

# CHAPTER I

## FINANCES OF THE STATE GOVERNMENT

### 1.1 Introduction

The accounts of the State Government are kept in three parts (i) Consolidated Fund, (ii) Contingency Fund and (iii) Public Account (**Appendix 1.1-Part A**). The Finance Accounts of the Government of Karnataka are laid out in 19 statements, presenting receipts and expenditure, revenue as well as capital, in the Consolidated Fund, the Contingency Fund and the Public Account of the State. The layout of the Finance Accounts is depicted in **Appendix 1.1-Part B**.

#### 1.1.1 Summary of receipts and disbursements

Table 1 below summarises the finances of the Government of Karnataka for the year 2006-07 as compared to the previous year, covering revenue receipts and expenditure, capital receipts and expenditure, contingency fund transactions and public account receipts/disbursements as emerging from statement-1 and other detailed statements of Finance Accounts.

**Table 1: Summary of receipts and disbursements**

(Rupees in crore)

2005-06	Receipts	2006-07	2005-06	Disbursements	2006-07		
					Non-Plan	Plan	Total
<b>Section-A: Revenue</b>							
<b>30,352.05</b>	<b>Revenue receipts</b>	<b>37,586.94</b>	<b>28,040.89</b>	<b>Revenue expenditure</b>	<b>25,582.89</b>	<b>7,852.54</b>	<b>33,435.43</b>
18,631.55	Tax revenue	23,301.03	10,035.82	General services	10,343.20	76.22	10,419.42
3,874.71	Non-tax revenue	4,098.41	8,898.79	Social services	6,728.55	4,208.16	10,936.71
4,213.42	State's share of Union taxes and duties	5,374.33	7,947.32	Economic services	6,901.58	3,538.66	10,440.24
3,632.37	Grants from GOI	4,813.17	1,158.96	Grants-in-aid/Contributions	1,609.56	29.50	1,639.06
<b>Section-B: Capital and others</b>							
---	Misc. capital receipts	---	5,821.93	Capital outlay	131.79	8,410.78	8,542.57
			217.92	General services	---	320.94	320.94
			1,105.30	Social services	0.79	1,291.83	1,292.62
			4,498.71	Economic services	131.00	6,798.01	6,929.01
123.55	Recoveries of loans and advances	59.97	299.60	Loans and advances disbursements	51.12	306.11	357.23
5,663.55	Public debt receipts	3,545.94	810.86	Repayment of public debt	1,749.37		1,749.37
38.91	Contingency fund (recoupment)	--		Contingency fund			13.28
38,025.00	Public account receipts	47,040.04	36,702.25	Public account disbursements			42,636.88
2,079.11	Opening cash balance	4,606.64	4,606.64	Closing cash balance			6,104.77
<b>76,282.17</b>	<b>Total</b>	<b>92,839.53</b>	<b>76,282.17</b>	<b>Total</b>	<b>27,515.17</b>	<b>16,569.43</b>	<b>92,839.53</b>

Following are the changes in receipts and disbursements during 2006-07 over the previous year:

- Revenue receipts grew by Rs.7,235 crore due to rise in tax revenue (Rs.4,669 crore), grants from GOI (Rs.1,181 crore) and State's share of union taxes and duties (Rs.1,161 crore) and non-tax revenue (Rs.224 crore).

- Revenue expenditure increased by Rs.5,394 crore. Increase was mainly under social services sector (Rs.2,038 crore) and economic services sector (Rs.2,493 crore).
- Capital outlay was more by Rs.2,721 crore. Significant enhanced outlay was under economic services sector (Rs.2,430 crore).
- Public debt receipts decreased by Rs.2,118 crore mainly due to reduction in internal debt receipts (Rs.2,103 crore), while the repayments were more by Rs.939 crore.
- Recovery of loans and advances was less by Rs.64 crore, while the disbursements were more by Rs.57 crore.
- Public account receipts and disbursements increased by Rs.9,015 crore and Rs.5,935 crore respectively.
- Cash balance of the State Government increased by Rs.1,498 crore.

### 1.1.2 Fiscal position by key indicators

The fiscal position of the State Government as reflected by the key indicators during the current year as compared to the previous year is given in table 2:

**Table : 2**

(Rupees in crore)

2005-06	Serial number	Major aggregates	2006-07
<b>30,352</b>	<b>1</b>	<b>Revenue receipts (2+3+4)</b>	<b>37,587</b>
18,632	2	Tax revenue	23,301
3,875	3	Non-tax revenue	4,099
7,845	4	Other receipts	10,187
<b>124</b>	<b>5</b>	<b>Non-debt capital receipts</b>	<b>60</b>
		Loans and advances recovered	
<b>30,476</b>	<b>6</b>	<b>Total receipts (1+5)</b>	<b>37,647</b>
<b>23,032</b>	<b>7</b>	<b>Non-plan expenditure (8+10+11)</b>	<b>25,766</b>
22,972	8	on Revenue account	25,583
3,765	9	Interest payments	4,236
16	10	on Capital account	132
44	11	Loans and advances disbursed	51
<b>11,131</b>	<b>12</b>	<b>Plan expenditure (13+14+15)</b>	<b>16,569</b>
5,069	13	on Revenue account	7,852
5,806	14	on Capital account	8,411
256	15	Loans and Advances disbursed	306
<b>34,163</b>	<b>16</b>	<b>Total expenditure (7+12)</b>	<b>42,335</b>
<b>- 3,687</b>	<b>17</b>	<b>Fiscal deficit [(1+5) – 16]</b>	<b>- 4,688</b>
<b>2,311</b>	<b>18</b>	<b>Revenue surplus [1-(8+13)]</b>	<b>4,152</b>
<b>78</b>	<b>19</b>	<b>Primary deficit (-) (6-16+9)/ Primary surplus (9-17)</b>	<b>-452</b>

During 2006-07, revenue receipts grew by Rs.7,235 crore (24 per cent) as against the increase in revenue expenditure by Rs.5,394 crore (19 per cent) resulting in increase of surplus on revenue account. Given the increase of Rs.1,841 crore in revenue surplus, growth of Rs.2,778 crore in capital expenditure (including loans and advances) and reduction of Rs.64 crore in non-debt capital receipts, resulted in increase of fiscal deficit by Rs.1,001 crore. The increase in fiscal deficit along with an increase of Rs 471 crore in

interest payments turned the primary surplus of Rs 78 crore in 2005-06 to a deficit of Rs 452 crore in 2006-07.

## 1.2 Methodology adopted for the assessment of fiscal position

The trends in the major fiscal aggregates of receipts and expenditure as emerged from the statements of Finance Accounts were analysed over the period from 2001-02 to 2006-07. The norms/ceilings prescribed by the Twelfth Finance Commission (TFC) as well as its projections and projections made by the State Government in their Fiscal Responsibility Act and in other statements required to be laid before legislature under the Act are used to make assessment of the trends and pattern of major fiscal aggregates during the current year. Assuming that Gross State Domestic Product (GSDP)<sup>1</sup> as published by the Director of Economics and Statistics, Government of Karnataka (table 3) is the good indicator of the performance of the State's economy, major fiscal aggregates like tax and non-tax revenue, revenue and capital expenditure, internal debt and revenue and fiscal deficits have been presented as percentage to the GSDP at current market prices. For revenue receipts, revenue expenditure, etc., buoyancy projections are provided to estimate the range of fluctuations with reference to the base represented by GSDP. The key indicators adopted for the purpose are (i) trends in aggregate receipts, (ii) application of resources (iii) assets and liabilities and (iv) management of deficits. Observations made also take into account the cumulative impact of resource mobilisation efforts, debt servicing and corrective fiscal measures. The overall financial performance of the State Government as a body corporate has been presented by the application of a set of ratios commonly adopted for the relational interpretation of fiscal aggregates. In addition, selected indicators of financial performance of the Government are listed in this section; some of the terms used in this context are explained in **Appendix 1.1-Part C**. Summarised financial position of the State Government as on 31 March 2007, abstract of receipts and disbursement for the year 2006-07, sources and application of funds and the time series data on State Government finances are given in **Appendices 1.2 to 1.5**.

**Table 3: Growth of GSDP**

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
GSDP (Rupees in crore)	107,933	117,492	128,556	148,541	170,741 <sup>φ</sup>	194,009 <sup>μ</sup>
Rate of growth ( <i>per cent</i> )	4.8	8.9	9.4	15.5	14.9	13.6

<sup>φ</sup> quick estimates, <sup>μ</sup> anticipated estimates

### 1.2.1 Fiscal reforms path in Karnataka

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 2000-01 to 2004-05 based on broad parameters of fiscal correction laid down by the Eleventh Finance Commission (EFC). MTFP

<sup>1</sup> GSDP is defined as the total income of the State or the marked value of goods and services produced using labour and all other factors of production.

became a rolling annual document to report on the actual performance of the State against fiscal targets of the previous year and to put in place a multi-year medium term reform framework dovetailed to the budgetary exercise.

The statutory backing for MTFP was provided by the Karnataka Fiscal Responsibility Act, 2002 (Act), which came into force from 1 April 2003. The Act aims to ensure fiscal stability and sustainability, enhance the scope for improving social and physical infrastructure and human development by achieving revenue surplus, reducing fiscal deficit, removing impediments to the effective conduct of fiscal policy and prudent debt management through limits on borrowings, debt and deficits, greater transparency in fiscal operations by the use of medium-term fiscal framework.

To give effect to the fiscal management principles, the Act prescribed the following fiscal targets for the State Government.

- elimination of revenue deficit by the end of the financial year 2005-06.
- reduction of fiscal deficit to not more than three *per cent* of the estimated GSDP by the end of the financial year 2005-06.
- limiting the total liabilities to not more than 25 *per cent* of the estimated GSDP within a period of 13 financial years, i.e., by the end of the financial year 2014-15.
- maintaining outstanding guarantees within the limit stipulated under the Karnataka Ceiling to Government Guarantees Act, 1999.

Revenue and fiscal deficits may exceed the specified limits due to unforeseen demands on the State finances on account of natural calamities to the extent of actual fiscal costs attributable to the situation.

### ***1.2.2 Fiscal policy statements 2006-07***

The State Government has laid the MTFP for the period 2006-10 before the State Legislature along with the annual budget for the 2006-07, which *inter alia* contained:

- medium term fiscal objectives of the State Government.
- evaluation of the performance of the prescribed fiscal indicators in the previous year.
- recent economic trends and prospects for growth and development.
- strategic priorities and key fiscal policies of the Government and evaluation of their consistency.
- four year rolling targets.
- assessment of sustainability relating to the revenue deficit and the use of capital receipts for productive purposes.

### 1.2.3 Roadmap to achieve the fiscal targets as laid down in the Act

Keeping in view the fiscal targets laid down in the Act, the anticipated annual rate of reduction of fiscal deficit of the States worked out by the Government of India for the TFC award period, the State Government has developed its own Fiscal Correction Path (FCP) indicating the milestones of outcome indicators with target dates of implementation during the period from 2004-05 to 2008-09 (**Appendix 1.6**). The State's MTFP (2006-10) presented along with budget for 2006-07 contained budget estimates of outcome indicators. The variations between FCP and MTFP regarding significant indicators for the year 2006-07 were as given in the table below:

**Table 4**

(Rupees in crore)

Outcome indicator	FCP projection	Budget estimates (MTFP)
Revenue receipts	32,471	35,875
Revenue expenditure	31,083	34,341
Expenditure on capital account	4,316	5,088
Revenue surplus	1,388	1,535
Fiscal deficit	5,603	5,211

The State achieved the fiscal targets laid down in the Act one year ahead, with the year 2004-05 ending in revenue surplus (Rs.1,638 crore) and fiscal deficit for the year (Rs.3,600 crore) at less than three *per cent* of GSDP. The revenue surplus increased to Rs.2,311 crore and Rs.4,152 crore for the years 2005-06 and 2006-07 respectively. The fiscal deficits for the years 2005-06 (Rs.3,687 crore) and 2006-07 (Rs.4,688 crore) were also below three *per cent* of GSDP. Outstanding guarantees given by the Government (Rs.9,879 crore) were within the prescribed limit of 80 *per cent* of the State's revenue receipts of the second preceding year. The ratio of fiscal liabilities to GSDP continued to decline from 2004-05 and was around 30 *per cent* in 2006-07. As a result, the State got the full benefit of incentive grants of Rs.286 crore for the EFC award period. Under GOI's scheme of States' Debt Consolidation and Relief Facility (DCRF)<sup>2</sup>, the State got the benefit of interest relief of Rs.568 crore for the years 2005-06 (Rs.292 crore) and 2006-07 (Rs.276 crore) along with waiver of GOI loan of Rs.716 crore.

