CHAPTER I

FINANCES OF THE STATE GOVERNMENT

1.1 Introduction

This chapter provides a broad perspective of the finances of the Government of Tamil Nadu during the current year and analyses critical changes in the major fiscal aggregates relative to the previous year, keeping in view the overall trends during the last five years. The structure of Government Accounts and the layout of the Finance Accounts are shown in **Appendix 1.1.** The methodology adopted for the assessment of the fiscal position of the State is given in **Appendix 1.2.** A time series data on State Government finances is given in **Appendix 1.3.**

1.1.1 Summary of Current Year's Fiscal Transactions

Table 1.1 presents the summary of the State Government's fiscal transactions during the current year (2008-09) vis-à-vis the previous year while **Appendix 1.4** provides details of receipts and disbursements as well as the overall fiscal position during the current year.

Table 1.1: Summary of Current Year's Fiscal Operations

(Rupees in crore)

2007-08	Receipts	2008-09	2007-08	Disbursements	2008-09		
Section-A: Revenue					**Non Plan**	**Plan**	**Total**
47,520	Revenue receipts	55,042	42,975	Revenue expenditure	43,052	10,538	53,590
29,619	Tax revenue	33,684	16,129	General Services	18,550	28	18,578
3,304	Non-tax revenue	5,712	15,726	Social Services	12,996	8,375	21,371
8,065	Share of Union Taxes/ Duties	8,511	7,771	Economic Services	7,815	1,846	9,661
6,532	Grants from Government of India	7,135	3,349	Grants-in-aid and Contributions	3,691	289	3,980
Section-B: Capital							
..	Misc. Capital Receipts	..	7462	Capital Outlay	33	9,071	9,104
1,013	Recoveries of Loans and Advances	1,934	1,782	Loans and Advances disbursed	1,920	910	2,830
7,647	Public Debt receipts	11,841	3,546	Repayment of Public Debt	**	**.	2,216
Nil	Contingency Fund	Nil	Nil	Contingency Fund	**	**	1
65,917*	Public Account receipts	81,409	64,661*	Public Account disbursements	**	**	78,429
10,501*	Opening Cash Balance	12,173	12,172*	Closing Cash Balance	**	**	16,229
1,32,598	**Total**	**1,62,399**	**1,32,598**	**Total**			**1,62,399**

(Source: Finance Accounts for the years 2007-08 and 2008-09)

* Differ from last year due to correction

** Bifurcation of Plan and Non- Plan not available

The significant changes during 2008-09 as compared to the previous year are given below:

- Revenue receipts of the State increased by Rs 7,522 crore (16 *per cent*) over the previous year, mainly due to increase in the State's own tax revenue (Rs 4,065 crore) and non-tax revenue (Rs 2,408 crore).

- Revenue expenditure increased by Rs 10,615 crore (25 *per cent*) over the previous year, mainly due to increase in expenditure on General Services (Rs 2,449 crore) and Social Services (Rs 5,645 crore) and Economic Services (Rs 1,890 crore).

- While the expenditure on Social Services registered an increase of 36 *per cent*, expenditure on Economic Services increased by 24 *per cent*.

- Capital expenditure on asset creation increased by Rs 1,642 crore (22 *per cent*) over the previous year.

- Public Account receipts and disbursements increased by Rs 15,492 crore (24 *per cent*) and Rs 13,768 crore (21 *per cent*) respectively. Net receipts under Public Account increased by Rs 1,724 crore over the previous year.

- The net impact of these transactions led to a significant increase of Rs 4,057 crore in the cash balance at the end of the year over pervious year.

Review of the fiscal situation

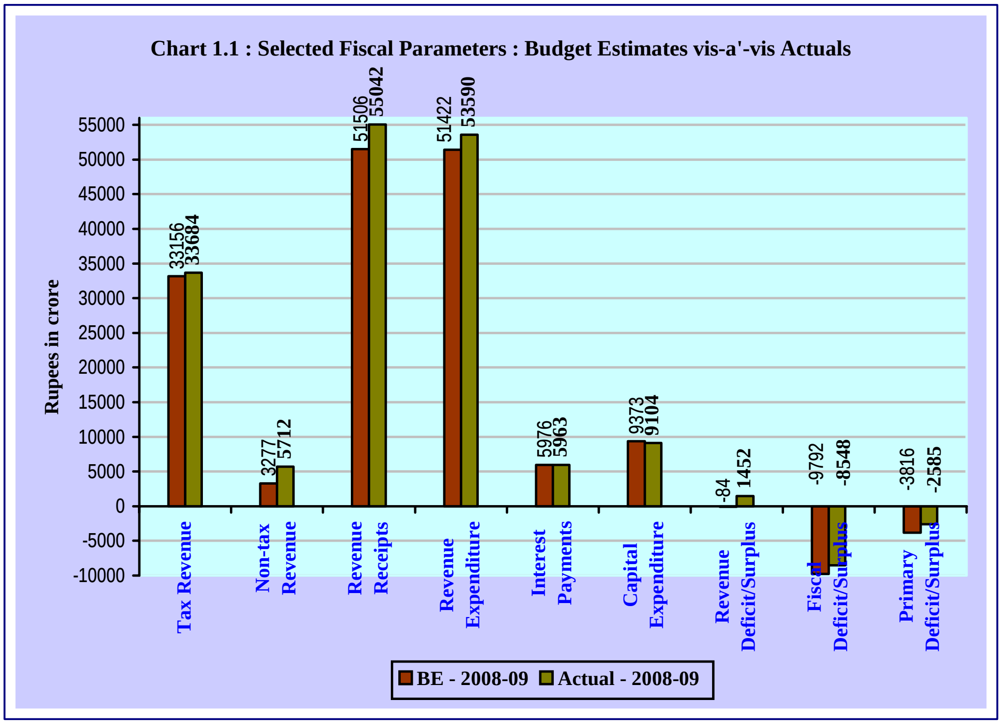
As per the Tamil Nadu Fiscal Responsibility Act, 2003 (FRBM Act), in line with the recommendations of the Twelfth Finance Commission (TFC), the State Government was to eliminate the revenue deficit by the end of 2007-08 and reduce the fiscal deficit to not more than three *per cent* of the Gross State Domestic Product (GSDP) by 2008-09. Further, the Act envisaged to cap outstanding guarantees at a level not exceeding the previous year's revenue receipts or 10 *per cent* of GSDP, whichever was the least.

The State has achieved and retained all the goals set in the FRBM Act. However, the surge in revenue expenditure vis-à-vis revenue receipts during 2008-09, if allowed to continue, poses a substantial threat to retention of the present fiscal situation.

Budget Analysis

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

Chart 1.1 presents the budget estimates and actuals for some important fiscal parameters.



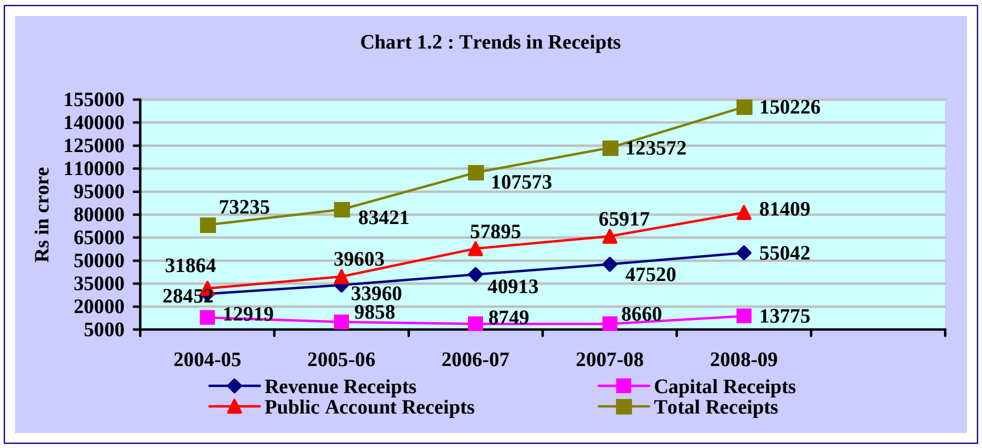
The actuals were fairly in line with estimates, barring the following:

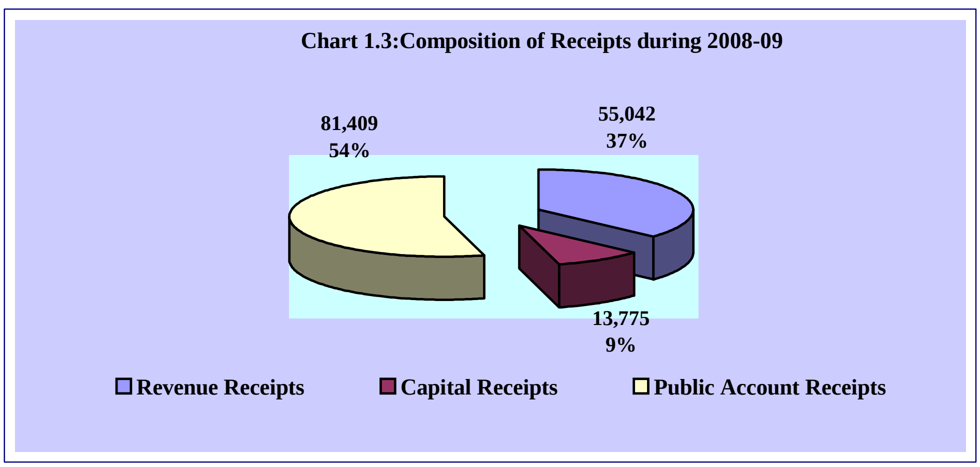
- Non-tax receipts surpassed the estimates by 74 *per cent*.
- While revenue receipts and revenue expenditure were higher than the estimates by Rs 3,536 crore (7 *per cent*) and Rs 2,168 crore (4.22 *per cent*) respectively, the capital expenditure fell short of the estimate by Rs 269 crore (2.87 *per cent*), indicating difficulties in fund absorption for capital works.
- Revenue deficit, fiscal deficit and primary deficit were off the mark, mainly due to the differences between estimates and actuals in revenue receipts and expenditure. Against an estimated revenue deficit of Rs 84 crore, the financial year ended with a revenue surplus of Rs 1,452 crore. The primary deficit was also Rs 2,585 crore against the estimate of Rs 3,816 crore.

