EXECUTIVE SUMMARY

In November 2006, Government of Mizoram responded to the recommendations of the Twelfth Finance Commission (TFC) by legislating its "Fiscal Responsibility and Budget Management (FRBM) Act" to ensure prudence in fiscal management and fiscal stability by progressive reduction of revenue deficit and fiscal deficit. The State Government formulated roadmap and reform agenda through its own Fiscal Correction Path (FCP) in the medium term with long-term goals of securing growth stability for its economy. The State Government's commitment to carry forward those reforms is largely reflected in certain policy initiatives announced in the subsequent budget. The benefits of FRBM legislation have been realized to a great extent in terms of reduction of deficit indicators but, the State Government still needs fiscal correction in areas like the introduction of new pension scheme, setting up of guarantee redemption fund, putting a check on increasing revenue expenditure and a host of other institutional and sectoral reforms measures. This will go a long way in building up the much needed "fiscal space"[1] for improving the quality of public expenditure and to promote fiscal stability.

The State Government has considerably improved the institutional mechanism on fiscal transparency as evident from the year-to-year presentation of the performance of the State during the FRBM Act regime in terms of key fiscal target fixed for selected variables laid down in the Act. Those outcome indicators tend to serve the limited purpose of measuring the performance against the targets. They do not, however, give the "big picture" of the status of financial management including debt position and cash management etc. for the benefit of the State Legislature and other stakeholders.

The Comptroller and Auditor General's (CAG's) Civil Audit Reports are an effort to fill this gap. CAG's reports have been commenting upon the Government's finances for over two years since FRBM legislation and two reports[2] have been published prior to this report. These comments then formed a part of the civil audit report but it was seen that the audit findings on the State finances remained camouflaged in the large body of audit findings on compliance and performance audits. The obvious fallout of this well intentioned but all inclusive reporting was that the financial management portion of these findings did not receive proper attention. In recognition of the need to bring State finances to center-stage once again, stand alone report on State Government finances is considered an appropriate audit response to this challenge. Accordingly, from the report year 2009 onwards, CAG has decided to bring out a separate volume titled "Report on State Finances".

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1 Efficiency in Public Expenditure.

2 Report of the CAG of India, Government of Mizoram, for the year 2006-07 and 2007-08.

THE REPORT

Based on the audited accounts of the Government of Mizoram for the year ending March 2009, this report provides an analytical review of the annual accounts of the State Government. The report is structured in three chapters.

Chapter-I is based on the audit of Finance Accounts and makes an assessment of Mizoram Government's fiscal position as on 31 March 2009. It provides an insight into the trends in committed expenditure, borrowing pattern. Besides, a brief accounts of central funds transferred directly to the State implementing agencies through off-budget route, is also included herein.

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

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

The report also has an appendices of additional data collated from several sources in support of the findings and at the end gives a glossary of selected terms related to State economy, used in this report.

AUDIT FINDINGS AND RECOMMENDATIONS

Fiscal Correction : Although the Government of Mizoram has been successful in bringing down the core fiscal deficit indicators within the ambit of TFC targets in time, some areas of concern relating to fiscal correction still remains. There is need for the State to undertake corrective fiscal reforms programme to eliminate the mismatch between receipt and expenditure. In particular the Non-Plan Revenue Expenditure needs to be curtailed. There is a need to initiate adequate measures to contain expenditure on pension and salaries relative to its own resources to achieve the FRBM targets within the award period **(Para-1.3).** The State has the reasonable prospect of achieving the targets set out in the FRBM Act provided an effort is made to strengthen the tax administration, reduce cost of tax administration and to collect revenue arrears **(Para-1.3.2)** in particular.

Greater priority to Capital Expenditure : The State Government may lay greater emphasis on the rationalization of Non-Plan Revenue Expenditure (NPRE) so that resources may be diverted to plan expenditure particularly to Capital Expenditure (CE) as well as for creation of capital assets. While there is adequate thrust for development expenditure, the CE/AE ratio in 2008-09 for Mizoram was marginally lower than the national average. Thus, the CE requires greater thrust **(Para-1.5.1)**.