### 1.2.4 Mid-term review of fiscal situation

According to the half-yearly review report for the current year placed before the State Legislature in compliance to the provisions of the Act, realisation of revenues upto end of September 2006 was on target. Revenue receipts at the year end exceeded the budget estimates. Revenue expenditure was less than the budgeted amount. Capital expenditure however, was more than the budget estimates.

<sup>2</sup> In pursuance of the recommendations of the TFC for fiscal consolidation and elimination of revenue deficit of the States, Government of India formulated a scheme of DCRF under which general debt relief is provided by consolidating and rescheduling at substantially reduced rates of interest the Central loans granted to States on enacting the Fiscal Responsibility Act and debt waiver is granted based on fiscal performance, linked to the reduction of revenue deficits of States.

### 1.3 Trends and composition of aggregate receipts

Resources of the State Government consist of revenue receipts and capital receipts. Revenue receipts consist of tax revenue, non-tax revenue, State's share of union taxes and duties and grants-in-aid from the GOI. Capital receipts comprise miscellaneous capital receipts such as proceeds from disinvestments, recovery of loans and advances, debt receipts from internal sources (market loans, borrowings from financial institutions/commercial banks) and loans and advances from GOI as well as accruals from public account.

Sources of receipts under different heads and GSDP during 2001-07 are indicated in table 5.

**Table 5: Trends in growth and composition of aggregate receipts**

(Rupees in crore)

Sources of State's receipts	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>I. Revenue receipts</b>	<b>15,321</b>	<b>16,169</b>	<b>20,760</b>	<b>26,570</b>	<b>30,352</b>	<b>37,587</b>
<b>II. Capital receipts</b>	<b>5,181</b>	<b>6,361</b>	<b>8,052</b>	<b>8,556</b>	<b>5,788</b>	<b>3,606</b>
Recovery of loans and advances	35	928	64	47	124	60
Public debt receipts	5,146	5,433	7,988	8,509	5,664	3,546
Miscellaneous capital receipts	Nil	Nil	Nil	Nil	Nil	Nil
<b>III. Contingency fund</b>	<b>54</b>	<b>8</b>	<b>0</b>	<b>41</b>	<b>39</b>	<b>0</b>
<b>IV. Public account receipts</b>	<b>28,502</b>	<b>27,879</b>	<b>30,513</b>	<b>36,325</b>	<b>38,025</b>	<b>47,040</b>
a. Small savings, Provident fund etc.	1,286	1,399	1,422	1,521	1,651	1,748
b. Reserve fund	233	338	396	570	1,289	1,656
c. Deposits and advances	14,150	13,428	14,686	17,211	15,926	19,073
d. Suspense and miscellaneous	10,755	10,606	11,308	14,390	16,393	20,772
e. Remittances	2,078	2,108	2,701	2,633	2,767	3,791
<b>Total receipts</b>	<b>49,058</b>	<b>50,417</b>	<b>59,325</b>	<b>71,492</b>	<b>74,204</b>	<b>88,233</b>

Total receipts increased by 80 per cent from Rs.49,058 crore in 2001-02 to Rs.88,233 crore in 2006-07, of which increase of revenue receipts was by 145 per cent from Rs.15,321 crore to Rs.37,587 crore. While non debt receipts increased by 71 per cent from Rs.35 crore in 2001-02 to Rs.60 crore in 2006-07, public account receipts increased by 65 per cent from Rs.28,502 crore to Rs.47,040 crore during the period. Public debt receipts, which create future repayment obligations, decreased from Rs.5,146 crore to Rs.3,546 crore, indicating the improvement fiscal position of the State.

#### 1.3.1 Revenue receipts

Statement-11 of the Finance Accounts details the revenue receipts of the Government. Revenue receipts are linked to economic activity and GSDP is its natural base. Apart from the quantum and rate of growth of revenue receipts, it is equally important to look at these receipts relative to this base and its expansion over time. Overall revenue receipts, their annual rate of growth, ratio of these receipts to GSDP and their buoyancy are indicated in table 6.

**Table 6 : Revenue receipts – Basic parameters**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Revenue receipts (RR)</b>	<b>15,321</b>	<b>16,169</b>	<b>20,760</b>	<b>26,570</b>	<b>30,352</b>	<b>37,587</b>
State's own taxes	9,853 (64)	10,440(65)	12,570 (61)	16,072(60)	18,632(61)	23,301(62)
Non-tax revenue	1,094 ( 7)	1,278 ( 8)	2,958 (14)	4,473(17)	3,875(13)	4,099(11)
Central tax transfers	2,623 (17)	2,786 (17)	3,245 (15)	3,878(15)	4,213(14)	5,374(14)
Grants-in-aid	1,751 (12)	1,665 (10)	1,987 (10)	2,147( 8)	3,632(12)	4,813(13)
<b>Rate of growth of RR (per cent)</b>	<b>3.4</b>	<b>5.5</b>	<b>28.4</b>	<b>27.9</b>	<b>14.2</b>	<b>23.8</b>
<b>RR-GSDP (per cent)</b>	<b>14.2</b>	<b>13.8</b>	<b>16.1</b>	<b>17.9</b>	<b>17.8</b>	<b>19.4</b>
<b>Revenue buoyancy w.r.t GSDP (ratio)</b>	<b>0.7</b>	<b>0.6</b>	<b>3.0</b>	<b>1.8</b>	<b>1.0</b>	<b>1.7</b>
<b>State's own taxes buoyancy w.r.t GSDP (ratio)</b>	<b>1.9</b>	<b>0.7</b>	<b>2.2</b>	<b>1.8</b>	<b>1.1</b>	<b>1.8</b>
<b>Revenue buoyancy w.r.t State's own taxes (ratio)</b>	<b>0.4</b>	<b>0.9</b>	<b>1.4</b>	<b>1.0</b>	<b>0.9</b>	<b>0.9</b>
<b>GSDP growth (per cent)</b>	<b>4.8</b>	<b>8.9</b>	<b>9.4</b>	<b>15.5</b>	<b>14.9</b>	<b>13.6</b>

Note: Figures in parenthesis represent percentage composition in revenue receipts.

Revenue receipts showed progressive increase from Rs.15,321 crore in 2001-02 to Rs.37,587 crore in 2006-07. On an average 74 per cent of the revenue came from State's own resources. The balance was from transfers from GOI in the form of State's share of Union taxes and grants-in-aid.

Significant increase in revenue receipts by Rs.7,235 crore during 2006-07, the highest during the five year period was mainly due to rise in tax revenue (Rs.4,669 crore), grants from GOI (Rs.1,181 crore) and State's share of union taxes and duties (Rs.1,161 crore).

### **Tax revenue**

Taxes on sales, trade etc., was the major source of State's own tax revenue which contributed 50 per cent followed by state excise (19 per cent), stamps and registration fees (14 per cent) and taxes on vehicles (6 per cent).

The table 7 below shows the trend of major constituents of tax revenue during 2001-07

**Table 7 : Tax revenue**

(Rupees in crore)

<b>Tax revenue</b>	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Taxes on sales, trade, etc.	5,269	5,474	6,649	8,700	9,870	11,762
<i>Rate of growth</i>	-2.2	3.89	21.47	30.85	13.45	19.17
State excise	1,977	2,094	2,334	2,806	3,397	4,495
<i>Rate of growth</i>	29.8	5.92	11.46	20.22	21.06	32.32
Stamps and registration fees	855	1,115	1,356	1,760	2,213	3,206
<i>Rate of growth</i>	34.0	30.41	21.61	29.79	25.74	44.87
Taxes on vehicles	712	676	800	983	1,105	1,374
<i>Rate of growth</i>	41.8	-5.06	18.34	22.88	12.41	24.34



Taxes on sales, trade etc., witnessed steep fall in rate of growth in 2005-06 due to reduction of effective rate of taxation with the introduction of Value Added Tax (VAT) from 01.04.2005. The State received VAT loss compensation of Rs.1,272 crore as non-plan grant for 2005-06 and a part compensation of Rs.392 crore for 2006-07 as non-plan grant from GOI. According to MTFP (2007-11), the improvement in growth rate in 2006-07 was due to general boom in the economy and increase in collection on account of lower base effect. The policy of canalisation of Indian made liquor and tracking of rectified spirit contributed to rise in revenue under State excise. The unexpected growth under housing sector in last few years was the reason for growth of revenue under stamps and registration. Reforms targeted towards improvement of tax base of transport sector and greater compliance by transport utilities with respect to tax dues contributed to higher growth rate of taxes on vehicles.

### **Non-tax revenue**

Non-tax revenue of Rs.4,099 crore in 2006-07 included the debt relief of Rs.358 crore the State got under the scheme of DCRF for the year 2005-06. The share of non-tax revenue in the total revenue receipts declined from 17 per cent in 2004-05 to 11 per cent in 2006-07. The State Government stated in the MTFP that the condition and quality of public services made the task of making any appreciable changes in user charges difficult as a result of which user charges are yet to be rationalised.

The actual state's own revenue receipts vis-à-vis assessment made by TFC and projections in fiscal correction path are given below:

**Table 8**

(Rupees in crore)

	As per		Actual
	TFC assessment	FCP	
Tax revenue	20,348.83	20,865	23,301
Non-tax revenue	2,641.61	4,516	4,099

Actual tax revenue exceeded the TFC assessment as well as the projections in FCP. Non tax revenue realised exceeded the TFC assessment but fell short of FCP projection.

### **Grants-in-aid from GOI**

Grants-in-aid from GOI increased from Rs.1,751 crore in 2001-02 to Rs.4,813 crore in 2006-07 as detailed in the table below:

**Table 9 : Grant-in-aid from GOI**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Non-plan schemes	213	421	530	263	1,736	2,224
State plan schemes	733	570	796	1,089	915	1,284
Central plan schemes	152	45	42	46	37	43
Centrally sponsored plan schemes	653	629	619	749	944	1,262
<b>Total</b>	<b>1,751</b>	<b>1,665</b>	<b>1,987</b>	<b>2,147</b>	<b>3,632</b>	<b>4,813</b>

Increase of non-plan grants by Rs.488 crore over the previous year was due to TFC award for specific purposes viz., roads and bridges (Rs.365 crore), other administrative services (Rs.105 crore). Increase was also under State plan schemes (Rs.369 crore) and Centrally sponsored schemes (Rs.318 crore).

Plan grants of Rs.26.24 crore were released to Karnataka Police Housing Corporation (Rs.16.27 crore), Director of Municipal Administration (Rs.7.08 crore) and National Information Centre (Rs.2.89 crore) without routing through the Consolidated Fund of the State.