1.2 Resources of the State

1.2.1 Resources of the State as per Annual Finance Accounts

Revenue and capital are the two streams of receipts that constitute the resources of the State Government. Revenue receipts consist of tax revenues, non-tax revenues, State's share of Union taxes and duties and grants-in-aid from the Government of India (GOI). Capital receipts comprise miscellaneous capital receipts such as proceeds from disinvestments, recoveries 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 the Public Account. **Table 1.1** presents the receipts and disbursements of the State during the current year as recorded in its Annual Finance Accounts while **Chart 1.2** depicts the trends in various components of the receipts of the State during 2004-09. **Chart 1.3** depicts the composition of resources of the State during the current year.





- The total resources of the State increased by Rs 26,654 crore (22 *per cent*) over the previous year, mainly due to increase of Rs 15,492 crore (24 *per cent*) in Public Account receipts and Rs 7,522 crore (16 *per cent*) in revenue receipts.

- Public Debt receipts went up by Rs 4,194 crore, an increase of 55 *per cent* over the previous year, mainly due to a substantial increase in open market borrowings. Open market borrowings increased from Rs 4,942 crore in 2007-08 to Rs 9,598 crore in 2008-09, a whopping 94 *per cent* over the previous year, accompanied by a sharp decrease of Rs 473 crore by way of resources raised through Special Securities issued to the National Small Savings Fund.

- The State's tax revenue increased from Rs 29,619 crore in 2007-08 to Rs 33,684 crore in 2008-09 (increase of 14 *per cent)*, but the percentage of tax receipts to revenue receipts declined from 62 *per cent* in 2007-08 to 61 *per cent* in 2008-09.

1.2.2 Funds transferred to State Implementing Agencies outside the State Budgets

The Central Government has been transferring a sizeable quantum of funds directly to State implementing agencies[1] for the implementation of various schemes/programmes in social and economic sectors which are recognized as critical. As these funds are not routed through the State Budget/State Treasury System, the Annual Finance Accounts do not capture the flow of these funds and to that extent, the State's receipts and expenditure as well as other fiscal variables/ parameters derived from them are underestimated. The funds directly transferred to State implementing agencies under nine major programmes assisted by Government of India are presented in **Table 1.2.**

Table 1.2: Funds Transferred Directly to State Implementing Agencies

(Rs in crore)

Programme/scheme	Implementing agency in the State	Funds transferred directly by Government of India during 2008-09
National Rural Employment Guarantee Scheme	District Rural Development Agencies	763
Sarva Shiksha Abhiyan	State Project Directorate	389
Accelerated Rural Water Supply Programme	Tamil Nadu Water Supply and Drainage Board	121
Rural Housing Programme (Indra Awas Yojana)	District Rural Development Agencies	101
National Rural Health Mission	State Health Mission	101
National AIDS Control including STD Control Programme	Tamil Nadu State AIDS Control Society	71
Swaranjayanti Gram Swarozgar Yojana (SGSY)	District Rural Development Agencies	47
Integrated Wasteland Development Programme	District Rural Development Agency	19
District Rural Development Agency - Administrative Fund	District Rural Development Agency	6
Total		**1,618**

(Source: Controller General of Accounts, Government of India)

[1] State implementing agencies include any organization/institution including non-Governmental organization which is authorized by the State Government to receive funds from the Government of India for implementing specific programmes in the State.

- Out of Rs 1,618 crore transferred to State implementing agencies, a major amount of Rs 936 crore (58 *per cent)* was transferred to District Rural Development Agencies. Direct transfer of funds from Union to State implementing agencies ran the risk of improper utilisation of funds by these agencies. Unless uniform accounting policies are followed by all these agencies with proper documentation and timely reporting of expenditure, it would be difficult to monitor the end use of these direct transfers.

1.3 Revenue Receipts

Statement-11 of the Finance Accounts details the revenue receipts of the Government. The revenue receipts consist of the State's own taxes and non-tax revenues, Central tax transfers and grants-in-aid from GOI. The trends and composition of revenue receipts over the period 2004-09 are presented in **Appendix 1.3** and depicted in **Charts 1.4 and 1.5** respectively.

Chart 1.4: Trends in Revenue Receipts

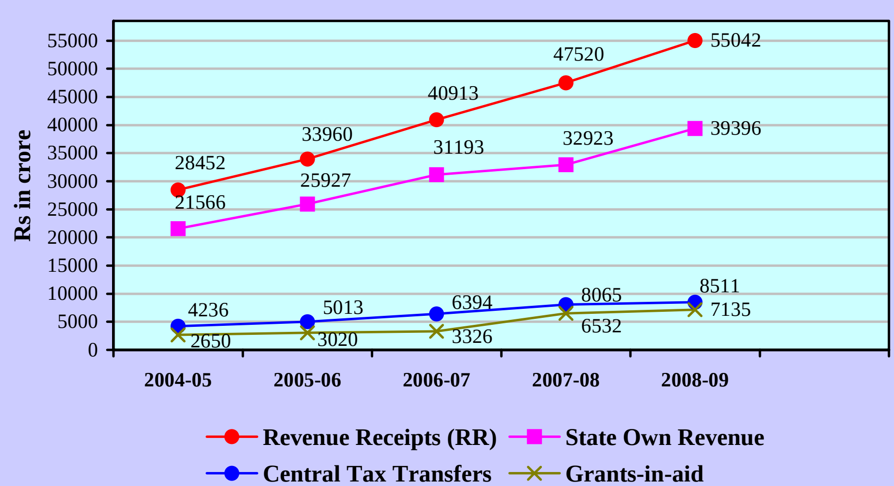
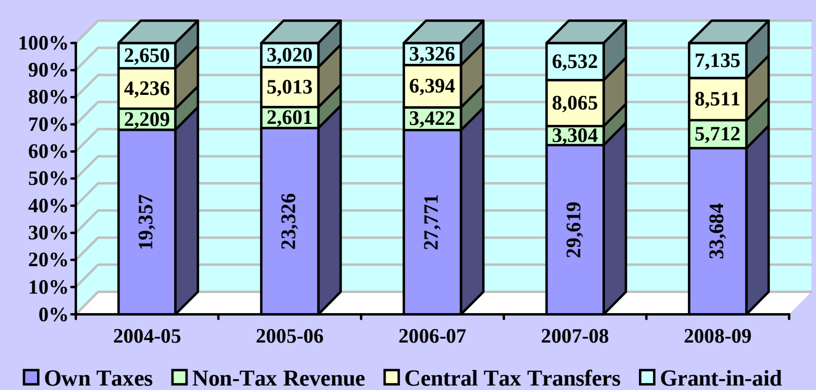


Chart 1.5: The Composition of Revenue Receipts during 2004-09



- The revenue receipts of the State grew by Rs 7,522 crore over the previous year. The growth was subdued at 16 *per cent* as against the average annual growth of 19 *per cent* during 2005-08. The sluggish growth in revenue receipts was due to the overall slowdown in the economy which impacted the State's own taxes and also the State's share of Union taxes.

- The increase of Rs 7,522 crore in revenue receipts (16 *per cent*) did not keep pace with the increase of Rs 10,615 crore in revenue expenditure (25 *per cent*).

- Non-tax revenue receipts registered a steep increase of 73 *per cent* from Rs 3,304 crore in 2007-08 to Rs 5,712 crore in 2008-09 due to receipt of Rs 2,046 crore by way of upfront land rent in respect of industrial lands leased out by the Government. Being a one time receipt, this may not help in sustenance of non-tax revenue at this level.

- Non-tax revenue during 2008-09 included Rs 263 crore received as debt relief from Government of India. The amount of receipt on this account was the same during 2007-08 as well.

The trends in revenue receipts relative to GSDP are presented in **Table 1.3** below:

Table 1.3: Trends in Revenue Receipts relative to GSDP

	2004-05	2005-06	2006-07	2007-08	2008-09
Revenue Receipts (RR) (Rupees in crore)	**28,452**	**33,960**	**40,913**	**47,520**	**55,042**
Rate of growth of RR (*per cent)*	20	19.4	20.5	16.1	15.8
RR/GSDP[2] (*per cent)*	14.2	15.2	16.6	17.0	16.2
Buoyancy Ratios[3]					
Revenue Buoyancy with reference to GSDP (ratio)	1.42	1.71	2.01	1.20	0.74
State's own tax Buoyancy with reference to GSDP (ratio)	1.51	1.81	1.87	0.50	0.64
Revenue Buoyancy with reference to State's own taxes (ratio)	0.93	0.95	1.07	2.4	1.16

(Source: Finance Accounts of Government of Tamil Nadu)

- The GSDP at the current rate was estimated to increase from Rs 2,79,287 crore in 2007-08 to Rs 3,39,212 crore in 2008-09, representing an increase of 21.46 *per cent.* However, the rate of growth of revenue receipts showed a declining trend despite the increase in GSDP, indicating that the State's aim to widen the tax base and augment revenue could not be achieved.

[2] Advance estimate of GSDP of Rs 3,39,212 crore has been adopted for 2008-09.

[3] Buoyancy ratio indicates the elasticity or degree of responsiveness of a fiscal variable with respect to a given change in the base variable. For instance, revenue buoyancy at 0.6 implies that revenue receipts tend to increase by 0.6 percentage points, if the GSDP increases by one *per cent*.

- The State's own tax buoyancy with reference to GSDP stood at 0.64 as against 1.2 prescribed by the TFC, indicating lower growth than the normative projection made by the Commission.

- Revenue receipts as a percentage of GSDP declined during the year 2008-09 after continuous increase during last three years.