Review of Government investment : The investment position of the Government has been dismal over the last five years with 'nil' returns whereas average interest outgo was in the range of 6.43 to 7.57 *per cent* (**Para-1.6.2**). This is obviously an unsustainable position. The State Government should therefore hasten to seek better value for money in investment. Otherwise high cost borrowed funds invested in projects without financial returns will continue to strain the economy. Projects which are justified on account of low financial but high socio-economic return, may be identified and prioritized with full justification for the high-cost borrowings. Time has come to revisit the workings of State owned public sector undertakings (**Para-1.6.2**) and work out either a revival strategy (for those that are strategic in nature and can be made viable) or close down (if they are not likely to be viable given current market conditions). Moreover, no specific law under Article 293 of the Constitution had been passed by the State Legislature laying down the maximum limit within which Government may give guarantees on the security of the Consolidated Fund of the State. The State Government is yet to implement the recommendations of the TFC by setting up a Guarantee Redemption Fund (GRF) through earmarked guarantee fees **(Para-1.7.3)**.

Prudent Cash Management : The cash balances decreased during the year 2008-09. Interest receipt on investments from cash balances during the year was 10 *per cent* against the payment of interest at the rate of 6.46 *per cent* by the Government on its borrowings. At the same time the investments from cash balances decreased by 18 *per cent* **(Para-1.6.4)** over the previous year. Proper debt management through advance planning could have maximised the interest receipts from the investments from cash balances.

Debt Sustainability : A prior condition for the debt sustainability is the debt stabilization in terms of debt/GSDP ratio. The Government of Mizoram should ideally keep the debt-GSDP ratio stable. Borrowed funds should be used as far as possible only to fund capital expenditure and revenue expenditure should be met from revenue receipts. Maintaining a calendar of borrowings to avoid bunching towards the end of the fiscal year and clear understanding of the maturity profile of debt payments will go a long way in prudent debt management.

Oversight of funds transferred directly from the Government of India (GOI) to the State Implementing Agencies : Funds flowing directly to the implementing agencies through off-budget routing inhibits FRBM requirements of transparency and therefore bypass accountability. There is no single agency monitoring its use and there is no readily available data on the amounts spent in any particular year on major flagship and other important schemes **(Para-1.2.2)**.

A system has to be urgently put in place to ensure proper accounting of these funds and the updated information should be validated by the State Government as well as the Accountant General (A&E).

Financial Management and Budgetary Control : Slow pace of programme implementation in the State left an overall savings of Rs.578.03 crore offset by excess of Rs.30.13 crore, which requires regularization under Article 205 of the Constitution of India (**Para-2.2, 2.3.6 and 2.3.7**). Planning and programme implementation Departments and Finance Department posted large savings persistently for the last five years (**Para-2.3.2**). There were also instances of inadequate provision of funds and unnecessary/excessive re-appropriation. Rush of expenditure at the end of the year is another chronic feature noticed in the overall financial management. In many cases, the anticipated savings were not surrendered. Detailed bills were not submitted for large amount of advances drawn on abstract contingent bills (**Para-2.4.1**) and substantial amounts of expenditure remained un-reconciled by controlling officers (**Para-2.4.2**). Budgetary control should be strictly observed to avoid such deficiencies in financial management. Last minute fund releases and issuance of re-appropriation orders/surrender orders should be avoided.

Financial Reporting : State Government's compliance with various rules, procedures and directives was unsatisfactory as evident from delays in furnishing utilization certificates against the loans and grants from various grantee institutions. Delays also figured in submission of annual accounts by Autonomous Bodies/Authorities. There were instances of losses and misappropriations. Departmental inquiries in such cases should be expedited to bring the defaulters to book. Internal control in all the organizations should be strengthened to prevent such cases in future.