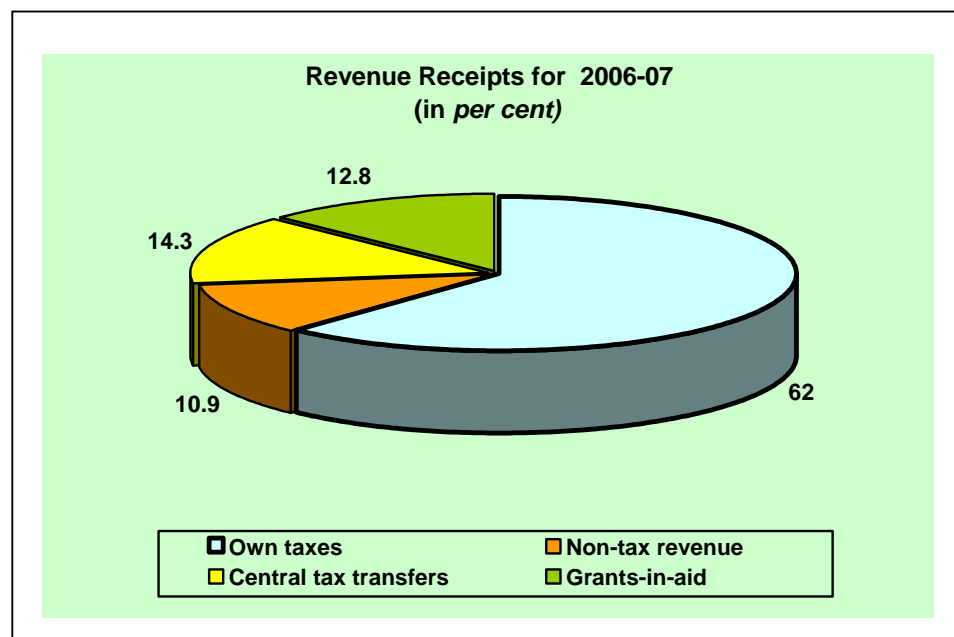
### ***Central tax transfers***

Devolution of taxes from GOI increased on account of improved buoyancy on GOI taxes. Increase of state's share of union taxes from Rs.4,213 crore in 2005-06 to Rs.5,374 crore in 2006-07 was mainly under corporation tax (Rs.514 crore), customs (Rs.227 crore) and service tax (Rs.204 crore)

### ***Arrears of revenue***

Arrears of revenue increased by 91 *per cent* from Rs.2,634 crore in 2001-02 to Rs.5,026 crore to end of 2006-07. Arrears in respect of state excise amounting to Rs.654 crore were outstanding for more than five years.

**Composition of revenue receipts during 2006-07 is indicated graphically below:**



## 1.4 Application of resources

### 1.4.1 Growth of expenditure

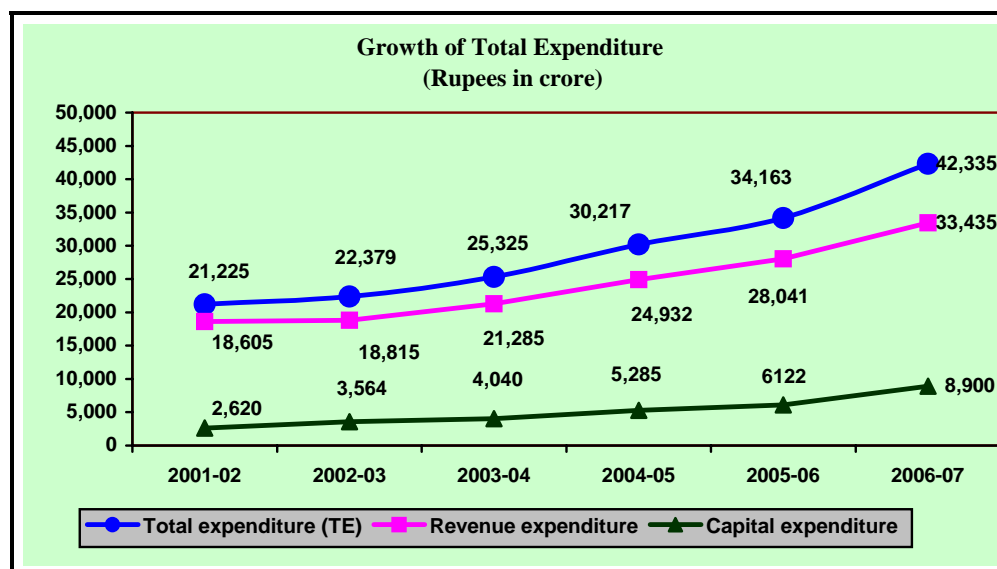
Statement 12 of the Finance Accounts depicts the detailed revenue expenditure by minor heads and capital expenditure by major heads. States raise resources to perform their sovereign functions, maintain their existing nature of delivery of social and economic services, extend the network of these services through capital expenditure and investments and discharge their debt servicing obligations.

Total expenditure, its annual growth rate and ratio of expenditure to GSDP and to revenue receipts and its buoyancy in relation to GSDP and revenue receipts are indicated in table 10 below followed by its graphic representation.

**Table 10 : Total expenditure – Basic parameters**

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Total expenditure (TE)* (Rupees in crore)	21,225	22,379	25,325	30,217	34,163	42,335
Rate of growth (Per cent)	10.9	5.4	13.2	19.3	13.1	23.9
TE/GSDP ratio (Per cent)	19.7	19.0	19.7	20.3	20.0	21.8
Revenue receipts/TE ratio (Per cent)	72.2	72.2	82.0	87.9	88.8	88.8
<b>Buoyancy of total expenditure with</b>						
GSDP(Ratio)	2.3	0.6	1.4	1.2	0.9	1.8
Revenue receipts (ratio)	3.2	1.0	0.5	0.7	0.9	1.0

\* Total expenditure includes revenue expenditure, capital expenditure & loans and advances



Capital expenditure includes disbursement of loans and advances

Total expenditure increased from Rs.21,225 crore in 2001-02 to Rs.42,335 crore in 2006-07 (99 per cent). Revenue expenditure which constituted 88 per cent of total expenditure in 2001-02 decreased to 79 per cent in 2006-07. Ratio of revenue receipts to total expenditure increased from 72 per cent to 89 per cent during the period, indicating that nearly 89 per cent of the State's total expenditure was met from its revenue receipts. Capital expenditure (including loans and advances), increased by 240 per cent from Rs.2,620 crore in 2001-02 to Rs.8,900 crore in 2006-07. It constituted 21 per cent of total expenditure in 2006-07 as against 12 per cent in 2001-02. During 2006-07, plan capital expenditure constituted 98 per cent of total capital expenditure. Of this, 24 per cent (Rs.2,095 crore) was towards repayment of off-budget borrowings.

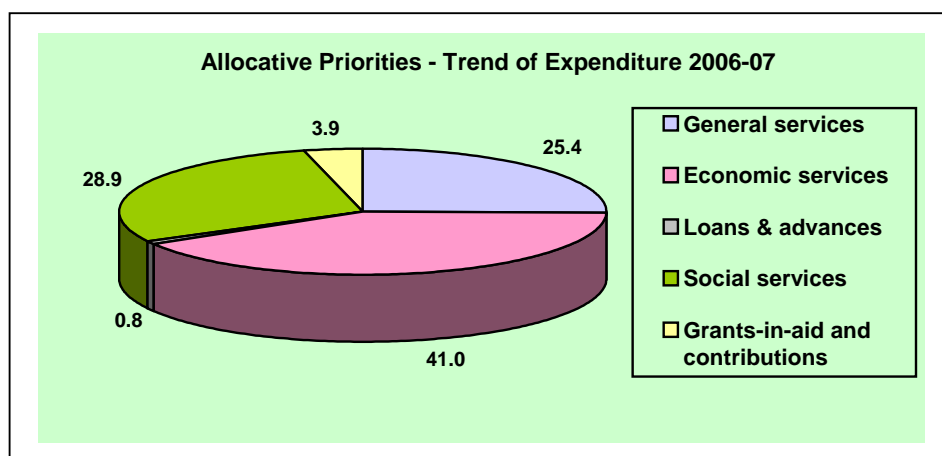
#### 1.4.2 Trends in total expenditure by activities:

In terms of activities, total expenditure could be considered as being composed of expenditure on general services including interest payments, social and economic services, grants-in-aid and loans and advances. Relative share of these components in total expenditure (including disbursements of loans and advances) is indicated in table 11 followed by its graphic representation.

**Table 11 : Components of expenditure – Relative share**

*(in per cent)*

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
General services	29.5	32.1	36.2	33.2	30.0	25.4
<i>Of which interest payments</i>	42.8	45.8	40.5	37.8	36.7	39.4
Social services	31.3	29.6	29.2	27.2	29.3	28.9
Economic services	34.1	32.9	28.1	35.0	36.4	41.0
Grants-in-aid	2.7	2.6	2.5	2.6	3.4	3.9
Loans and advances	2.4	2.8	4.0	2.0	0.9	0.8



The movement of relative share of these components indicates that while the share of social services in total expenditure declined from 31 *per cent* in 2001-02 to 29 *per cent* in 2006-07, the relative share of general services, considered as non-developmental, increased from 30 *per cent* in 2001-02 to 36 *per cent* in 2003-04, thereafter declined to 25 *per cent* in 2006-07. The share of economic services expenditure increased from 34 *per cent* in 2001-02 to 41 *per cent* in 2006-07 with inter-year variations.

### 1.4.3 Incidence of revenue expenditure

Revenue expenditure has the predominant share in the total expenditure. Revenue expenditure is incurred to maintain the current level of services and make payment for the past obligations and as such does not result in any addition to the State's infrastructure and service network. The overall revenue expenditure, its rate of growth, ratio of revenue expenditure to GSDP and to revenue receipts and its buoyancy are indicated in table 12.

**Table 12 : Revenue expenditure – Basic parameters**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Revenue expenditure (RE)	18,605	18,815	21,285	24,932	28,041	33,435
Non-plan revenue expenditure (NPRE)	14,662	15,570	17,732	19,807	22,972	25,583
Plan revenue expenditure (PRE)	3,943	3,245	3,553	5,125	5,069	7,852
<b>Rate of growth (Per cent)</b>						
NPRE	11.0	6.2	13.9	11.7	16.0	11.4
PRE	13.3	-17.7	9.5	44.2	-1.1	54.9
NPRE/ GSDP (Per cent)	13.6	13.3	13.8	13.3	13.5	13.2
NPRE as <i>per cent</i> of TE	69.1	69.6	70.0	65.5	67.2	60.4
NPRE as <i>per cent</i> to revenue receipts	95.7	96.3	85.4	74.5	75.7	68.1
<b>Buoyancy of revenue expenditure with</b>						
GSDP (ratio)	2.4	0.1	1.4	1.1	0.8	1.4
Revenue receipts (ratio)	3.4	0.2	0.5	0.6	0.9	0.8

Revenue expenditure increased from Rs.18,605 crore in 2001-02 to Rs.33,435 crore in 2006-07 (increase 80 *per cent*). While plan revenue expenditure increased from Rs.3,943 crore to Rs.7,852 crore (increase 99 *per cent*) and non-plan revenue expenditure increased from Rs.14,662 crore to Rs.25,583 crore (increase 74 *per cent*).

The non plan revenue expenditure was at 60 *per cent* of total expenditure and 68 *per cent* of revenue receipts during 2006-07. The increase of Rs.2,611 crore in 2006-07 over the previous year was mainly due to increase in subsidy payments (Rs.643 crore), salaries (Rs.613 crore), pension payments (Rs.259 crore) and interest payments (Rs.471 crore). The increase in plan revenue expenditure by Rs.2,783 crore was mainly under education, sports, art and culture (Rs.286 crore), water supply, sanitation, housing and urban development (Rs.309 crore) social welfare (Rs.329 crore), agriculture and allied services (Rs.280 crore), transport (Rs.267 crore) and general economic services (Rs.956 crore).