- Revenue buoyancy with reference to GSDP and with reference to State's own taxes came down during the year. In 2006-07, the growth rate of revenue receipts was 2.01 times more than that of GSDP, but in the next two years, the low growth rate of revenue receipts relative to GSDP pushed the revenue buoyancy ratio down. The revenue buoyancy ratio was 0.74 in 2008-09.

1.3.1 State's Own Resources

As the State's share in Central taxes and grants-in-aid is determined on the basis of recommendations of the Finance Commission, collection of Central tax receipts, Central assistance for Plan schemes etc, the State's performance in mobilization of additional resources was assessed in terms of its own resources comprising revenue from its own tax and non-tax sources. The gross collection in respect of major taxes and duties as well as the components of non-tax receipts are given in **Table 1.4** below.

Table 1.4: Components of State's own resources

(Rs in crore)

Revenue Head	**2004-05**	**2005-06**	**2006-07**	**2007-08**	**2008-09**
Tax Revenue					
Taxes on sales, trades etc.	12,996	15,555	17,727	18,156	20,675
State excise	2,549	3,177	3,986	4,764	5,756
Taxes on vehicles	1,015	1,125	1,261	1,483	1,710
Stamp duty and Registration fees	1,604	2,085	2,997	3,805	3,794
Land revenue	72	179	121	78	208
Taxes on goods and passengers	764	985	1244	1,097	979
Other taxes[4]	357	220	435	236	562
Total	**19,357**	**23,326**	**27,771**	**29,619**	**33,684**
Non-Tax Revenue					
Interest receipts	566	797	1104	1242	1465
Dividends & Profits	24	22	30	40	36
Other non-tax receipts	1,619	1,782	2,288	2,022	4,211
Total	**2,209**	**2,601**	**3,422**	**3,304**	**5,712**

- As per the Medium Term Fiscal Policy Statement, tax revenue was projected as 10.10 *per cent* of GSDP. Against the projected revenue of

[4] Other taxes include taxes on immovable property other than agricultural land and taxes and duties on electricity.

Rs 34,260 crore, the State could realise Rs 33,684 crore, resulting in short collection of tax revenue of Rs 576 crore.

- Though the own tax revenue of the State increased by Rs 4,065 crore over the previous year, the growth rate of its own tax revenue, which averaged 15.4 *per cent* per annum during 2005-08 slowed down to 13.7 *per cent* during 2008-09.

- The marked decline in the growth rate of own tax revenue was mainly due to reduced collection of stamp duty and registration fees. The revenue through stamp duty and registration fees marginally declined by Rs 11 crore due to the impact of the economic slowdown as against the high annual average growth of 33.6 *per cent* during 2005-08. There was also a decrease of 10.75 *per cent* in respect of taxes on goods and passengers over the previous year's receipts, mainly due to decrease under tax on entry of goods into local areas.

1.3.2 Loss of Revenue due to Evasion of Taxes

Tax evasion leads to non-realisation of legally available revenue to the Government. As of 31 March 2008, the Commercial Taxes Department of the Government had detected 4,148 cases of evasion of sales tax / value added tax. During 2008-09, 410 new cases were detected. However, the department completed assessments only in respect of 650 cases leading to a pendency of 3,908 cases as at the end of March 2009. As assessments were not completed in a large number of cases, the extent of revenue realisable from tax evaders could not be assessed.

1.3.3 Revenue Arrears

As on 31 March 2009, revenue arrears amounted to Rs 9,874.97 crore (sales tax: Rs 9,871.35 crore; taxes on vehicles: Rs 3.62 crore). Out of this, Rs 3,445.60 crore was outstanding for more than five years (sales tax: Rs 3,443.53 crore; taxes on vehicles: Rs 2.07 crore). Recovery proceedings for Rs 1,516.83 crore (sales tax) were stayed by judicial authorities and sales tax recovery amounting to Rs 422.07 crore was proposed to be written off.

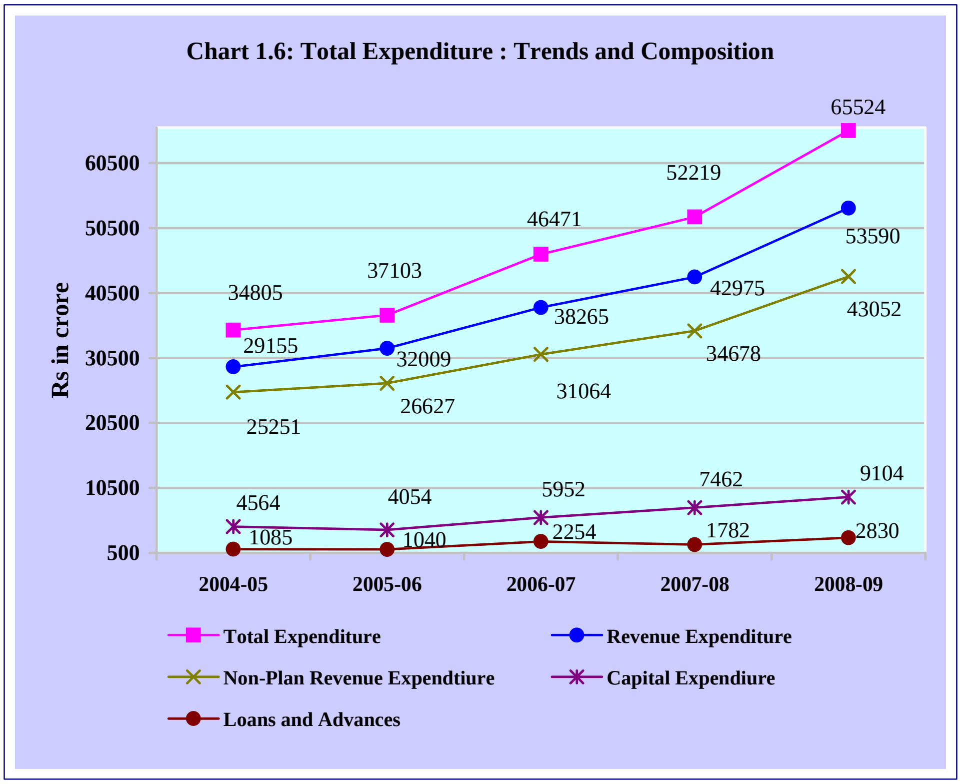
Considering the huge sums involved, Government needs to take note of these mounting arrears.

1.4 Application of Resources

Analysis of the allocation of expenditure at the State Government level assumes significance since major expenditure responsibilities are entrusted with them. Within the framework of fiscal responsibility legislations, there are budgetary constraints in raising public expenditure financed by deficit or borrowings. It is, therefore, important to ensure that the ongoing fiscal correction and consolidation process at the State level is not at the cost of expenditure, especially the expenditure directed towards development of social sectors.

1.4.1 Growth and Composition of Expenditure

Chart 1.6 presents the trends in total expenditure over a period of five years (2004-09) and its composition both in terms of 'economic classification' and 'expenditure by activities' is depicted in **Charts 1.7 and 1.8** respectively.



- The total expenditure[5] during 2008-09 increased by Rs 13,305 crore (25 *per cent*) over the previous year. The revenue expenditure increased by Rs 10,615 core (24.7 *percent),* capital expenditure by Rs 1,642 crore (22 *per cent)* and loans and advances by Rs 1,048 crore (58.8 *per cent).* The revenue expenditure was 81.78 *per cent* of the total expenditure, of which 80 *per cent* was on the Non-Plan component.

- The Non-Plan revenue expenditure increased by Rs 8,374 crore (24.14 *per cent*) as against an increase of Rs 2,241 crore (27 *per cent*) in revenue expenditure under Plan heads.

- The capital expenditure increased by 22 *per cent*, which was mainly due to increase of Rs 680.50 crore (138.87 *per cent)* on power projects, Rs 522.31 crore (24 *per cent)* on roads and bridges and Rs 307.30 crore (30.62 *per cent)* on other rural development programmes.

[5] Total expenditure includes revenue expenditure, capital expenditure and loans and advances.

- Revenue receipts of the State met 84 *per cent* of the total expenditure during 2008-09 as against 82 *per cent* during 2004-05 and 91 *per cent* during 2007-08.

Chart 1.7: Total Expenditure : Trends in Share of its Components

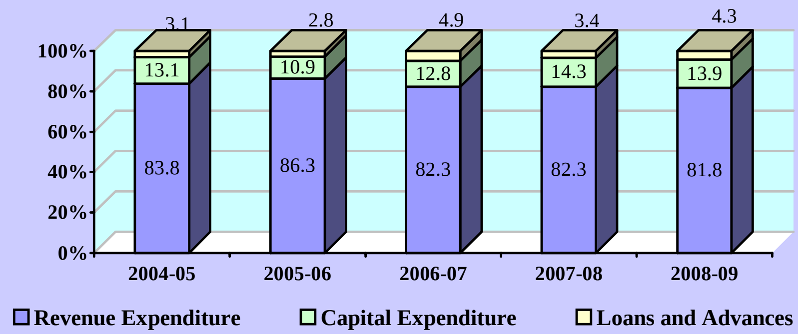
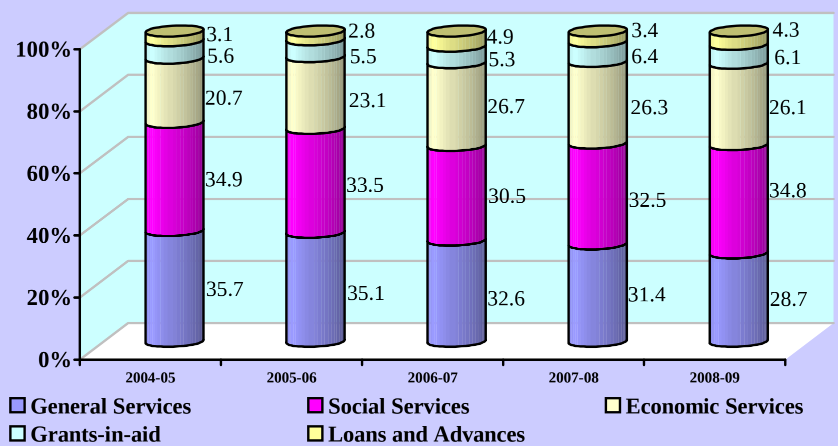


Chart 1.8: Total Expenditure: Trends by 'Activities'



- The expenditure on General Services, Social Services and Economic Services during 2008-09 grew by 15 *per cent*, 36 *per cent* and 24 *per cent* respectively over the previous year.

