092**	**2.84**	**(-)19,576**	**2.86**	**(-)19,169**	**2.60**
1	Revenue surplus	4,521	1.04	1,883	0.36	353	0.06	528	0.07	1,789	0.24
2	Net capital expenditure	15,417	3.55	15,446	2.96	16,859	2.80	19,612	2.86	20,361	2.76
3	Net loans and advances	1,574	0.36	944	0.18	586	0.10	492	0.07	597	0.08
Financing pattern of fiscal deficit*											
1	Market borrowings	6,207	1.43	9,149	1.76	13,406	2.23	16,093	2.34	14,914	2.03
2	Loans from GOI	637	0.15	652	0.13	461	0.08	586	0.09	321	0.04
3	Special securities issued to NSSF	(-)844	(-)0.19	(-)517	(-)0.10	(-)344	(-)0.06	437	0.06	1,563	0.21

Breakdown of fiscal deficit		2011-12		2012-13		2013-14		2014-15		2015-16	
		Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP	Amount	% of GSDP
4	Loans from financial institutions	208	0.05	454	0.09	(-)53	(-)0.01	(-)54	-	164	0.02
5	Small Savings, PF etc.,	1,398	0.32	1,732	0.33	2,107	0.35	2,156	0.31	2,086	0.28
6	Deposits and advances	1,410	0.32	2,511	0.48	2,840	0.47	3,702	0.54	284	0.04
7	Suspense and Miscellaneous	2,634	0.61	98	0.02	2,671	0.44	3,282	0.48	990	0.13
8	Remittances	(-)11	-	(-)32	(-)0.01	(-)12	-	(-)32	-	(-)17	-
9	Reserve Funds	2,761	0.63	1,362	0.26	135	0.02	1,547	0.23	2,081	0.28
10	Increase(-)/ decrease (+) in cash balance	(-)1,942	(-)0.45	(-)902	(-)0.17	(-)4,119	(-)0.68	(-)8,141	(-)1.19	(-)3,217	(-)0.43
11	Net of Contingency Fund transactions	12	-	-	-	-	-	-	-	-	-
	Total	**12,470**	**2.87**	**14,507**	**2.79**	**17,092**	**2.84**	**19,576**	**2.86**	**19,169**	**2.60**

Source: Finance Accounts

**All these figures are net disbursements/outflows during the year.*

The components of fiscal deficit are Deduct Revenue Surplus, Net Capital Expenditure and Net Loans and Advances. Since the State had attained revenue surplus in 2004-05 itself, the surplus on revenue account along with market borrowings, loans from GOI etc., were utilized to finance capital expenditure. The capital expenditure could be financed by revenue surplus to the extent of 29, 12 and 2 *per cent* in 2011-12, 2012-13 and 2013-14 respectively. In 2014-15 and 2015-16, revenue surplus could finance 3 and 9 *per cent* of capital expenditure.

In 2015-16, there was substantial decrease in market borrowings and its share in financing fiscal deficit decreased to 78 *per cent*. There was decrease in Small Savings, Provident Fund and Deposits and Advances over the previous year and increase in loans from financial institutions. There was also decrease in suspense and miscellaneous balances which comprised transactions relating mainly to cheques and bills, the net transactions of which were added for financing the fiscal deficit. There was a considerable increase in the receipts during 2015-16 under special securities issued to NSSF.

1.11.3 Quality of deficit/surplus

The position of primary deficit with bifurcation of factors are given in **Table 1.47**.

Table 1.47: Primary deficit/surplus-Bifurcation of factors

(₹ in crore)

Year	Non-debt receipts	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)**
2011-12	70,136	58,511	15,506	1,815	75,832	11,625	(-)5,866
2012-13	78,367	68,839	15,479	1,102	85,420	9,528	(-)7,053
2013-14	89,739	81,162	16,947	695	98,804	8,577	(-)9,065
2014-15	1,04,236	93,810	19,622	576	1,14,008	10,426	(-)9,772
2015-16	1,19,229	1,05,685	20,713	657	1,27,055	13,544	(-)7,826

Source: Finance Accounts

Primary deficit which was ₹5,866 crore during 2011-12 increased to ₹7,826 crore during 2015-16.The interest payment with respect to fiscal deficit was 59 *per cent* during 2015-16.

1.12 Follow up

The Report of the C&AG of India on State Finances for the year 2009-10 was discussed by the PAC during the period May 2011 to August 2011. The report containing the recommendations was placed before the Legislature in December 2011. Compliance to the recommendations of the PAC, the Action Taken Note were placed before the PAC for its consideration during September 2014. The PAC discussed the Action Taken Note submitted by the Government in five sittings and submitted its report on the Action Taken Note of the Government on 20-07-2015.

1.13 Conclusion and recommendations

Fiscal Position

The State continued to maintain revenue surplus during 2011-12 to 2012-13 to 2015-16 and kept fiscal deficit relative to GSDP below the limit prescribed under KFRA.