### 1.4.4 Committed expenditure

#### Expenditure on salaries

Salary expenditure increased from Rs.5,030 crore in 2001-02 to Rs.6,545 crore in 2006-07 as indicated in table below:

**Table 13 : Expenditure on salaries**

(Rupees in crore)

Heads	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07 <sup>■</sup>
Expenditure on salaries <sup>♦</sup>	5,029.74	4,940.70	5,322.76	5,392.15	5,932.49	6,545.37
Non-plan	4,304.51	4,634.00	5,007.07	5,074.62	5,597.59	6,110.82
Plan <sup>∇</sup>	725.23	297.70	315.69	317.53	334.90	434.55
As percentage of GSDP	4.7	4.2	4.1	3.6	3.5	3.4
As percentage of Revenue receipts	32.8	30.6	25.6	20.3	19.5	17.4

Expenditure on salaries declined from five *per cent* of GSDP in 2001-02 to three *per cent* in 2006-07. As a percentage of revenue receipts, it decreased from 33 to 17 due to reform measures undertaken by the State Government, viz., freeze on creation of posts and recruitment except in high priority departments like health, police and education. It was however around 25 *per cent* of revenue expenditure (net of pensions and interest payments), within the limit of 35 *per cent* recommended by TFC.

#### Pension payments

Year-wise break-up of expenditure incurred on pension during the years 2001-2002 to 2006-07 was as under:

**Table 14 – Expenditure on pensions**

(Rupees in crore)

Head	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Expenditure on pension	1,641	1,773	1,901	2,157	2,237	2,496
As <i>per cent</i> of GSDP	1.5	1.5	1.5	1.5	1.3	1.3
As <i>per cent</i> of revenue receipts	10.7	11.0	9.2	8.1	7.4	6.6

Expenditure on pension payments was Rs.2,496 crore which constituted seven *per cent* of the total revenue receipts of the State during 2006-07. The State Government introduced contributory pension scheme to cover employees recruited after 1 April 2006.

Based on trend growth rates, the State Government projected expenditure on pension at Rs.2,661 crore but actual expenditure was Rs.165 crore below the FCP projection.

■ Revised estimates

♦ Includes salary expenditure of panchyat raj institutions. Source : Finance Department

∇ Includes salaries under Centrally Sponsored Schemes

### Interest payments

The details of interest payments of the State Governments for the period 2001-02 to 2006-07 and its percentage with reference to revenue receipts and revenue expenditure are given in table 15.

**Table 15 : Interest payments**

Year	Revenue receipts	Revenue expenditure	Interest payment	Percentage of interest payment with reference to	
	(Rupees in crore)			Revenue receipts	Revenue expenditure
2001-2002	15,321	18,605	2,683	17.5	14.4
2002-2003	16,169	18,815	3,292	20.4	17.5
2003-2004	20,760	21,285	3,710	17.9	17.4
2004-2005	26,570	24,932	3,794	14.3	15.2
2005-2006	30,352	28,041	3,765	12.4	13.4
2006-2007	37,587	33,435	4,236	11.3	12.7

Interest payments increased by Rs,1,553 crore from Rs.2,683 crore in 2001-02 to Rs.4,236 crore in 2006-07. Bulk of the expenditure on interest payments, i.e. 40 per cent amounting to Rs.1,715 crore, was on NSSF loans which carried interest rate of 9.5 per cent.

The ratio of interest payments to revenue receipts determines the sustainability of debt of the State. As per the recommendation of TFC, the level of interest payments relative to revenue receipts should fall to 15 per cent by 2009-10. In 2006-07, interest payments constituted 11 per cent of revenue receipts below the limit of 15 per cent prescribed by TFC. This was partly due to gain of Rs. 276 crore in the nature of reduction of interest payments to be paid during 2006-07 under DCRF envisaged by TFC.

### Subsidies

In any welfare State it is not uncommon to provide subsidies/subventions to disadvantaged sections of the society and making provision for merit goods – education, housing, health, etc. at subsidised prices.

The trends in the subsidies given by the State Government are given in table 16.

**Table 16 : Subsidies**

Year	Amount (Rs. in crore)	Percentage increase (+)/ decrease (-) over previous year	Percentage of subsidy to revenue expenditure
2001-02	2,861	89	15
2002-03	2,230	(-) 22	12
2003-04	2,066	(-) 07	10
2004-05	2,732	32	11
2005-06	3,712	36	13
2006-07	4,355	17	13

Subsidy payments during 2006-07 were mainly in the areas of power (Rs.2,371 crore), co-operation (Rs.821 crore), food (Rs.750 crore) and transport (Rs.273 crore) as discussed below:

### ***Power***

Power sector continued to be highly subsidised with subsidy being extended to electricity supply companies to cover loss due to rural electrification (Rs.2,042 crore), pension payment contribution (Rs.240 crore), irrigation pump set regularisation (Rs.59 crore), power bill arrears of households below poverty line (Rs.25 crore), fixed meter connection (Rs.5 crore). Subsidy dispensation in the power sector was largely affected due to failure to achieve hundred *per cent* metering of IP sets.

The power subsidy of Rs.2,371 crore during the year does not include the tariff subsidy of Rs.130 crore to the electricity supply companies. The amount was ordered (March 2007) by the Government to be classified as 'debt servicing' and met from the supplementary provision of Rs.135 crore for debt servicing of Power Finance Corporation and Rural Electrification Corporation loans taken over by the State Government. The Finance Accounts 2006-07, however, did not reflect this liability as orders of this taking over were not issued. The State Government stated (November 2007) that debt would be included in off-budget side in 2008-09, which was against the State's commitment in MTFP 2007-11 to phase out off-budget borrowings from 2008-09.

### ***Co-operation***

Subsidy of Rs.821 crore in the co-operative sector included Rs.500 crore towards waiver of crop loans and Rs.277 crore towards interest waiver. However, the recovery of short term, medium term and long term loans declined from 81, 61 and 63 *per cent* in 2005-06 to 47, 12 and 22 *per cent* in 2006-07 as reported in Economic Survey of Karnataka, 2006-07. The State Government stated (December, 2007) that subsidy of Rs.500 crore towards loan waiver was released at the fag end of the year and its impact on recovery of loans would be felt only in 2007-08.

### ***Food***

Food subsidy to meet the difference between the cost price of food grains and issue price from the Public Distribution System rose from Rs.730 crore in 2005-06 to Rs.750 crore in 2006-07. In the face of expected decline in poverty level and possible review in issue price, the State Government maintained the food subsidy projections at constant level in MTFP 2004-10.

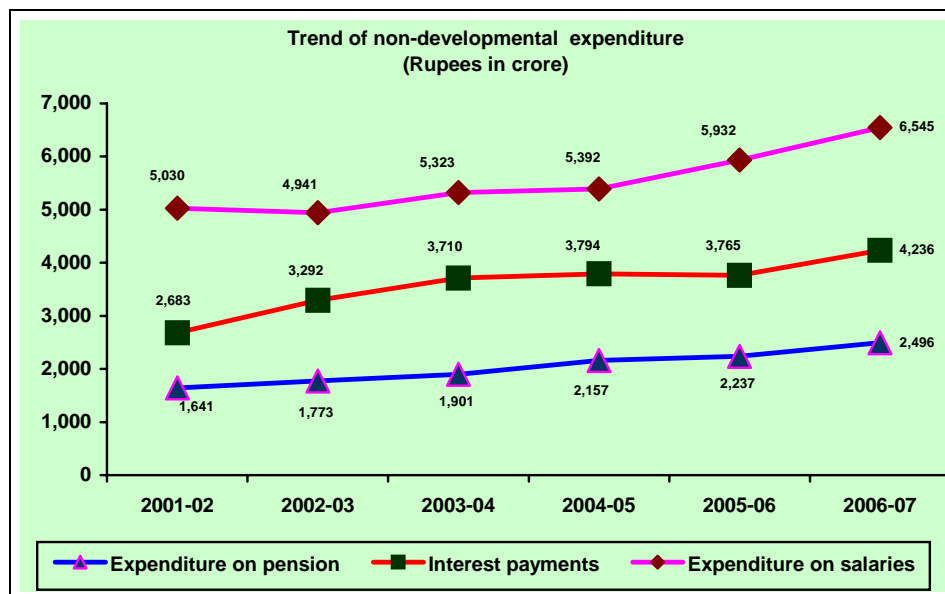
### ***Transport***

Transport subsidy of Rs.273 crore during the year did not include an implicit subsidy of Rs.53 crore released as investment to Bangalore Metropolitan Transport Corporation towards compensation of loss incurred on issue of student concession passes.

Subsidies are dispensed not only explicitly but also implicitly by providing subsidised public service to the people. Budgetary support to financial institutions, inadequate returns on investments and poor recovery of user charges (revenue receipt/revenue expenditure) from the social and economic services provided by the Government fall in the category of implicit subsidies.



Trends in expenditure on pension, interest payments and salaries are graphically depicted below:



## 1.5 Expenditure by allocative priorities

### 1.5.1 Quality of expenditure

The availability of better social and physical infrastructure in the State reflects its quality of expenditure. Therefore ratio of capital expenditure to total expenditure as well as to GSDP and proportion of revenue expenditure being spent on running efficiently and effectively the existing social and economic services would determine the quality of expenditure. Higher the ratio of these components to total expenditure and GSDP better is the quality of expenditure. Table 17 gives these ratios during 2001-07.

**Table 17: Indicators of quality of expenditure**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Capital expenditure</b>	2,106	2,936	3,029	4,674	5,822	8,543
<b>Revenue expenditure, of which</b>	18,605	18,815	21,285	24,932	28,041	33,435
Social & Economic services						
Salary component	3,679.87	3,589.85	3,796.47	3,887.09	4,315.20	4,791.43
Non-salary component	8,146.72	7,538.82	7,820.27	10,346.18	12,530.91	16,585.52
<b>As per cent of total expenditure</b>						
Capital expenditure	10.17	13.50	12.46	15.79	17.19	20.35
Revenue expenditure	89.83	86.50	87.54	84.21	82.81	79.65
<b>As per cent of GSDP</b>						
Capital expenditure	1.95	2.50	2.36	3.15	3.41	4.40
Revenue expenditure	17.24	16.01	16.56	16.78	16.42	17.23

Capital expenditure as a percentage of total expenditure showed an increasing trend from 10 in 2001-02 to 20 in 2006-07. Its ratio with reference to GSDP also increased from two to four *per cent* during the period. Expenditure on non-salary component under revenue expenditure also showed increasing

trend from 2002-03. In 2006-07 the increase was 32 per cent over previous year from Rs.12,531 crore to Rs.16,586 crore. These trends indicate the improvement in the quality of expenditure and the impetus being given for asset formation.

### 1.5.2 Expenditure on social services

Given the fact that human development indicators such as access to basic education, health services and drinking water and sanitation facilities etc., have a strong linkage with eradication of poverty and economic progress, it would be prudent to make an assessment with regard to the expansion and efficient provision of these services in the State. Table 18 summarises the expenditure incurred by the State Government in expanding and strengthening social services in the State during 2001-07.