- The steep increase in the expenditure on Social Services was mainly on account of increased spending of Rs 1,901 crore on General Education, Rs 793 crore on housing, Rs 453 crore on Medical and Public Health and Rs 953 crore on relief on account of natural calamities.

- The expenditure on General Education (Rs 8,466 crore) and Health and Family Welfare (Rs 2,288 crore) surpassed the normative projections made by TFC by Rs 1,975 crore and Rs 708 crore respectively, indicating greater thrust laid on these areas by the Government. It was, however, noticed that the salaries and wages component of the expenditure for General Education grew by 47 *per cent* against TFC's recommended growth of six *per cent*. Similarly, the salaries and wages component under Health and Family Welfare grew by 44 *per cent* against TFC's recommended growth rate of five *per cent*.

- Expenditure on repayment of Public Debt came down from Rs 3,546 crore in 2007-08 to Rs 2,216 crore in 2008-09.

1.4.2 Committed Expenditure

The committed expenditure of the State Government on revenue account mainly consists of interest payments, expenditure on salaries and wages, pensions and subsidies. **Table 1.5** and **Chart 1.9** present the trends in the expenditure on these components during 2004-09.

Table 1.5: Components of Committed Expenditure

(Rupees in crore)

Components of Committed Expenditure	**2004-05**	**2005-06**	**2006-07**	**2007-08**	**2008-09**
Salaries and wages, *of which*	8,406	8,376	8,694	9,690	12,859
	(29.5)	(24.6)	(21.2)	(20.4)	(23.4)
Non-Plan Head	NA	7,449	7,673	8,641	11,470
Plan Head*	NA	927	1,021	1,049	1,389
Salary grants**	1,469	1,590	1,863	2,072	2,756
	(5.1)	(4.6)	(4.5)	(4.3)	(5)
Interest Payments	4,755	4,559	5,506	6,086	5,963
	(16.7)	(13.4)	(13.5)	(12.8)	(10.8)
Expenditure on Pension	3,902	4,460	5,430	6,017	7,735
	(13.7)	(13.1)	(13.3)	(12.7)	(14)
Subsidies	2,513	3,426	4,177	4,305	6,600
	(8.8)	(10.1)	(10.2)	(9.1)	(12)
Total	**21,045 (73.8)**	**22,412 (65.3)**	**25,670 (62.7)**	**28,170 (59.3)**	**35,913 (65.5)**

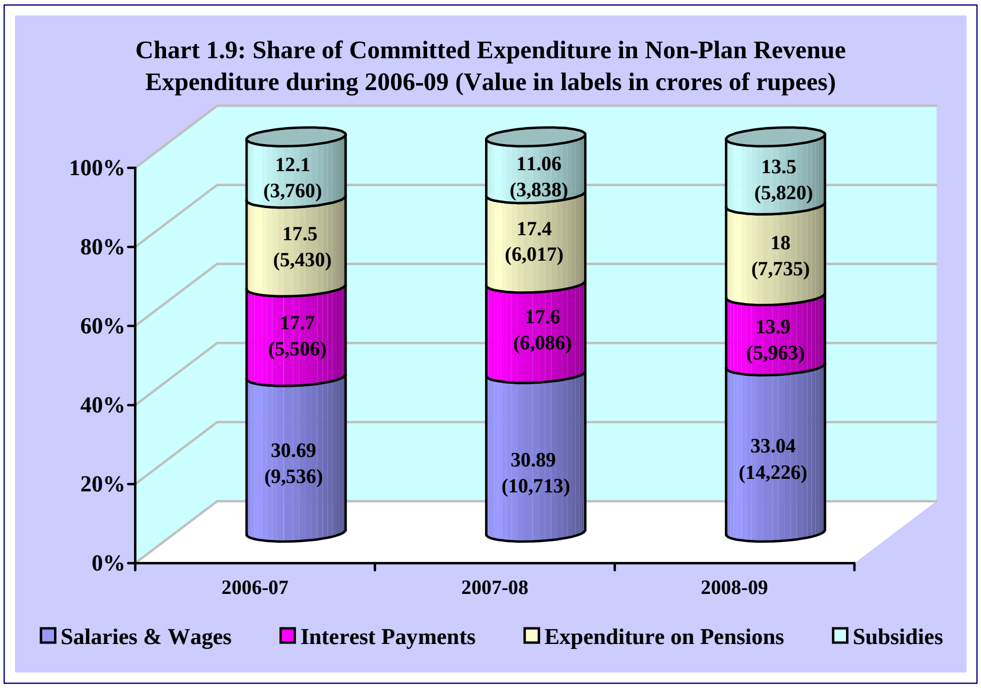
(Source: Finance Accounts of Government of Tamil Nadu)

Figures in the parentheses indicate percentage of revenue receipts

NA: Not Available

* Plan head also includes the salaries and wages paid under Centrally Sponsored Schemes

** Salary grants are released to aided educational institutions and Urban Local Bodies towards meeting the expenditure on staff salaries of teachers and staff in Urban Health Facilities respectively.



- The committed expenditure stood at 65.5 *per cent* of total revenue receipts of the State during 2008-09 as against 62.7 *per cent* during 2006-07 and 59.3 *per cent* during 2007-08.

- The committed expenditure stood at 78.44 *per cent* of the Non-Plan revenue expenditure during 2008-09 as against 77.99 *per cent* during 2006-07 and 76.95 *per cent* during 2007-08.

- The expenditure on salaries and wages, inclusive of salary grants was Rs 15,615 crore and accounted for 39 *per cent* of revenue expenditure net of interest and pension as against TFC's normative prescription of 35 *per cent*.

- The expenditure on salaries and wages, which gradually declined from the level of 34.6 *per cent* of revenue receipts in 2004-05 to the level of 24.7 *per cent* in 2007-08, moved upward in 2008-09 and stood at 28.4 *per cent*. The increase was mainly due to payment of interim relief to Government staff.

- Expenditure on pension, as a percentage of revenue receipts, increased from 12.7 *per cent* in 2007-08 to 14 *per cent* in 2008-09.

- Expenditure on pension at Rs 7,735 crore overshot the TFC's projection of Rs 6,732 crore. There was an increase of 29 *per cent* in pension expenditure over the previous year.

- Subsidies were on a continuous increase. They went up from Rs 2,513 crore in 2004-05 to Rs 6,600 crore in 2008-09. The increase during

2008-09 was Rs 2,295 crore, which was 55 *per cent* more than the previous year. The increase was mainly due to increased spending on subsidized power (Rs 1,167 crore in 2007-08 to Rs 1,291 crore in 2008-09), subsidy for crop husbandry (Rs 53 crore in 2007-08 to Rs 326 crore in 2008-09) and relief on account of natural calamities (Rs 142 crore in 2007-08 to Rs 501 crore in 2008-09).

- The expenditure towards interest payments declined by Rs 123 crore (2.04 *per cent*) over the previous year. As a percentage of Non-Plan expenditure, it came down from 17.6 in 2007-08 to 13.9 in 2008-09.

1.4.3 Financial Assistance by State Government to Local Bodies and other institutions

The quantum of assistance provided by way of grants and loans to local bodies and others during the current year relative to the previous years is presented in **Table 1.6.**

Table 1.6: Financial Assistance to Local Bodies etc

(Rupees in crore)

Financial Assistance to Institutions	2004-05	2005-06	2006-07	2007-08	2008-09
Educational Institutions (Aided Schools, Aided Colleges, Universities, etc.)	388	484	570	605	433
Municipal Corporations and Municipalities	919	954	1591	393	1865
Zilla Parishads and Other Panchayati Raj Institutions	1,584	1,287	1,508	3,216	1,890
Development Agencies	189	202	295	920	217
Hospitals and Other Charitable Institutions	9	20	20	19	106
Other Institutions[6]	2,395	2,119	4,753	3,248	5,726
Total	**5,484**	**5,066**	**8,737**	**8,401**	**10,237**
Assistance as per percentage of Revenue Expenditure	19	16	23	20	19

(Source: Accounts compiled by the Accountant General (A&E), Tamil Nadu)

- Financial assistance to local bodies and other institutions increased from Rs 5,484 crore in 2004-05 to Rs 10,237 crore in 2008-09. As a percentage of the revenue expenditure, it declined marginally from the level of 20 *per cent* in 2007-08 to 19 *per cent* in 2008-09. Assistance to hospitals and other charitable institutions showed a quantum jump from Rupees nine crore in 2004-05 to Rs 106 crore in 2008-09. As a percentage of revenue expenditure, the assistance to municipal corporations and municipalities increased from 0.91 *per cent* in 2007-08 to 3.48 *per cent* in 2008-09. However, the assistance to educational institutions showed a decline of 28 *per cent* over the previous year.

[6] Institutions/agencies connected with water supply and sanitation, housing, social welfare, labour and employment, forestry and wild life, agriculture and allied activities, village and small industries, industries and minerals and relief on account of natural calamities.

1.5 Quality of Expenditure

The availability of better social and physical infrastructure in the State generally reflects the quality of its expenditure. The improvement in the quality of expenditure basically involves three aspects, viz., adequacy of the expenditure (i.e. adequate provisions for providing public services); efficiency of expenditure use and its effectiveness (assessment of outlay-outcome relationships for select services).