During 2015-16, revenue surplus was ₹1,789 crore which was partly on account of compression of revenue expenditure of ₹213.37 crore relating to Sarvasiksha Abhiyan transactions, write back of ₹419.10 crore for the years 2013-14 and 2014-15 under Zilla Panchayat Fund II and Taluk Panchayat Fund and write back of ₹18.70 crore of unutilised funds relating to XIII FC grants contributed in maintaining surplus of Revenue Account.

The fiscal deficit during 2015-16 was 2.60 *per cent* of GSDP (₹7,35,975 crore), which was within the limit laid down under the KFRA as the capital expenditure was also compressed to the extent of ₹2,418 crore on account of adjustment of the expenditure under the Consolidated Fund to the Infrastructure Initiative Fund in Public Account.

Recommendation: Timely and proper accounting adjustments need to be carried out to reflect the true and fair picture of the fiscal parameters.

State's own resources

The ratio of State's tax revenue to GSDP was between 10.24 and 10.70 *per cent* during 2011-12 to 2015-16 indicating attainment of the saturation level. However, there was no improvement in the ratio of non-tax revenue to GSDP and it continued to be less than one *per cent* of the GSDP during 2011-12 to 2015-16 also.

Recommendation: Revision of the rates of user charges etc., of the sources for Non-tax revenues is required to be considered from time to time as recommended by Expenditure Reforms Commission.

Revenue expenditure

During 2015-16 there was 18 *per cent* growth under social sector over the previous year and the share of expenditure on social services to total revenue expenditure increased by 2 *per cent* over the previous year and was at 40 *per cent* in 2015-16. The growth in expenditure on economic services remained at 13 *per cent* during 2014-15 as well as in 2015-16.

The share of plan revenue expenditure to total revenue expenditure increased from 33 *per cent* in 2014-15 to 34 *per cent* in 2015-16.

Eighty one *per cent* of revenue expenditure constituted of committed expenditure on salaries, pensions, interest payments, subsidies, grants-in-aid and financial assistance, administrative expenditure and devolution to local bodies. Expenditure on subsidy of ₹17,062 crore contained implicit subsidy amounting to ₹3,913 crore which was in the form of financial assistance under various schemes of socio-economic services.

Recommendation: Since the costs of salary, pension and interest are inflexible, the expenditure on subsidies, grants-in-aid other than to local bodies, which are increasing steadily, requires utmost attention from the State Government. Adequate priority needs to be given to both education and health sectors as the ratio under both these sectors are below the GCS average during 2015-16. Accounting adjustments should be done according to the orders issued and should not be belatedly resorted to resulting in distortion of the expenditure pattern.

Quality of expenditure

The share of capital expenditure to total expenditure during 2015-16 (15 *per cent*) decreased by one *per cent* from that of previous year which was mainly on account of debiting capital expenditure on infrastructure projects to fund account in Public Account of ₹2,418 crore. The percentage of developmental expenditure to total expenditure increased to 73 *per cent* in 2015-16 from 72 *per cent* in 2014-15.

Funds aggregating ₹1,495 crore were locked up in incomplete projects at the end of 2015-16.

The return from investment of ₹61,356 crore as of 31 March 2016 in Companies/Corporations was negligible (₹69.40 crore). The investment included ₹25,002 crore (41 *per cent*) to Companies/Corporations which were under perennial loss. A Government Company 'Bangalore Bioinnovation Centre' was established without the approval of the Cabinet.

Recommendation: The State Government should formulate guidelines for quick completion of incomplete projects and strictly monitor reasons for time and cost overrun with a view to take corrective action. The State Government should review the working of State Public Sector Undertakings incurring huge losses and take appropriate action for their closure/revival.

Funds and other Liabilities

Reserve funds of the State viz., corpus fund of Guarantee Redemption Fund was not created/ revived. During 2015-16, the transactions relating to the Consolidated Sinking Fund included interest of ₹142.86 crore accrued on re-investment made by the RBI, which did not pass through the accounts and inordinate delay in transfer of Environment Protection Fees to the Fund Account (₹75.00 crore) and Green Tax collections of ₹45.90 crore was not accounted and utilised.

Recommendation: Rules with regard to administration and investment pattern of various reserve funds are required to be framed. Also, expenditure should match the revenues so as to liquidate the balances within a reasonable period of time. Amendment to the Guarantees Act may be considered to exclude the Companies/Corporations/PSUs who are not in a position to pay the guarantee commission dues to the Government from the purview of the act to avoid book adjustments of Guarantee Commission dues.

Debt sustainability

Open Market Loans formed a predominant share (46 *per cent*) in the total fiscal liabilities of the State. The burden of interest payments measured by interest payments to revenue receipts ratio (IP/RR) hovered between 9.0 *per cent* and 9.6 *per cent* during 2011-12 to 2015-16. The net debt available to the State during 2015-16 (₹16,962 crore) decreased by one *per cent* when compared to the previous year. Non-remittance of borrowings to Consolidated Fund resulted in understatement of Public Debt receipts during 2015-16.

Recommendation: Parking of funds especially with reference to developmental schemes either in nationalized banks/deposit account should be avoided. The accounting adjustments should be in accordance with the principles governing the adjustments. Delay in remittance of borrowings to Government Account should be avoided. Interest on Off-budget borrowings should form part of calculation of IP/RR ratio.