**Table 18 : Expenditure on social services**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Education, sports, art and culture</b>	<b>3505.88</b>	<b>3570.72</b>	<b>3771.33</b>	<b>4362.83</b>	<b>4890.07</b>	<b>5758.19</b>
<i>Revenue expenditure, of which</i>	<b>3501.41</b>	<b>3564.01</b>	<b>3766.02</b>	<b>4357.91</b>	<b>4837.40</b>	<b>5703.21</b>
<i>Salary component</i>	2104.99	2017.82	2142.56	2292.74	2606.79	3019.53
<i>Non-salary component</i>	1396.42	1546.19	1623.46	2065.17	2230.61	2683.68
<b>Capital expenditure</b>	<b>4.47</b>	<b>6.71</b>	<b>5.31</b>	<b>4.92</b>	<b>52.67</b>	<b>54.98</b>
<b>Health and family welfare</b>	<b>1085.84</b>	<b>1004.12</b>	<b>995.70</b>	<b>1043.91</b>	<b>1146.19</b>	<b>1349.61</b>
<i>Revenue expenditure, of which</i>	<b>986.32</b>	<b>953.65</b>	<b>958.93</b>	<b>1035.61</b>	<b>1138.50</b>	<b>1206.66</b>
<i>Salary component</i>	559.71	570.10	581.78	573.95	616.03	651.87
<i>Non-salary component</i>	426.61	383.55	377.15	461.66	522.47	554.79
<b>Capital expenditure</b>	<b>99.52</b>	<b>50.47</b>	<b>36.77</b>	<b>8.30</b>	<b>7.69</b>	<b>142.95</b>
<b>Water supply, sanitation, housing and urban Development</b>	<b>769.34</b>	<b>743.36</b>	<b>1083.03</b>	<b>1269.27</b>	<b>1881.55</b>	<b>2130.92</b>
<i>Revenue expenditure, of which</i>	<b>713.41</b>	<b>576.04</b>	<b>794.22</b>	<b>857.89</b>	<b>911.77</b>	<b>1205.44</b>
<i>Salary component</i>	12.47	12.02	13.34	12.86	14.69	14.54
<i>Non-salary component</i>	700.94	564.02	780.88	845.03	897.08	1190.90
<b>Capital expenditure</b>	<b>55.93</b>	<b>167.32</b>	<b>288.81</b>	<b>411.38</b>	<b>969.78</b>	<b>925.48</b>
<b>other social services</b>	<b>1280.05</b>	<b>1303.35</b>	<b>1542.19</b>	<b>1532.78</b>	<b>2086.28</b>	<b>2990.61</b>
<i>Revenue expenditure, of which</i>	<b>1227.67</b>	<b>1232.55</b>	<b>1445.87</b>	<b>1471.34</b>	<b>2011.12</b>	<b>2821.40</b>
<i>Salary component</i>	187.59	189.40	207.16	216.59	214.12	249.89
<i>Non-salary component</i>	1040.08	1043.15	1238.71	1254.75	1797.00	2571.51
<b>Capital expenditure</b>	<b>52.38</b>	<b>70.80</b>	<b>96.32</b>	<b>61.44</b>	<b>75.16</b>	<b>169.21</b>
<b>Total (social services)</b>	<b>6641.11</b>	<b>6621.55</b>	<b>7392.25</b>	<b>8208.79</b>	<b>10004.09</b>	<b>12229.33</b>
<i>Revenue expenditure, of which</i>	<b>6428.81</b>	<b>6326.25</b>	<b>6965.04</b>	<b>7722.75</b>	<b>8898.79</b>	<b>10936.71</b>
<i>Salary component</i>	2864.76	2789.34	2944.84	3096.14	3451.63	3935.83
<i>Non-salary component</i>	3564.05	3536.91	4020.20	4626.61	5447.16	7000.88
<b>Capital expenditure</b>	<b>212.30</b>	<b>295.30</b>	<b>427.21</b>	<b>486.04</b>	<b>1105.30</b>	<b>1292.62</b>

Expenditure on social services increased from Rs.6,641 crore in 2001-02 to Rs.12,229 crore in 2006-07. Out of total developmental expenditure of Rs.29,599 crore, expenditure on social services accounted for 41 per cent during the year.

Education, health and family welfare and water supply and sanitation were the identified priority sectors under social services and 76 per cent of the total expenditure on social services was on these priority sectors.

Capital expenditure of Rs.1,293 crore in 2006-07 under Social Services included Rs.236 crore (18 per cent) on debt servicing and the remaining 82 per cent of the capital expenditure was available for development.

The optimum level of social expenditure depends on the size of the population, level of human development and stage in the development of infrastructure. According to Human Development Report of UNDP, in order to benefit human development, the ratio of social expenditure to total expenditure should be at least 0.4. The ratio of social services sector expenditure to total expenditure, however, fell from 0.32 in 2001-02 to 0.29 in 2006-07.

### 1.5.3 Expenditure on economic services

The expenditure on economic services includes all such expenditures as to promote directly or indirectly, productive capacity within the State's economy. The expenditure on economic services (Rs.17,369 crore) accounted for 59 per cent of total developmental expenditure of Rs.29,599 crore. In the economic services sector, expenditure on priority sectors like agriculture and allied activities (Rs.3,174 crore), irrigation and flood control,(Rs.4,410 crore) and energy (Rs.2,832 crore) consumed 60 per cent of the total expenditure on economic services. Major trends were as follows:

**Table 19: Economic services sector expenditure**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Agriculture and allied activities</b>	<b>1115.75</b>	<b>1100.05</b>	<b>1356.37</b>	<b>2083.71</b>	<b>2883.82</b>	<b>3173.99</b>
<i>Revenue expenditure, of which</i>	<b>1088.11</b>	<b>1077.10</b>	<b>1348.92</b>	<b>2064.90</b>	<b>2866.65</b>	<b>3140.84</b>
<i>Salary component</i>	422.89	413.68	430.70	420.01	459.07	467.08
<i>Non-salary component</i>	665.22	663.42	918.22	1644.89	2407.58	2673.76
<b>Capital expenditure</b>	<b>27.64</b>	<b>22.95</b>	<b>7.45</b>	<b>18.80</b>	<b>17.17</b>	<b>33.15</b>
<b>Irrigation and flood control</b>	<b>1715.62</b>	<b>2235.19</b>	<b>2060.52</b>	<b>3223.64</b>	<b>3545.50</b>	<b>4410.16</b>
<i>Revenue expenditure, of which</i>	<b>190.76</b>	<b>206.73</b>	<b>179.06</b>	<b>213.91</b>	<b>215.81</b>	<b>294.42</b>
<i>Salary component</i>	133.33	128.48	140.36	92.42	89.40	76.66
<i>Non-salary component</i>	57.43	78.25	38.70	121.49	126.41	217.76
<b>Capital expenditure</b>	<b>1524.86</b>	<b>2028.46</b>	<b>1881.46</b>	<b>3009.73</b>	<b>3329.69</b>	<b>4115.74</b>
<b>Power &amp; energy</b>	<b>2336.69</b>	<b>1906.92</b>	<b>1733.05</b>	<b>1896.71</b>	<b>1886.93</b>	<b>2832.48</b>
<i>Revenue expenditure, of which</i>	<b>2336.69</b>	<b>1906.92</b>	<b>1733.05</b>	<b>1896.71</b>	<b>1836.93</b>	<b>2402.01</b>
<i>Salary component</i>	0.08	0.09	0.09	0.13	0.25	0.13
<i>Non-salary component</i>	2336.61	1906.83	1732.96	1896.58	1836.68	2401.88
<b>Capital expenditure</b>	---	---	---	---	<b>50.00</b>	<b>430.47</b>
<b>Transport</b>	<b>778.28</b>	<b>818.87</b>	<b>821.64</b>	<b>1513.42</b>	<b>1786.55</b>	<b>3387.48</b>
<i>Revenue expenditure, of which</i>	<b>513.62</b>	<b>395.79</b>	<b>311.43</b>	<b>617.60</b>	<b>756.10</b>	<b>1563.98</b>
<i>Salary component</i>	15.44	16.21	17.80	15.01	18.27	19.21
<i>Non-salary component</i>	498.18	379.58	293.63	602.59	737.83	1544.77
<b>Capital expenditure</b>	<b>264.66</b>	<b>423.08</b>	<b>510.21</b>	<b>895.82</b>	<b>1030.45</b>	<b>1823.50</b>
<b>Other economic services</b>	<b>1293.27</b>	<b>1306.24</b>	<b>1153.87</b>	<b>1844.47</b>	<b>2343.23</b>	<b>3565.14</b>
<i>Revenue expenditure, of which</i>	<b>1268.60</b>	<b>1215.88</b>	<b>1079.24</b>	<b>1717.39</b>	<b>2271.83</b>	<b>3038.99</b>

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Salary component	243.37	242.04	262.68	263.37	296.58	292.52
Non-salary component	1025.23	973.84	816.56	1454.02	1975.25	2746.47
<b>Capital expenditure</b>	<b>24.67</b>	<b>90.36</b>	<b>74.63</b>	<b>127.08</b>	<b>71.40</b>	<b>526.15</b>
<b>Total (economic services)</b>	<b>7239.61</b>	<b>7367.27</b>	<b>7125.45</b>	<b>10561.95</b>	<b>12446.03</b>	<b>17369.25</b>
<b>Revenue expenditure, of which</b>	<b>5397.78</b>	<b>4802.42</b>	<b>4651.70</b>	<b>6510.52</b>	<b>7947.32</b>	<b>10440.24</b>
Salary component	815.11	800.51	851.63	790.95	863.57	855.60
Non-salary component	4582.67	4001.91	3800.07	5719.57	7083.75	9584.64
<b>Capital expenditure</b>	<b>1841.83</b>	<b>2564.85</b>	<b>2473.75</b>	<b>4051.43</b>	<b>4498.71</b>	<b>6929.01</b>

Expenditure on economic services increased from Rs.7,240 crore in 2001-02 to Rs.17,369 crore in 2006-07. Out of total developmental expenditure of Rs.29,599 crore, expenditure on economic services accounted for 59 per cent during the year.

Out of total expenditure on economic services during 2006-07, 25 per cent was under irrigation and flood control, 19 per cent on transport, 18 per cent on agriculture and allied activities and 16 per cent was under power. As compared to 2001-02 significant increases in 2006-07 was observed in irrigation and flood control -157 per cent, agriculture and allied activities -184 per cent and transport - 335 per cent. The salary component in expenditure on economic services ranged between 12 and 5 per cent. The non salary component increased from Rs.3,800 crore in 2003-04 to Rs.9,585 crore in 2006-07. Capital expenditure included an expenditure of Rs.1,859 crore (27 per cent) on repayment of off-budget borrowings.

#### 1.5.4 Financial assistance to local bodies and other institutions

The quantum of assistance provided by way of grants and loans to local bodies and others during the six year period 2001-07 is presented in table 20.

**Table 20: Financial assistance to local bodies and other institutions**

(Rupees in crore)						
Description	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Panchayat raj institutions	3,829.68	4,515.66	4,524.31	4,956.93	6,088.61	7,767.93
Urban local bodies	631.95	644.42	892.48	1,169.85	1,605.85	2,113.48
Educational institutions (including universities)	499.85	646.99	603.16	688.93	695.62	750.27
Co-operative societies and co-operative institutions	3.34	5.00	57.62	167.65	955.45	882.98
Other institutions and bodies (including statutory bodies)	2,464.01	1,863.28	1,702.81	1,745.28	1,837.43	2,400.54
<b>Total</b>	<b>7,428.83</b>	<b>7,675.35</b>	<b>7,780.38</b>	<b>8,728.64</b>	<b>11,182.96</b>	<b>13,915.20</b>
Percentage growth over previous year	15	3	1	11	22	20
Revenue receipts	15,321.25	16,168.76	20,759.88	26,569.66	30,352.05	37,586.94
Assistance as a percentage of revenue receipts	48	47	37	33	37	37
Revenue expenditure	18,605.00	18,814.50	21,284.71	24,931.85	28,040.89	33,435.43
Percentage of assistance to revenue expenditure	40	41	37	35	40	42
Percentage of assistance to panchayat raj institutions to total assistance	52	59	58	57	54	56

The assistance to Panchayat Raj Institutions (PRI) increased from Rs.3,830 crore in 2001-02 to Rs.7,768 crore in 2006-07. The assistance to Urban Local Bodies (ULB) increased from Rs.632 crore in 2001-02 to Rs.2113 crore in 2006-07. Out of the total devolution of Rs.9,881 crore to PRIs & ULBs, Rs.3,774 crore (38 per cent) were towards salaries during 2006-07 as the State Government's functions viz., education, water supply and sanitation, housing, health and family welfare etc., remained transferred to PRIs and ULBs. Assistance (Rs.2,401 crore) to other institutions and bodies included expenditure of Rs.2,371 crore on subsidy paid to electric supply companies.

#### ***1.5.5 Delay in furnishing utilisation certificates***

Of the 1281 utilisation certificates (UC) due in respect of grants and loans aggregating Rs.912.74 crore paid upto 2006-07, 1211 UCs for an aggregate amount of Rs.804.78 crore were in arrears. Department-wise break-up of outstanding UCs is given in **Appendix 1.7**.