1.5.1 Adequacy of Public Expenditure

The expenditure responsibilities relating to the social sector and the economic infrastructure assigned to the State Governments are largely State subjects. Enhancing human development levels requires the States to step up their expenditure on key Social Services like education, health etc. Low levels of spending on any sector by a particular State may be either due to the low fiscal priority attached by the State Government to these sectors or on account of the low fiscal capacity of the State Government or due to both working together. Low fiscal priority (ratio of expenditure category to aggregate expenditure) would be attached to a particular sector if it was below the national average while low fiscal capacity would be reflected if the State's per capita expenditure was below the national average even after having a fiscal priority that was more than or equal to the national average. **Table 1.7** analyses the fiscal priority and fiscal capacity of the State Government with regard to development expenditure, social sector expenditure and capital expenditure during the current year.

Table-1.7: Fiscal Priority and Fiscal Capacity of the State in 2005-06 and 2008-09

Fiscal Priority of the State	**AE/GSDP**	**DE/AE**	**SSE/AE**	**CE/AE**
All States/National Average* (Ratio) 2005-06	**19.50**	**61.44**	**30.41**	**14.13**
Tamil Nadu's Average (Ratio) 2005-06	17.88	59.45	33.52	10.93
All States/National Average* (Ratio) 2008-09	**19.16**	**67.68**	**33.90**	**16.87**
Tamil Nadu Average (Ratio)* 2008-09	19.32	65.22	34.80	13.89
Fiscal Capacity of the State	**DE#**	**SSE**	**CE**	
All States Average per capita expenditure 2005-06	**3,010**	**1,490**	**692**	
Tamil Nadu's per capita expenditure (Amount in Rs) in 2005-06	3,404	1,919	626	
Adjusted per capita** expenditure (Amount in Rs) in 2005-06	3,838	NR	883	
All States' Average per capita expenditure 2008-09	**5,030**	**2,520**	**1,254**	
Tamil Nadu's per capita expenditure (Amount in Rs) in 2008-09	6,446	3,440	1,373	
Adjusted per capita** expenditure (Amount in Rs) in 2008-09	6,688	NR	1668	

* As percentage of GSDP.
** Calculated as per the methodology explained in the Appendix 1.2.
AE: Aggregate Expenditure DE: Development Expenditure SSE: Social Sector Expenditure.
CE: Capital Expenditure. NR: No adjustment required since the State is giving adequate fiscal priority
Population of Tamil Nadu: 6.48 crore in 2005-06 and 6.63 crore in 2008-09.
Development Expenditure includes Development Revenue Expenditure, Development Capital Expenditure and Loans and Advances disbursed.
Source : (1) For GSDP, the information was collected from the State's Directorate of Economics and Statistics (2) Population figures were taken from Projection 2001-2026 of the Registrar General & Census Commissioner, India (Website: http://www.censusindia.gov.in) Population = Average of projected population for 2005 and 2006.
Data for Arunachal Pradesh has not been included in All States average and (3) Expenditure figures are from the Finance Accounts of Government of Tamil Nadu.

Table 1.7 compares the fiscal priority given to different categories of expenditure and the fiscal capacity of Tamil Nadu in 2005-06 (the first year of the Award Period of the TFC) and 2008-09.

Fiscal Priority

In 2005-06, the Tamil Nadu Government spent relatively less as a proportion of GSDP compared to the all States' average. In the current year, the Government spent relatively higher as a proportion of GSDP as the AE/GSDP ratio of the State at 19.32 *per cent* was higher than the all States' average of 19.16 *per cent*. However, the relatively low fiscal priority given to DE in 2005-06 continues even during the current year as the State's DE/AE ratio of 65.22 *per cent* during 2008-09 was lower than the all State's DE/AE ratio of 67.68 *per cent*. Similarly, the priority given to CE continues to be relatively lower in comparison with the all States' average as the CE/AE ratios of the State at 10.93 and 13.89 *per cent* during 2005-06 and 2008-09 respectively were lower than the all States' average ratios of 14.13 and 16.87 *per cent* in these years. The priority given to SSE in the State was adequate as the State's SSE/AE ratio of 34.80 *per cent* was higher than the all States average ratio of 33.90 *per cent* in 2008-09. This indicates that even though the aggregate spending of the State as a proportion of GSDP has increased in comparison with the all States' average during the Award Period, there is no marked departure in the relative priorities accorded by the Government to DE, SSE and CE. The priority given to DE and CE continue to lag behind the all States' average even as the SSE continues to receive higher priority. In other words, the relative increase in aggregate expenditure has not really helped the Economic Sector and in asset formation.

Fiscal Capacity

In 2005-06, the State's per capita DE of Rs 3,404 and SSE of Rs 1,919 were higher than the all States' average Rs 3,010 and Rs 1,490 respectively, whereas the State's per capita expenditure of Rs 626 on CE was below the all States' average of Rs 692. However, during 2008-09, the State's per capita expenditure on CE also surpassed the all States' average. The State's per capita DE of Rs 6,446, SSE of Rs 3,440 and the CE of Rs 1,373 were higher than the all States' average Rs 5,030, Rs 2,520 and Rs 1,254.

Despite the relatively low fiscal priority given to DE and CE by the State Government, the per capita DE and CE were higher than the national average. This means that the absorptive capacity [7] in the State is relatively high and that effective systems are in place to benefit the people. Considering the good absorptive capacity, had the Government spent as much on DE and CE as the national average, the adjusted per capita expenditure on DE and CE during

[7] Absorptive capacity in this case refers to the ability of a State to implement a developmental scheme in such a way that with the given resources, there is maximum benefit to the people. This is usually achieved when the designs of schemes are well planned with careful risk mitigation strategies in place; administrative costs are low; operation, maintenance, monitoring and control mechanisms are in place etc so that the State is able to effectively achieve targeted outcomes.

2008-09 (calculated as per the methodology given in **Appendix 1.2**) would have been even higher at Rs 6,688 and Rs 1,668 respectively.

1.5.2 Efficiency of Expenditure Use

In view of the importance of public expenditure on development heads from the point of view of social and economic development, it is important for the State Governments to take appropriate expenditure rationalisation measures and lay emphasis on provision of core public and merit goods[8]. Apart from improving the allocation towards development expenditure[9], particularly in view of the fiscal space being created on account of decline in debt servicing in recent years, the efficiency of expenditure use is also reflected by the ratio of capital expenditure to total expenditure (and/or GSDP) and the proportion of revenue expenditure on operation and maintenance of the existing Social and Economic Services. The higher the ratio of these components to the total expenditure (and/or GSDP), the better would be the quality of expenditure. While **Table 1.8** presents the trends in development expenditure relative to the aggregate expenditure of the State during 2004-09, **Table 1.9** provides the details of capital expenditure and the components of revenue expenditure incurred on the maintenance of the selected Social and Economic Services during 2007-08 and 2008-09.

Table 1.8: Development Expenditure

(Rupees in crore)

Components of Development Expenditure	2004-05	2005-06	2006-07	2007-08	2008-09
Development Expenditure (a to c)	20,411 (58.6)	22,058 (59.4)	28,835 (62.1)	32,464 (62.2)	42,736 (65.2)
a. Development Revenue Expenditure	15,137 (43.5)	17,089 (46.0)	20,823 (44.8)	23,497 (45.0)	31,032 (47.4)
b. Development Capital Expenditure	4,188 (12.0)	3,929 (10.6)	5,758 (12.4)	7,185 (13.8)	8,874 (13.5)
c. Development Loans and Advances	1,086 (3.1)	1,040 (2.8)	2,254 (4.9)	1,718 (3.3)	2,761 (4.2)

(Source: Finance Accounts of Government of Tamil Nadu)
Figures in parentheses indicate percentage of aggregate expenditure

[8] Core public goods are goods which all citizens enjoy in common in the sense that each individual's consumption of such a good leads to no subtractions from any other individual's consumption of that good, e.g. enforcement of law and order, security and protection of rights; pollution free air and other environmental goods, road infrastructure etc. Merit goods are commodities that the public sector provides free or at subsidized rates because an individual or society should have them on the basis of some concept of need, rather than the ability and willingness to pay the Government and therefore wishes to encourage their consumption. Examples of such goods include the provision of free or subsidized food for the poor to support nutrition, delivery of health services to improve quality of life and reduce morbidity, providing basic education to all, drinking water and sanitation etc.

[9] The analysis of expenditure data is disaggregated into development and non-development expenditure. All expenditure relating to Revenue Account, Capital Outlay and Loans and Advances is categorized into Social Services, Economic Services and General Services. Broadly, the Social and Economic Services constitute development expenditure, while expenditure on General Services is treated as non-development expenditure.

Table 1.9: Efficiency of Expenditure Use in Selected Social and Economic Services

(Percentage)

Social/Economic Infrastructure	2007-08		2008-09	
	Ratio of CE to TE	Ratio of S&W to RE	Ratio of CE to TE	Ratio of S&W to RE
Social Services (SS)				
General Education	3.14	81.21	1.12	85.55
Health and Family Welfare	5.23	70.24	7.78	71.57
WS, Sanitation, & HUD	34.15	2.02	21.82	1.29
Total (SS)	**7.19**	**50.63**	**6.06**	**50.14**
Economic Services (ES)				
Agri & Allied Activities	35.98	32.14	27.54	30.99
Irrigation and Flood Control	36.74	24.41	43.38	28.56
Power & Energy	29.43	0.07	47.49	0.08
Transport	70.53	10.98	71.09	10.78
Total (ES)	**39.22**	**15.06**	**39.14**	**15.57**
Total (SS+ES)	**22.13**	**38.87**	**20.76**	**39.37**

(Source: Finance Accounts of Government of Tamil Nadu)

TE: Total expenditure on the Sector/Service concerned; CE: Capital Expenditure;
RE: Revenue Expenditure; S&W: Salaries and Wages.

Development expenditure, in real terms and as a percentage of the aggregate expenditure of the State, was increasing continuously during 2004-09.

However, the development capital expenditure as a percentage of aggregate expenditure of the State, declined marginally from the level of 13.8 in 2007-08 to 13.5 in 2008-09. As a percentage of development expenditure, it came down from 22.13 in 2007-08 to 20.76 in 2008-09.

Expenditure on Social Services

- Though the capital expenditure on Social Services had increased from Rs 1,239 crore in 2007-08 to Rs 1,434 crore in 2008-09 (15.74 *per cent)* in real terms, as a percentage of aggregate expenditure of the State, it had declined from 2.37 in 2007-08 to 2.19 in 2008-09. As a percentage of total expenditure on Social Services, it declined from 7.19 in 2007-08 to 6.06 in 2008-09.

- The capital expenditure on General Education fell steeply from Rs 222 crore in 2007-08 to Rs 99.77 crore in 2008-09. It fell from 3.14 *per cent* of the total expenditure on General Education in 2007-08 to 1.12 *per cent* in 2008-09. This indicated that Government's spending on infrastructural requirement of General Education was not keeping pace with the overall development expenditure.

- Expenditure on salaries and wages for General Education consumed a bulk of the revenue expenditure. It increased from Rs 5,559 crore in 2007-08 to Rs 7,532 crore in 2008-09 (35.5 per *cent).* As a percentage of revenue expenditure on General Education, it increased from 81.21 in 2007-08 to 85.5 in 2008-09.

Expenditure on Economic Services

- Though the capital expenditure on Economic Services had increased from Rs 5,946 crore in 2007-08 to Rs.7440 crore (25 *per cent)* in 2008-09, as a percentage of total expenditure on Economic Services, it had declined marginally from 39.22 in 2007-08 to 39.14 in 2008-09.

- The capital expenditure on Agriculture and Allied Activities declined marginally from Rs 1,576 crore in 2007-08 to Rs 1,484 crore in 2008-09. As a percentage of total expenditure on Agriculture and Allied Activities, it declined from 35.98 in 2007-08 to 27.54 in 2008-09.

- Expenditure on salaries and wages for Economic Services increased from Rs 1,170 crore in 2007-08 to Rs 1,504 crore in 2008-09 (28.54 *per cent).* As a percentage of revenue expenditure on Economic Services, it increased marginally from 15.06 in 2007-08 to 15.57 in 2008-09.

1.6 Financial Analysis of Government Expenditure and Investments

In the post-Fiscal Responsibility and Budget Management (FRBM) framework, the State is expected to keep its fiscal deficit (and borrowings) not only at low levels but also meet its capital expenditure/investment (including loans and advances) requirements. In addition, in a transition to complete dependence on market-based resources, the State Government needs to initiate measures to earn adequate returns on its investments, recover its cost of borrowed funds rather than bearing the same on its budget in the form of implicit subsidies and take requisite steps to infuse transparency in financial operations. This section presents a broad financial analysis of investments and other capital expenditure undertaken by the Government during the current year vis-à-vis the previous years.

1.6.1 Financial Results of Irrigation Works

Ensuring the commercial viability of irrigation projects through realization of adequate revenue by way of user charges has been a policy of Government of India. The TFC prescribed recovery of 80 *per cent* of the maintenance expenditure on major, medium and minor irrigation projects by way of non-tax revenue from them. Audit, however, found that the revenue from irrigation projects (Rs 33 crore) during 2008-09 was only 4.71 *per cent* of the maintenance expenditure.

Statement 3 of Finance Accounts depicts the financial results of five major and 47 medium irrigation projects. The revenue realized from these projects during 2007-08 was Rs 11.87 crore. After meeting the working and maintenance expenditure (Rs 128.87 crore) and interest charges (Rs 145.14 crore), these 52 projects suffered a net loss of Rs 262.53 crore during 2007-08.

1.6.2 Incomplete projects

The department-wise information pertaining to incomplete projects as on 31 March 2009 is given in **Table 1.10**.

Table 1.10: Department-wise Profile of Incomplete Projects

(Rupees in crore)

Department	No. of Incomplete Projects*	Initial Budgeted Cost	Revised Total Cost of Projects**	Cost Over-runs	Cumulative actual expenditure as on 31.3.2009
Buildings	9	4,123.74	13,374.75	9,251.01	1,765.76
Roads and Bridges	46	37,462.95	49,371.13	11,908.18	27,948.55
Irrigation (Water Resources) and Flood Control	1	700.00	1,350.00	650.00	1,202.00
Total	**56**	**42,286.69**	**64,095.88**	**21,809.19**	**30,916.31**

(Source: Finance Accounts of Government of Tamil Nadu)

* Only those projects which were scheduled to be completed before 31 March 2009 were included

** Indicates the revised total cost of the projects as per the last revision by the State Government as of March 2009.

- Failure to complete projects on time leads to escalation of project costs and delays the accrual of the projects' benefits to the society at large. Further, delays also result in postponement of revenue realization from projects.

- Analysis of the reasons for delay in completion of 21 of the above projects disclosed that nine projects were held up due to problems in land acquisition, three projects were delayed due to non-completion of sub-works, five projects were delayed due to contractor's faults and four projects were delayed due to other reasons like rain, etc.

1.6.3 Investment and returns

As of 31 March 2009, Government had invested Rs 6,471 crore in statutory corporations, rural banks, joint stock companies and co-operatives **(Table 1.11).** The average return on these investments was 0.5 *per cent* while Government paid an average interest rate of 7.7 *per cent* on its borrowings during 2008-2009.

Table 1.11: Return on Investment

Investment/Return/Cost of Borrowings	2004-05	2005-06	2006-07	2007-08	2008-09
Investment at the end of the year (Rs in crore)	2,557.71	2,744.60	4,278.43	6,230.40	6,471.22
Return (Rs in crore)	24.25	20.92	26.32	22.10	35.59
Return (*per cent*)	0.9	0.8	0.6	0.4	0.5
Average rate of interest on Government borrowing *(per cent)*	9.1	7.8	8.6	8.9	7.7
Difference between interest rate and return *(per cent)*	8.2	7.0	8.0	8.5	7.2

(Source: Finance Accounts of Government of Tamil Nadu)

- As of March 2009, Government has invested in two statutory corporations (Rs 714 crore), 68 Government companies (Rs 2,406 crore), six joint stock companies (Rs two crore) and 9,330 co-operatives (Rs 3,349 crore). During 2008-09, Government infused an additional capital of Rs 177 crore into seven ailing State Transport Undertakings, which had accumulated a total loss of Rs 3,688 crore. Other major investments made included Rs 67 crore on Chennai Metro Rail Corporation and Rs 25 crore on Arasu Cable Corporation.

1.6.4 Loans and advances by State Government

In addition to investments in co-operative societies, corporations and companies, Government has also been providing loans and advances to many of these institutions/ organizations. **Table 1.12** presents the outstanding loans and advances as on 31 March 2009 and interest receipts vis-à-vis interest payments during the last three years.

Table 1.12: Average Interest Received on Loans Advanced by the State Government

(Rupees in crore)

Quantum of Loans/Interest Receipts/ Cost of Borrowings	2006-07	2007-08	2008-09
Opening Balance	5,497	6,149	6,918
Amount advanced during the year	2,254	1,782	2,830
Amount repaid during the year	1,602	1,013	1,934
Closing Balance	6,149	6,918	7,814
Net addition	652	769	896
Interest Receipts	251	72	205
Interest receipts as percentage of outstanding Loans and advances	4.3	1.1	2.8
Interest payments as percentage of outstanding fiscal liabilities of the State Government.	8.6	8.9	7.7
Difference between interest payments and interest receipts (*per cent*)	(-) 4.3	(-) 7.8	(-) 4.9

(Source: Finance Accounts of Government of Tamil Nadu)

- The quantum of loans advanced increased from Rs 1,782 crore in 2007-08 to Rs 2,830 crore in 2008-09, an increase of 58.8 *per cent*. Repayments also increased from Rs 1,013 crore in 2007-08 to Rs 1,934 crore in 2008-09 (90.9 *per cent*), resulting in increase in the outstanding balance from Rs 6,918 crore in 2007-08 to Rs 7,814 crore in 2008-09. The difference between the interest payments and interest receipts decreased from 7.8 *per cent* in 2007-08 to 4.9 *per cent* in 2008-09.

- The major recipients of loans and advances were the (i) Social Sector-water supply, sanitation, housing and urban development (Rs 811 crore), out of which Rs 500 crore was advanced to Metro Rail project in Chennai and the (ii) Economic Sector - (a) Agriculture and Allied Services (Rs 1,427 crore), out of which Rs 1,150 crore was advanced for food storage and warehousing to statutory corporations, boards and Government companies, (b) Industries and Mines (Rs 228 crore) and (iii) Transport Sector (Rs 250 crore), out of which Rs 165 crore was given as short term loans to State transport undertakings.

1.6.5 Cash Balances and Investment of Cash Balances

Table 1.13 depicts the cash balances and investments made by the State Government out of cash balances during the year.

Table 1.13: Cash Balances and Investment of Cash Balances

(Rs in crore)

Particulars	As on 1 April 2008	As on 31 March 2009	Increase (+)/ Decrease (-)
Cash Balances	12,172	16,229	4,057
Investments from Cash Balances (a to d)			
(a) GOI Treasury Bills	11,136	14,060	2,923
(b) GOI Securities	1,826	2,280	455
(c) Other Securities, if any specify	(-) 815	(-) 137	678
(d) Others - (Treasury/departmental cash balance, remittance etc.)	25	26	1
Funds-wise Break-up of Investment from Earmarked balances (a to c)			
(a) Sinking Fund	1,826	2,273	447
(b) Famine Relief Fund	-	-	-
(c) Infrastructure Development Fund	846	142	(-) 704
Interest realised	613	589	(-) 24

(Source: Finance Accounts of Government of Tamil Nadu)

- The cash balance as on 31 March 2009 increased by Rs 4,057 crore over the previous year despite decrease of Rs 257 crore in the balances of earmarked funds.

- The interest realised during the year on investment of cash balances was less by Rs 24 crore as compared to the previous year.

The efficiency of handling of cash balances by the State can also be assessed by monitoring the trends in the monthly daily average of cash balances held by the State to meet its normal banking transactions. **Table 1.14** presents the trends in monthly average daily cash balance and investments of cash balance in 14 day Treasury Bills and in Auction Treasury Bills for the last three years (2006-09).