#### ***1.5.6 Non-submission of accounts***

In order to identify the institutions which attract audit under sections 14 and 15 of the Comptroller and Auditor General's (Duties, Powers and Conditions of service) Act, 1971, the Government/Heads of the Department are required to furnish to audit every year detailed information about the financial assistance given to various institutions, the purpose of assistance granted and the total expenditure of the institutions. As of March 2007, 16 departments of the Government have not furnished details for the year 2006-07 as shown in **Appendix 1.8**.

#### ***1.5.7 Audit of performance of the autonomous bodies***

The audit of accounts of eight bodies in the State has been entrusted to the Comptroller and Auditor General of India. The status of entrustment to audit, rendering of accounts to audit, issuance of separate audit report and its placement in the Legislature is indicated in **Appendix 1.9**.

#### ***1.5.8 Misappropriations, losses, defalcations, etc.***

The State Government reported 220 cases of misappropriation, defalcation, etc., involving Government money amounting to Rs.10.04 crore upto the period 31 March 2007 on which final action was pending. The department wise breakup of pending cases is given in **Appendix 1.10**.

#### ***1.5.9 Write-off of losses, etc.***

A sum of Rs.0.57 lakh being the cost of food grains lost in transit was written-off during 2006-07 by the Government in Food and Civil Supplies department.

### **1.6 Assets & Liabilities**

In Government accounting system, comprehensive accounting of fixed assets like land 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 1.2** gives an

abstract of such liabilities and assets as on 31 March 2007, compared with the corresponding position on 31 March 2006. While liabilities shown in this statement consist mainly of internal borrowings, loans and advances from GOI, receipts from the public account and reserve funds; assets comprise mainly of capital outlay and loans and advances given by the State Government and the cash balances. The liabilities of the State depicted in the Finance Accounts, however, do not include pension, other retirement benefits payable to retired/retiring State employees, guarantees / letters of comfort issued by State Government and borrowings through special purpose vehicles termed off-budget borrowings. Appendix 1.2 shows that while the growth rate of assets remained stagnant at 22 *per cent*, growth rate of liabilities fell to 11 *per cent* in 2006-07 as against 12 *per cent* in the previous year.

### 1.6.1 Incomplete projects

Incomplete projects/works reflect failure on part of the State to prioritise expenditure and to spread its resources adequately over these projects. Additional statement of Finance Accounts gives the details of these works. As reported by the departments of the State Government, there were 261 incomplete projects/works. Expenditure incurred upto end of 2006-07 was Rs.1,174 crore (17 *per cent*) as against the original cost of Rs.6,869 crore.

### 1.6.2 Investments and returns

As on 31 March 2007, Government had invested Rs.18,698.57 crore in statutory corporations, rural banks, Government companies, joint stock companies and co-operatives (table 21).

**Table 21 : Return on investment**

(Rupees in crore)

Year	Investment at the end of the year	Amount of return	Percentage of return	Average interest rate on Government borrowing – market loans ( <i>per cent</i> )	Difference between interest rate and return
2001-2002	4,840.34	10.6	0.2	9.1	8.9
2002-2003	6,150.37	21.3	0.4	9.4	9.0
2003-2004	7,984.19	18.0	0.2	9.4	9.2
2004-2005	10,741.40	16.7	0.2	8.5	8.3
2005-2006	14,052.53	16.9	0.1	7.6	7.5
2006-2007	18,698.37	19.5	0.1	7.7	7.6

The return on this investment was 0.1 to 0.4 *per cent* in the last six years, while the Government paid interest on its borrowing at the average rate of eight to nine *per cent*.

The aggregate cumulative loss was Rs.2,658.81 crore against the investment of Rs.2,020.61 crore made by the Government in 20 companies which included the following three major companies falling under economic services sector.

**Table : 22**

(Rupees in crore)

Sl. No.	Company	Investment	Cumulative loss	
			Amount	to end of
1.	Karnataka State Road Development Corporation	812.52	59.26	2005-06
2.	Karnataka State Industrial Investment and Development Corporation, Bangalore	625.10	574.64	2004-05
3.	Karnataka State Road Transport Corporation	433.67	200.00	2005-06
<b>Total</b>		<b>1,871.29</b>	<b>833.90</b>	

**1.6.3 Loans and advances by State Government**

In addition to investment in corporations, companies and cooperative societies, Government has also been providing loans and advances to many of these institutions/organisations. Total outstanding loans and advances as on 31 March 2007 was Rs.6,240.83 crore (table 23).

**Table 23 : Average interest received on loans advanced by the State Government**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Opening balance	4,076.69	4,556.46	4,256.04	5,202.95	5,767.53	5,943.58*
Amount advanced during the year	514.47	627.58	1,011.20	611.43	299.60	357.23
Amount repaid during the year	34.70	928.00	64.29	46.85	123.55	59.97
<b>Closing balance</b>	<b>4,556.46</b>	<b>4,256.04</b>	<b>5,202.95</b>	<b>5,767.53</b>	<b>5,943.58</b>	<b>6,240.83</b>
Net addition (+) / reduction (-)	479.77	-300.42	946.91	564.58	176.05	297.26
Interest received (Rupees in crore)	112.11	19.98	96.27	88.18	94.95	38.49
Interest received as <i>per cent</i> to outstanding loans and advances	2.6	0.4	2.0	1.6	1.6	0.6
Average interest	9.1	9.4	9.4	8.5	7.6	7.7
Difference between average interest and interest received ( <i>per cent</i> )	6.5	9.0	7.4	6.9	6.0	7.1

♦ Differs in closing balance by Rs.0.01 crore due to rounding as shown in Appendix 1.2.

Outstanding loans as on March 2007 included Rs.377 crore given to 19 companies for implementation of voluntary retirement scheme, and Rs.286 crore given to five institutions for loan repayment. The interest earned during 2006-07 was about 0.6 *per cent* of the outstanding loans.

Terms and conditions of repayment were not specified in respect of loans amounting to Rs.347.12 crore (19 cases) advanced by the State Government during the year.

As of March 2007, recovery of Rs.2,256.65 crore (principal: Rs.822.32 crore and interest: Rs.1,434.33. crore) was over-due. Loans aggregating Rs.201 crore pertain to 11 companies which were either liquidated or under liquidation. A few illustrative cases are given in the table below:

**Table: 24**

(Rupees in crore)

Sl. No.	Government companies under liquidation / liquidated	loan outstanding for recovery
1.	New Government Electric Factory, Bangalore	122.59
2.	Mysore Acetate and Chemicals Ltd, Bangalore	15.52
3.	Karnataka Film Industries Development Corporation	0.75
4.	Mysore Lamp works Ltd	46.26
5.	Karnataka Telecom Ltd	4.21
6.	Karnataka Agro Proteins Ltd	0.70

**1.6.4 Management of Cash balances**

It is generally desirable that State's flow of resources should match its expenditure obligations. However, to take care of any temporary mismatches in the flow of resources and the expenditure obligations, a mechanism of Ways and Means Advances (WMA) - ordinary and special - from Reserve Bank of India (RBI) has been put in place. The operative limit for normal WMA is reckoned on the three-year average of revenue receipts and the operative limit for special WMA are fixed by the RBI from time to time depending on the holdings of Government Securities. During the year, the limit of normal WMA was fixed at Rs.625 crore. The operative limit of special WMA varied between Rs.2.18 crore and Rs.5,607.47 crore during the year depending on the securities held by the State. WMA and overdraft availed and interest paid by the State is detailed in table 25 below.

**Table 25 : Ways and means advances and overdrafts of the State and interest paid thereon**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Ways &amp; Means advances</b>						
Availed in the year	735.88	4,045.45	4,623.92	1,462.79	--	---
Interest paid	0.91	5.22	7.94	1.2	--	---
No. of days availed	40	170	163	61	--	---
<b>Overdraft</b>						
Availed in the year	--	47.84	757.72	--	--	---
Interest paid	--	0.01	0.9	--	--	---
Number of days	--	1	33	--	--	---

In 2006-07, the liquidity position of the State Government continued to be stable and the State Government did not avail WMA / over-draft. The cash balance of the State in 2006-07 increased by Rs. 1,498 crore over the previous year and included sinking fund balance of Rs.340 crore. Cash-balance investments in GOI treasury bills, securities, etc in 2006-07 increased by Rs.1,319 crore over the previous year.

**1.7 Un-discharged liabilities**

Total liabilities, as defined in the Karnataka Fiscal Responsibility Act, are the liabilities under the consolidated fund and the public account of the State.



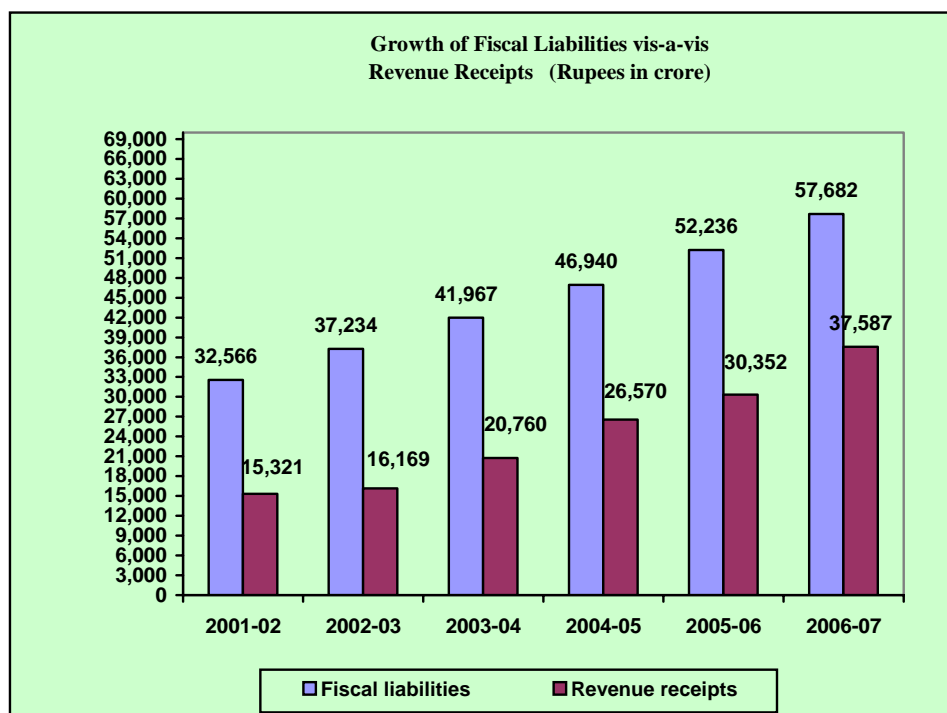
### 1.7.1 Fiscal liabilities-Public debt and Guarantees

There are two sets of liabilities namely, public debt and other liabilities. Public debt consists of internal debt of the State and is reported in the annual financial Statements under the consolidated fund – capital account. It includes market loans, special securities issued to RBI and loans and advances from Central Government. The Constitution of India provides that State may borrow within the territory of India upon the security of its consolidated fund, within such limits, as may from time to time, be fixed by an Act of the Legislature and give guarantees within such limits as may be fixed. Other liabilities which are a part of public account include deposits under small savings scheme, provident funds, and other deposits.

Table 26 and the graph below show the fiscal liabilities of the State, their rate of growth, ratio of these liabilities to GSDP, to revenue receipts and to own resources as also the buoyancy of fiscal liabilities with respect to these parameters.

**Table 26 : Fiscal liabilities –Basic parameters**

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Fiscal liabilities	32,566	37,234	41,967	46,940	52,236	57,682
Rate of growth ( <i>per cent</i> )	22.6	14.3	12.7	11.8	11.3	10.4
<b>Ratio of fiscal liabilities to</b>						
GSDP ( <i>Per cent</i> )	30.2	31.7	32.6	31.6	30.6	29.7
Revenue receipts ( <i>Per cent</i> )	212.6	230.3	202.1	176.7	172.1	153.5
Own resources ( <i>Per cent</i> )	297.5	317.8	270.3	228.5	232.1	210.5
<b>Buoyancy of fiscal liabilities to</b>						
GSDP(ratio)	4.7	1.6	1.3	0.8	0.8	0.8
Revenue receipts (ratio)	6.6	2.6	0.4	0.4	0.8	0.4
Own resources(ratio)	9.9	2.0	0.4	0.4	1.2	0.5



Fiscal liabilities of the State increased from Rs.32,566 crore in 2001-02 to Rs.57,682 crore in 2006-07 comprising consolidated fund liabilities (Rs.41,846 crore) and public account liabilities (Rs.15,836 crore).

The rate of growth of fiscal liabilities of the State has been following a downward path and fell to 10.4 *per cent* in 2006-07 from 22.6 *per cent* in 2001-02.

In 2006-07, the growth rate of fiscal liabilities was lower than the growth of GSDP and the buoyancy of fiscal liabilities to GSDP which was as high as 4.7 in 2001-02 came down to 1.6 in 2003-04 and remained constant at 0.8 during the last three years.

As per the recommendation of the TFC, all states were required to set-up a Sinking Fund for amortisation of all loans including liabilities on account of National Small Savings Fund (NSSF), etc., The State Government had already constituted a sinking fund for amortisation of open market loans. However, there were no contributions to the sinking fund since 1999-2000. The sinking fund was yet to be revived.

### 1.7.2 Status of Guarantees – contingent liabilities

Guarantees are liabilities contingent on the consolidated fund of the State in case of default by the borrower for whom the guarantee has been extended. The maximum amount for which guarantees were given by the State and outstanding guarantees at the end of year since 2001-02 as per Statement 6 of Finance Accounts is given in table 27.

**Table 27 : Guarantees given by the Government of Karnataka**

(Rupees in crore)

Year	Max amount guaranteed	Outstanding amount of guarantees	Percentage of outstanding amount guaranteed to total revenue receipts of the second preceding year
2001-02	20,823	12,279	95
2002-03	20,973	13,314	90
2003-04	21,225	14,179	93
2004-05	19,910	11,574	72
2005-06	20,107	8,984	43
2006-07	19,793	9,879	37

The Karnataka Ceiling on Government Guarantees Act, 1999, provides for a cap on outstanding guarantees at the end of any year at 80 *per cent* of the State's revenue receipts of the second preceding year. The outstanding guarantees to the end of 2006-07 constituted 37 *per cent* of the revenue receipts of the year 2004-05 but as stated in the MTFP 2007-11, there existed no risk-based assessment of outstanding guarantees to enable corrective action. TFC recommended setting up of Guarantee Redemption Fund through earmarked guarantee fees based on risk weighing of guarantees. The State Government had already set up a Guarantee Reserve Fund in 1999-2000 with a corpus of Rs. one crore but there had been no transactions under this fund.

The departments of the Government are expected to levy guarantee fee at the rate of one *per cent* on the amount of outstanding guarantee. Guarantee fees

of Rs.10 crore remitted to Government account under the head 'miscellaneous general services' in 2006-07 was not transferred to the Guarantee reserve fund.

### 1.7.3 Off-budget borrowings

The borrowings of a State are governed under Article 293 of the Constitution of India. In addition to the liabilities shown in table 26, the State guaranteed loans taken by Government companies/corporations. These companies/corporations borrowed funds from the market/financial institutions for implementation of various State plan programmes projected outside the State budget. Although the estimates of the plan programmes of the State Government projected that funds for these programmes would be met out of resources of the companies/corporations outside the State budget, in reality the borrowings of many of these concerns were ultimately the committed liabilities of the State Government termed 'off-budget borrowings'. Though off-budget borrowings are not permissible under Article 293 (3), the State resorted to off-budget borrowings as evident by the data furnished by the Finance Department. Table 28 captures the trends in the off-budget borrowings of the State during 2001-07 while table 29 gives the entity-wise position of borrowings.

**Table 28 : Trend in off-budget borrowings**

(Rupees in crore)

Year	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07 (RE)
Amount as per MTFP <sup>^</sup>	1,533	1,388	1,129	838	1,078	845

<sup>^</sup> figures are yet to be reconciled with those of the financial institutions.

**Table 29 : Entity-wise position of off-budget borrowings**

(Rupees in crore)

Company/Corporation/Board	Off-budget borrowings			Repayment to end of 2006-07	
	upto 2005-06	During 2006-07	Total	Principal	Interest
Krishna Bhagya Jala Nigam	2,433.17	50.00	2,483.17	947.48	411.84
Karnataka Neeravari Nigam Limited	1,915.05	0.00	1,915.05	1,055.95	730.47
Karnataka Road Development Corporation	590.29	0.00	590.29	56.60	48.17
Rajiv Gandhi Rural Housing Corporation	826.62	0.00	826.62	69.59	54.76
KEONICS	60.00	54.00	114.00	67.71	43.06
Karnataka Police Housing Corporation	372.87	23.00	395.87	30.29	25.38
Karnataka Land Army Corporation	160.00	0.00	160.00	46.46	79.05
Karnataka Renewable Energy Development Limited	8.06	0.00	8.06	1.98	2.27
Cauvery Neeravari Nigam	674.55	115.00	789.55	0.00	36.44
Karnataka Residential Education Institution Society	7.63	0.00	7.63	28.91	26.11
Karnataka Small Industrial Investment Development Corporation	240.59	74.80	315.39	60.90	27.38
<b>Total</b>	<b>7,288.83</b>	<b>316.80</b>	<b>7,605.63</b>	<b>2,365.87</b>	<b>1,484.93</b>

Information as furnished by the Companies/Corporations.

Taking into account the off-budget borrowings of the State, the total liabilities at the end of March 2007 work out to Rs.62, 922 crore as against Rs.57,682 crore reflected in table 26. In view of this the ratio of fiscal liabilities to

GSDP would increase to 32 *per cent* at the end of the year. The Government's commitment according to MTFP 2007-11 is to phase out off-budget borrowings from 2008-09 by bringing them on budget.

#### 1.7.4 Debt sustainability

Liabilities are considered sustainable if the government is able to service the stock of liabilities over the foreseeable future and the debt-GSDP ratio does not grow to unmanageable proportions. A government which does not generate enough current revenues for debt service will default on its obligations or borrow more to service its past debts and cover its current receipt-expenditure imbalance. Solvency of the state and sustainability are inter-related and unsustainable liabilities will threaten the solvency of the state. Debt sustainability of the State has been examined in terms of debt/GSDP ratio or Domar's Gap, net availability of borrowed funds and adequacy of incremental revenue receipts to meet the incremental interest burden and primary expenditure.

#### 1.7.5 Debt stability

An important condition for debt sustainability is stabilisation in terms of debt/GSDP ratio. According to Domar's debt stability equation, 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. When the quantum spread and primary deficit is negative, debt-GSDP ratio will be high indicating unsustainable levels of public debt and when the quantum spread and primary deficit are positive, debt-GSDP ratio will be low indicating sustainable levels of public debt.

**Table 30: Debt sustainability – interest rate and GSDP growth**

	(In <i>per cent</i> )					
	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Average interest rate	9.1	9.4	9.4	8.5	7.6	7.7
GSDP growth	4.8	8.9	9.4	15.5	14.9	13.6
Interest spread	-4.3	-0.5	0	7.0	7.3	5.9
Quantum spread (Rs. in crore)	-1400.34	-186.17	0	3,285.80	3,813.23	3,403.24
Primary deficit (-) / primary surplus (+) (Rs. in crore)	-3,186.00	-1,990.00	-791.00	194	78	-452.00

For the period 2001-03, quantum spread together with primary deficit was negative resulting in increase in debt / GSDP ratio from 30 to 32 *per cent*. In 2004-05 and 2005-06, quantum spread together with primary deficit / surplus turned out to be positive resulting in decrease of debt / GSDP ratio to 31 *per cent* in 2006-07. These trends along with declining fiscal deficit/GSDP ratio indicated that capacity of the Government to sustain the debt has improved over the years.

#### 1.7.6 Sufficiency of incremental non-debt receipts

Another indicator of debt sustainability is the adequacy of incremental non-debt receipts of the State to meet the incremental interest burden and incremental primary expenditure. The table below gives the position of sufficiency of incremental non-debt receipts.

**Table 31**

(Rupees in crore)

Period	Incremental				Resource gap
	Non-debt receipts	Primary expenditure	Interest payments	Total expenditure	
1	2	3	4	5=(3+4)	6=(2-5)
2001-02	432	1,625	295	1,920	-1,488
2002-03	1,741	-399	609	210	1,531
2003-04	3,727	2,052	418	2,470	1,257
2004-05	5,793	3,563	84	3,647	2,146
2005-06	3,859	3,138	-29	3,109	750
2006-07	7,171	4,923	471	5,394	1,777

The negative resources gap in 2001-02 indicated the inadequacy of incremental revenue receipts to meet the incremental expenditure. The shift towards sustainable debt level began in 2002-03. Positive resource gap indicated the adequacy of revenue receipts to meet revenue expenditure. In 2005-06, interest expenditure declined over the previous year and incremental interest expenditure turned negative. In 2006-07, the shift towards the path of sustainability continued as the incremental revenue receipts were more than incremental revenue expenditure.

#### 1.7.7 Net availability of borrowed funds

Another important indicator of debt sustainability is the net availability of funds after payment of the principal on account of earlier contracted liabilities and interest. Table 32 below gives the position of the receipt and repayment of internal debt and other fiscal liabilities of the State over the last five years.

**Table 32: Net availability of borrowed funds**

(Rupees in crore)

	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Internal debt</b>						
Receipts	2,969.48	3,888.52	6,531.33	6,953.68	4,994.89	2,891.48
Repayment (principal + interest)	1,193.45	1,618.53	2,523.27	2,666.13	2,910.82	3,925.98
Net fund available	1,776.03	2,269.99	4,008.06	4,287.55	2,084.07	-1,034.50
Net fund available ( <i>Per cent</i> )	60	58	61	62	42	---
<b>Loans and advances from GOI</b>						
Receipts	2,176.88	1,544.22	1,457.00	1,555.75	668.66	654.46
Repayment (principal + interest)	1,799.41	2,932.84	4,196.92	4,703.74	1,132.66	1,491.41
Net fund available	377.47	-1,388.62	-2,739.92	-3,147.99	-464.00	-836.95
Net fund available ( <i>Per cent</i> )	17	-	-	-	-	---
<b>Other obligations</b>						
Receipts	15,531.58	15,077.11	16,426.71	19,227.98	18,806.35	22,435.86
Repayment (principal + interest)	14,373.54	14,582.31	16,671.81	19,188.30	18,895.15	19,354.70
Net fund available	1,158.04	494.80	-245.10	39.68	-88.80	3,081.16
Net fund available ( <i>Per cent</i> )	7	3	-	0.2	-	14
<b>Total liabilities</b>						
Receipts	20,677.94	20,509.85	24,415.04	27,737.41	24,469.90	25,981.80
Repayment (principal + interest)	17,366.40	19,133.68	23,392.06	26,558.17	22,938.63	24,772.09
Net fund available	3,311.54	1,376.17	1,023.04	1,179.24	1,531.27	1,209.71
Net fund available ( <i>Per cent</i> )	16	7	4	4	6	5

The State Government did not raise market loans during the current year but internal debt receipts of Rs.2,891 crore were mainly on account of securities issued to NSSF (Rs.2,593 crore) and loans from NABARD (Rs.289 crore). Against these receipts, Government discharged the past debt obligations (principal plus interest) of Rs.3,926 crore resulting in negative net funds available under the debt account.

During the current year, the Government repaid GOI loans including interest amounting to Rs.1,491 crore and also discharged other obligations of Rs.19,355 crore along with interest. The net funds available on account of internal debt and loans and advances from GOI and other obligations after providing for the interest and repayments of the principal declined from 16 per cent in 2001-02 to 5 per cent in 2006-07.