Table 1.14: Trends in Monthly Average Daily Cash Balances and Investments in Auction Treasury Bills

(Rs in crore)

Month	Monthly Average Daily Cash Balances (available for investment)			Investment in 14 day Treasury Bills			Investment in Auction Treasury Bills		
	2006-07	2007-08	2008-09	2006-07	2007-08	2008-09	2006-07	2007-08	2008-09
April	6,717.30	7,234.25	9,243.21	2,411.17	2,328.41	4,222.07	4,306.13	4,905.84	5,021.14
May	6,820.03	6,686.40	9,395.68	2,529.41	1,909.06	3,691.70	4,290.62	4,777.34	5,703.98
June	7,915.72	6,961.87	10,422.19	3,677.47	2,136.38	3,101.51	4,238.25	4,825.49	7,320.68
July	8,665.23	6,645.77	10,528.86	4,463.84	1,638.14	2,274.53	4,201.39	5,007.63	8,254.33
August	9,047.25	7,152.88	10,609.99	4,845.86	1,901.25	1,877.81	4,201.39	5,251.63	8,732.18
September	9,377.19	8,021.84	10,618.88	4,934.13	2,530.43	1,981.38	4,443.06	5,491.41	8,637.50
October	9,645.53	7,916.33	9,982.96	4,719.06	2,433.45	2,279.61	4,926.47	5,482.88	7,703.35
November	9,837.69	7,417.89	9,693.44	4,669.91	1,941.61	1,975.38	5,167.78	5,476.28	7,718.06
December	9,551.38	7,699.14	11,265.53	4,381.62	2,223.93	4,549.58	5,169.76	5,475.21	6,715.95
January	9,549.90	8,809.22	11,341.49	4,377.71	3,334.58	6,248.87	5,172.19	5,474.64	5,092.62
February	10,113.25	10,273.40	10,523.57	4,942.12	4,787.83	6,941.11	5,171.13	5,485.57	3,582.46
March	9,269.28	10,650.55	12,282.90	4,233.17	5,391.64	9,965.69	5,036.11	5,258.91	2,317.21

(Source: Finance Department, Government of Tamil Nadu)

- Governments invest their cash balances including the balances of earmarked funds in GOI Treasury Bills, GOI securities and other instruments. Investments in 90 day/180 day/360 day Auction Treasury Bills fetch higher rates of interest than investments in 14 day Treasury Bills. During 2006-09, the monthly daily average balances held in 14 day Treasury Bills exceeded Rs 2,000 crore in 29 out of the 36 months and exceeded Rs 4,000 crore in 16 months. Keeping huge balances in 14 day Treasury Bills pointed to the inadequacies in the Government's fund flow management system.

1.7 Assets and Liabilities

1.7.1 Growth and Composition of Assets and Liabilities

In the existing Government accounting system, comprehensive accounting of fixed assets like land and buildings owned by the Government is not done. However, the Government accounts do capture the financial liabilities of the Government and the assets created out of the expenditure incurred. **Appendix 1.4** gives an abstract of such liabilities and assets as on 31 March 2009, compared with the corresponding position on 31 March 2008. While the liabilities in this Appendix consist mainly of internal borrowings, loans and advances from GOI, receipts from the Public Account and Reserve Funds, the assets comprise mainly the capital outlay, loans and advances given by the State Government and cash balances.

The Tamil Nadu Fiscal Responsibility Act, 2003 defines the total liability of the State as ‘the liabilities under the Consolidated Fund of the State and the Public Account of the State’, which include loans and advances from the Central Government, open market borrowings, loans from financial institutions, Provident Fund balances of Government employees, Reserve funds, Deposits etc.

1.7.2 Fiscal Liabilities

The trends in outstanding fiscal liabilities of the State are presented in **Appendix 1.3**. However, the composition of fiscal liabilities during the current year vis-à-vis the previous year is presented in **Charts 1.10** and **1.11.**

Chart 1.10: Composition of Outstanding Fiscal Liabilities as on 01.04.2008 (Rs in crore)

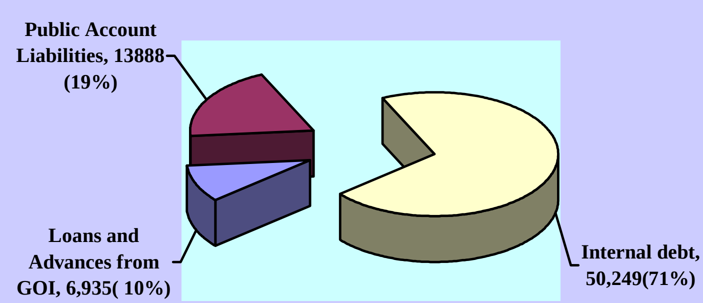
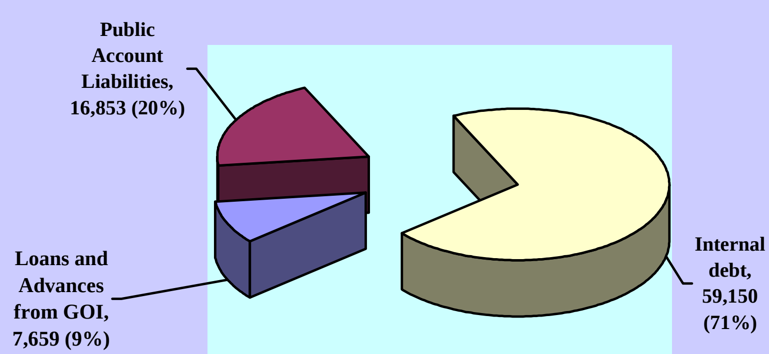


Chart 1.11: Composition of Outstanding Fiscal Liabilities as on 01.04.2009 (Rs in crore)



- The outstanding fiscal liabilities have shown a steady increase from Rs 55,144 crore at the end of 2004-05 to Rs 83,662 crore as at the end of 2008-09.

- The fiscal liabilities as at the end of 2008-09 represented 152 *per cent* of the revenue receipts during the year as against 149.6 *per cent* during 2007-08.

- Internal debts, at 71 *per cent* of the fiscal liabilities at the end of 2008-09, remained the same as that of the previous year. While the Public Account liabilities as a percentage of the fiscal liabilities increased from 19 *per cent* in 2007-08 to 20 *per cent* in 2008-09, the outstanding loans and advances from GOI decreased from 10 *per cent* to nine *per cent* of the fiscal liabilities during the same period.

1.7.3 Status of Guarantees – Contingent liabilities

Guarantees are liabilities contingent on the Consolidated Fund of the State in cases of defaults by borrowers for whom the guarantees have been extended.

As per Statement 6 of the Finance Accounts, the maximum amount for which guarantees were given by the State and the outstanding guarantees for the last three years is given in **Table 1.15.**

Table 1.15: Guarantees given by the Government of Tamil Nadu

(Rupees in crore)

Guarantees	2006-07	2007-08	2008-09
Maximum amount guaranteed	15,942	20,090	11,062
Outstanding amount of guarantees	4,038	5,410	4,633
Percentage of maximum amount guaranteed to total Revenue receipts	39	42	20
Criteria as per the TN Fiscal Responsibility Act, 2003	Cent *per cent* revenue receipts of previous year or 10 *per cent* of GSDP, whichever is lower.		

(Source: Finance Accounts of Government of Tamil Nadu)

- Government has constituted (March 2003) a "Guarantees Redemption Fund" for discharge of invoked guarantees. An amount of Rs 10 crore was credited to the Fund during 2008-09, but no expenditure was met. The balance in the Fund as of March 2009 was Rs 109 crore.

- The maximum amount guaranteed was well within the stipulations of the Tamil Nadu Fiscal Responsibility, Act 2003. As a percentage of revenue receipts, it came down from 42 in 2007-08 to 20 in 2008-09. As a percentage of GSDP, it came down from 7.19 in 2007-08 to 3.26 in 2008-09.

1.7.4 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 **Appendix 1.4**, the State guarantees loans availed of by Government companies/corporations. These companies/corporations borrow funds from the market/financial institutions for implementation of various State Plan programmes projected outside the State budget. Although the State Government projects that funds for these programmes would be met out of the resources mobilized by these companies/corporations outside the State budget, in reality, the borrowings of many of these concerns are repaid by the Government and ultimately turn out to be liabilities of the State Government termed as 'off-budget borrowings'. Though off-budget borrowings are not permissible under Article 293 (3), the State continues to undertake such off-budget borrowings as per the data furnished by the following Special Purpose Vehicles (SPVs). **Table 1.16** gives the off-budget borrowings by the State as of 31 March 2009.

Table 1.16: Off-Budget Borrowings

(Rupees in crore)

Sector	Name of SPV	Amount borrowed	Amount outstanding as of 31.3.2009
Social Services	Tamil Nadu Water Supply and Drainage Board	397	124
	Tamil Nadu Cooperative Housing Federation Ltd.	3,156	738

(Source: Information furnished by SPVs. Not a complete list of off budget borrowings)

The off-budget borrowings given above add to the fiscal liability of the State, but are not indicated as such in the Government Accounts as they are not captured in the Finance Accounts of the State.

1.8 Debt Sustainability

Apart from the magnitude of debt of the State Government, it is important to analyze the various indicators that determine the debt sustainability[10] of the State. This section assesses the sustainability of debt of the State Government in terms of debt stabilization[11]; sufficiency of non-debt receipts[12]; net

[10] Debt sustainability is defined as the ability of the State to maintain a constant debt-GDP ratio over a period of time and also embodies the concern about the ability to service its debt. Sustainability of debt, therefore, also refers to the sufficiency of liquid assets to meet current or committed obligations and the capacity to keep a balance between the costs of additional borrowings and the returns from such borrowings. It means that the rise in fiscal deficit should match the increase in the capacity to service the debts.