## 1.8 Management of deficits

### 1.8.1 Trends in deficits

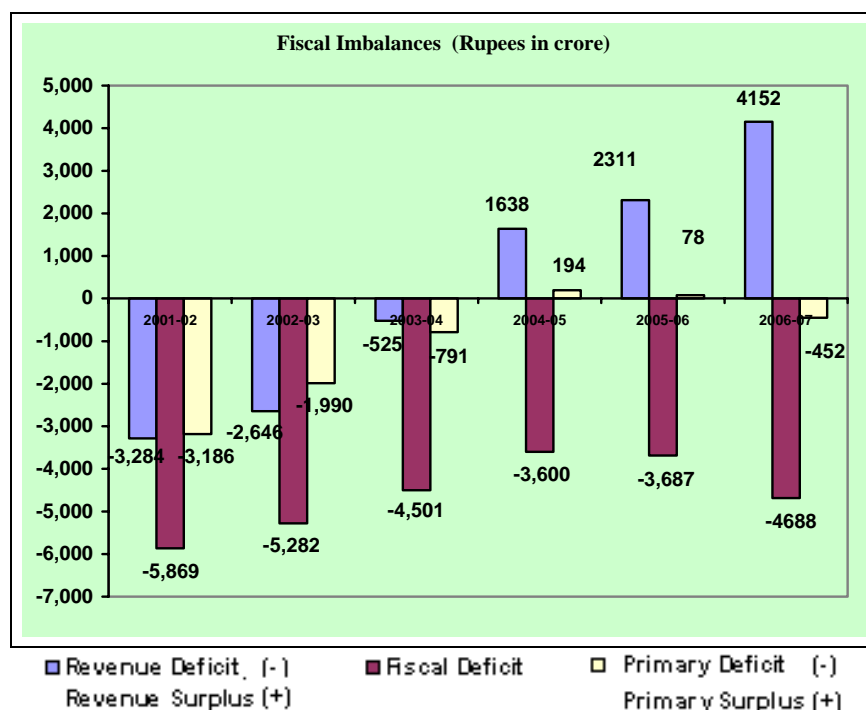
The deficit in the Government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the Government. Further, the ways in which the deficit is financed and the resources raised are applied are important pointers to its fiscal health. The trends in fiscal parameters depicting the position of fiscal equilibrium in the State are presented in table 33.

**Table 33 : Fiscal imbalances – Basic parameters**

(Amount Rupees in crore and Ratios in per cent)

Parameters	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
Revenue deficit (-) (RD) / Revenue surplus (+)	-3,284	-2,646	-525	1,638	2,311	4,152
Fiscal deficit (FD)	5,869	5,282	4,501	3,600	3,687	4,688
Primary deficit (-) (PD) / Primary surplus (+)	-3,186	-1,990	-791	194	78	-452
RD/ GSDP	3.04	2.25	0.41	---	---	---
FD/ GSDP	5.44	4.50	3.50	2.42	2.16	2.42
PD/ GSDP	2.95	1.69	0.62	0.13	0.05	0.23
RD/FD	55.9	50.1	11.7	---	---	---

Revenue surplus is the excess of revenue receipts over revenue expenditure. From 2004-05, the State's finances showed revenue surplus which increased from Rs.1,638 crore in 2004-05 to Rs.4,152 crore in 2006-07. Fiscal deficit is the excess of total expenditure over non-debt receipts (revenue receipts, recovery of loans and misc. capital receipts). Fiscal deficit increased by Rs.1,001 crore from Rs.3,687 crore to Rs.4,688 crore due to increase in capital expenditure including loans and advances (Rs.2,778 crore) and reduction of Rs.64 crore in non-debt capital receipts. The increase in revenue surplus during 2006-07 may however, be assessed keeping in view of the fact that non-tax revenue of the State is inclusive of debt waiver of Rs.358 crore each for the years 2005-06 and 2006-07 granted by the Government of India under the scheme of DCRF. This amount of debt waiver which is credited under non-tax receipts as an incentive, were adjustments on account of debt waiver in terms of the TFC by contra entry under loans and advances from the Central Government.



### 1.8.2 Quality of deficit/surplus

The ratio of revenue deficit (RD) to fiscal deficit (FD) and the decomposition of primary deficit<sup>3</sup> (PD) into primary revenue deficit<sup>4</sup> and capital expenditure (including loans and advances) would indicate the quality of deficit in the States' finances. The ratio of RD to FD indicates the extent to which borrowed funds were used for current consumption. The ratio of RD to FD declined from 56 per cent in 2001-02 to 12 per cent in 2003-04 and thereafter the revenue account turned into surplus which has consistently increased during the last three years. This trajectory shows a consistent improvement in the quality of the deficit during 2004-07 as the borrowed funds were used in activities resulting in expansion in the asset backup of the State. Table 34 below shows the bifurcation of the factors resulting in primary deficit or surplus of the State during the period 2001-07.

**Table 34 : Primary deficit/surplus-bifurcation of factors**

(Rupees 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)
2001-02	15,356	15,922	2,106	514	18,542	-566	-3,186
2002-03	17,097	15,523	2,936	628	19,087	1,574	-1,990
2003-04	20,824	17,575	3,029	1,011	21,615	3,249	-791
2004-05	26,617	21,138	4,674	611	26,423	5,479	194
2005-06	30,476	24,276	5,822	300	30,398	6,200	78
2006-07	37,647	29,199	8,543	357	38,099	8,448	-452

<sup>3</sup> Primary deficit defined as the fiscal deficit net of interest payments indicates the extent of deficit which is an outcome of the fiscal transactions of the States during the course of the year.

<sup>4</sup> Primary revenue deficit defined as gap between non interest revenue expenditure of the state and its non-debt receipts indicates the extent to which the non-debt receipts of the State are able to meet the primary expenditure incurred under revenue account.

In 2001-02 non-debt receipts were lower than the primary revenue expenditure<sup>5</sup> and 56 per cent of borrowed funds were used for meeting current expenditure. Due to acceleration of tax revenue from 2002-03 onwards, though non-debt receipts of the State were more than the primary revenue expenditure, the surplus of non-debt receipts were not enough to meet the expenditure on capital account resulting in primary deficit which however consistently declined from Rs.3,186 crore in 2001-02 to Rs.791 crore in 2003-04. During 2004-05 and 2005-06, the non debt receipts were adequate to meet the expenditure requirements under the capital account resulting in primary surplus during these years. On account of a steep increase of Rs.2,778 crore in capital expenditure (45 per cent), primary account had indicated a marginal deficit of Rs.452 crore during the current year.

## 1.9 Fiscal ratios

The finances of a State should be sustainable, flexible and non-vulnerable. Table 35 below presents a summarised position of Government Finances during the period 2001-2007, with reference to certain key indicators that help assess the adequacy and effectiveness of available resources and their application, highlight areas of concern and captures its important facts.

**Table 35 : Indicators of fiscal health (in per cent)**

Fiscal ratios	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
<b>Resource mobilisation</b>						
Revenue receipts (RR)/GSDP	14.2	13.8	16.1	17.9	17.8	19.4
Revenue buoyancy	0.7	0.6	3.0	1.8	1.0	1.7
Own tax/GSDP	9.1	8.9	9.8	10.8	10.9	12.0
<b>Expenditure management</b>						
Total expenditure (TE)/GSDP	19.7	19.0	19.7	20.3	20.0	21.8
Revenue receipts /Total expenditure	72.2	72.2	82.0	87.9	88.8	88.8
RE/Total expenditure	87.7	84.1	84.0	82.5	82.1	79.0
Salary expenditure on social & economic services/RE	19.8	19.1	17.8	15.6	15.4	14.3
<b>Non-salary expenditure on social &amp; economic services/RE</b>	43.8	40.1	36.7	41.5	44.7	49.6
Capital expenditure (CE)/TE	10.1	13.5	12.4	15.8	17.2	20.4
CE on social & economic services/TE	9.9	13.1	11.9	15.4	16.5	19.6
Buoyancy of TE with RR	3.2	1.0	0.5	0.7	0.9	1.0
Buoyancy of RE with RR	3.4	0.2	0.5	0.6	0.9	0.8
<b>Management of fiscal imbalances</b>						
Revenue deficit (-) (RD) / Revenue Surplus (+) (Rs. in crore)	-3,284	-2,646	-525	1,638	2,311	4,152
Fiscal deficit (Rs. in crore)	5,869	5,282	4,501	3,600	3,687	4,688
Primary deficit -(PD)/Primary surplus (+)	-3,186	-1,990	-791	194	78	-452
Revenue deficit / fiscal deficit	55.9	50.1	11.7	---	---	---
<b>Management of fiscal liabilities</b>						
Fiscal liabilities (FL)/GSDP	30.2	31.7	32.6	31.6	30.6	29.7
Fiscal liabilities/RR	212.6	230.3	202.1	176.7	172.1	153.5
Buoyancy of FL with RR	6.6	2.6	0.4	0.4	0.8	0.4
Buoyancy of FL with own receipts	9.9	2.0	0.4	0.4	1.2	0.5
PD vis-a-vis quantum spread	2.3	10.69	-	-	-	0.13
Net fund available (%)	16	7	4	4	6	5
<b>Other fiscal health indicators</b>						
Return on investment (Rs. in crore)	10.6	21.3	18.0	16.7	16.9	19.5
BCR (Rs. in crore)	(-) 879	(-) 645	1,571	4,879	5,483	9,415
Financial assets / liabilities	0.7	0.7	0.7	0.8	0.8	0.9

<sup>5</sup> Primary revenue expenditure of the State defined as the total expenditure net of the interest payments indicates the expenditure incurred on the transactions undertaken during the year.



The ratios of revenue receipts and State's own taxes to GSDP indicate the adequacy of the resources. The buoyancy of the revenue receipts indicates the nature of the tax regime and the State's increasing access to resources. Revenue receipts are comprised not only of the tax and non-tax resources of the State but also the transfers from GOI. The ratio of revenue receipts to GSDP during the current year increased by around two percentage points over the previous year. During 2001-07, the ratio of own taxes to GSDP showed continued improvement.

Various ratios concerning the expenditure management of the State indicate quality of its expenditure and sustainability of these in relation to its resource mobilisation efforts. The revenue expenditure as a percentage to total expenditure showed a continuous declining trend from 88 in 2001-02 to 79 in 2006-07.

Increasing reliance on revenue receipts to finance the total expenditure which amounts to 89 *per cent* during 2005-07 indicated decreasing dependence on borrowed funds. This was also reflected by the low ratio (less than one) of fiscal liabilities to revenue receipts. Increasing proportion of plan expenditure and capital expenditure in the total expenditure also indicated improvement in both developmental and quality of expenditure. Significant increase in revenue surplus with fiscal deficit at less than three *per cent* of GSDP during 2005-07 indicated improvement in fiscal position of the State. The Balance from Current Revenue (BCR) (Rs.9,415 crore) increased by 72 *per cent* over previous year indicating availability of funds for programme spending after meeting non-plan expenditure on revenue account.

### **1.10 Conclusion**

The fiscal position of the State viewed in terms of trends in fiscal parameters-revenue and fiscal deficit/surplus showed consistent improvement during the period 2002-07. The steep increase in revenue surplus, with fiscal deficit at less than three *per cent* of GSDP over the past three years indicated the fiscal health of the State. The total non-plan revenue expenditure constituted 77 *per cent* of total revenue expenditure of which, 67 *per cent* of expenditure was on salaries, pensions, subsidies and interest payments leaving relatively less resources for effective delivery and expansion of social and economic services. Although the share of re-payment of off-budget borrowings in the State in its capital expenditure has declined in 2006-07 from the level of 35 per cent in 2005-06, yet it constituted 28 per cent during the current year. Strain on the fiscal budget of the State due to negligible returns from investments in Government companies/statutory corporations and meagre recovery of loans and advances continued to be a cause of concern.