[11] A necessary condition for stability states that if the rate of growth of the economy exceeds the interest rate or cost of public borrowings, the debt-GDP ratio is likely to be stable provided primary balances are either zero, positive or moderately negative. Given the rate spread (GSDP growth rate – interest rate) and the quantum spread (Debt X rate spread), the debt sustainability condition states that if the quantum spread together with the primary deficit is zero, the debt-GSDP ratio would be constant or the debt would stabilize eventually. On the other hand, if the primary deficit together with the quantum spread turns out to be negative, the debt-GSDP ratio would be rising. In case it is positive, the debt-GSDP ratio would eventually be falling.

[12] Adequacy of incremental non-debt receipts of the State to cover incremental interest liabilities and incremental primary expenditure. Debt sustainability could be significantly facilitated if incremental non-debt receipts could meet the incremental interest burden and the incremental primary expenditure.

availability of borrowed funds[13]; burden of interest payments (measured by interest payments to revenue receipts ratio) and the maturity profile of State Government securities. **Table 1.17** analyzes the debt sustainability of the State according to these indicators for a period of three years beginning from 2006-07.

Table 1.17: Debt Sustainability: Indicators and Trends

(Rupees in crore)

Indicators of Debt Sustainability	2006-07	2007-08	2008-09
Debt Stabilization (Quantum Spread + Primary Deficit)	2,528	5,391	7,195
Sufficiency of Non-debt Receipts (Resource Gap)	(-) 1,705	(+) 270	(-) 4,862
Net Availability of Borrowed Funds	(-) 1,496	(-) 1,334	6,627
Burden of Interest Payments (IP/RR Ratio)	13.5	12.8	10.8
Maturity Profile of internal debts & GOI loans (in years)			
0 – 1		1,359(2.4)	1,629(2.4)
1 – 3		3,967(6.9)	5,148(7.7)
3 – 5		6,687(11.7)	7,632(11.4)
5 – 7		10,295(18)	7,870(11.8)
7 and above		34,875(61)	44,531(66.7)

(Source: Finance Accounts of Government of Tamil Nadu)
Figures in brackets represent percentage of total outstanding internal debts and GOI loans

- As may be seen from the above, debt stabilisation does not seem to be a major concern, indicating a falling debt-GSDP ratio.

- The net availability of borrowed funds during 2008-09 was Rs 6,627 crore, an increase of Rs 7,961 crore over the negative figure of Rs 1,334 crore during 2007-08. This was a result of increase in receipts under internal debts from Rs 6,868 crore in 2007-08 to Rs 10,798 crore in 2008-09 and simultaneous decrease in expenditure on repayment of internal debts from Rs 3,231 crore in 2007-08 to Rs 1,897 crore in 2008-09. Further, the interest payments, which were on an increasing trend during 2004-08 declined marginally from Rs 6,086 crore in 2007-08 to Rs 5,963 crore in 2008-09.

- Despite positive indicators in terms of debt stabilisation and increased net availability of borrowed funds, the negative resource gap (Rs 4,862 crore) was a matter of concern. This was a result of insufficiency of the incremental non-debt receipts (Rs 8,443 crore) to meet the incremental primary expenditure (Rs 13,428 crore). The high incremental primary expenditure was mainly due to an increase of Rs 10,738 crore under primary revenue expenditure.

- The maturity profile of the State’s debt indicates a year-on-year increase in its repayment burden.

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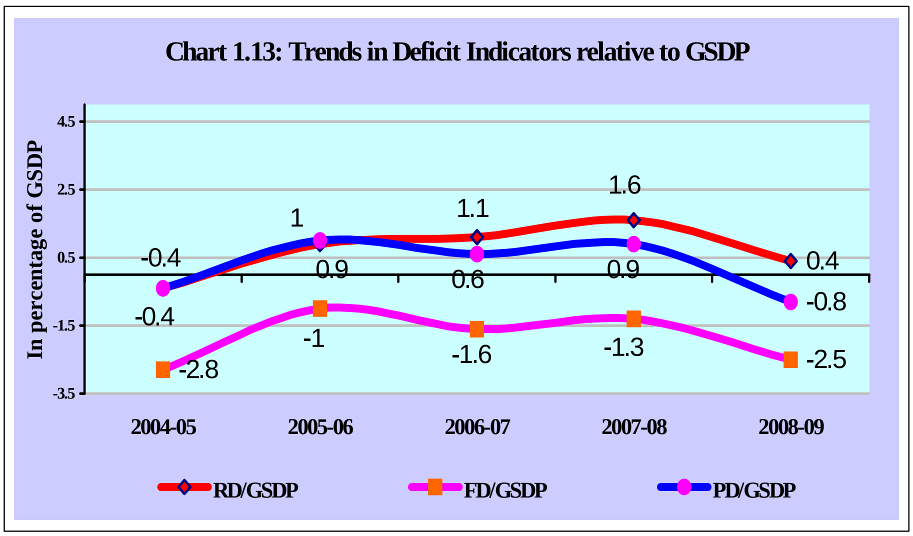
[13] Defined as the ratio of the debt redemption (principal + interest payments) to total debt receipts and indicates the extent to which the debt receipts are used in debt redemption, indicating the net availability of borrowed funds.

1.9 Fiscal Imbalances

Three key fiscal parameters - revenue, fiscal and primary deficits - indicate the extent of overall fiscal imbalances in the finances of the State Government during a specified period. The deficit in the Government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the Government. Further, the ways in which the deficit is financed and the resources raised are applied are important pointers to its fiscal health. This section presents trends, nature, magnitude and the manner of financing these deficits and also the assessment of actual levels of revenue and fiscal deficits vis-à-vis targets set under FRBM Act/Rules for the financial year 2008-09.

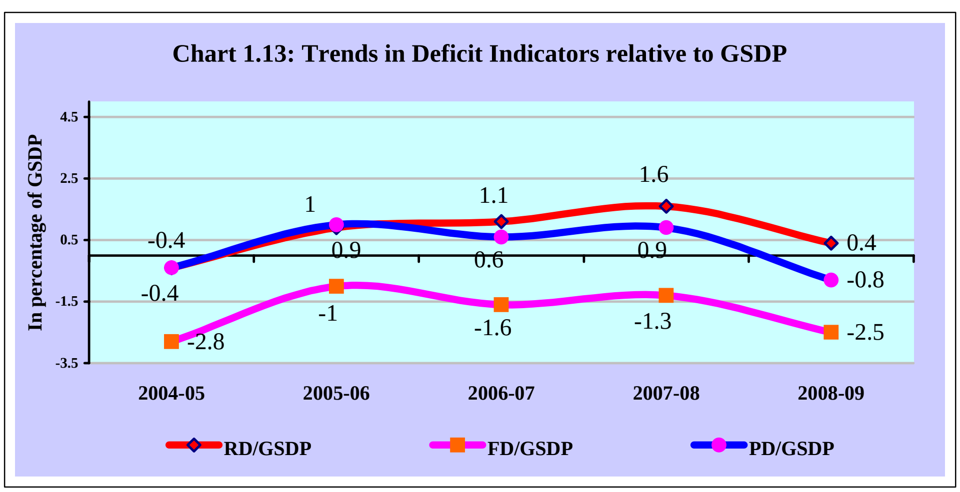
1.9.1 Trends in Deficits

Charts 1.12 and **1.13** presents the trends in deficit indicators over the period 2004-09.



- The primary surplus, which prevailed during the last three continuous years, turned negative with a deficit of Rs 2,585 crore.

- The fiscal deficit increased by Rs 4,862 crore over 2007-08.



1.9.2 Composition of Fiscal Deficit and its Financing Pattern

The financing pattern of the fiscal deficit has undergone a compositional shift as reflected in **Table 1.18.**

Table1.18: Components of Fiscal Deficit and its Financing Pattern

(Rupees in crore)

	Particulars	2004-05	2005-06	2006-07	2007-08	2008-09
Decomposition of Fiscal Deficit		**(-) 5,570**	**(-) 2,251**	**(-) 3,956**	**(-) 3,686**	**(-) 8,548**
1	Revenue Surplus/Deficit (-)	(-) 703	1,951	2,648	4,545	1,452
2	Net Capital Expenditure	4,564	4,054	5,952	7,462	9,104
3	Net Loans and Advances	303	148	652	769	896
Financing Pattern of Fiscal Deficit*						
1	Market Borrowings	2,249	1,214	1,372	4,127	8,792
2	Loans from GOI	(-) 2,887	139	(-) 213	469	724
3	Special Securities issued to National Small Savings Fund	5,864	6,094	3,898	(-) 782	(-) 173
4	Loans from Financial Institutions	(-) 277	(-) 528	(-) 2,600	287	282
5	Small Savings, PF etc	(-) 428	328	256	383	578
6	Deposits and Advances	1383	(-) 7	1130	138	1576
7	Suspense and Miscellaneous	426	1086	963	162	194
8	Remittances	(-) 48	138	52	(-) 130	78
9	Reserve Funds	(-) 204	(-) 74	168	130	553
10	Contingency Fund	-	(-) 16	16	-	-
	Total	**6,078**	**8,374**	**5,042**	**4,784**	**12,604**
11	Overall Surplus/Deficit (-) (Cash Balance)	508	6,123	1,086	1,098	4,056

(Source: Finance Accounts of Government of Tamil Nadu)

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

- The fiscal deficit increased from Rs 3,686 crore in 2007-08 to Rs 8,548 crore in 2008-09 (132 *per cent)* due to decrease in the revenue surplus from Rs 4,545 crore in 2007-08 to Rs 1,452 in 2008-09 (68 *per cent)* and increase in the net capital expenditure and net loans and advances from Rs 8,231 crore in 2007-08 to Rs 10,000 crore in 2008-09 (21 *per cent).*

- The State is increasingly banking on market borrowings for financing its fiscal deficit. The net market borrowings during 2008-09 increased to Rs 8,792 crore from Rs 4,127 crore during 2007-08.

- Deposits and Advances increased by Rs 1,438 crore over 2007-08.

- The overall surplus of Rs 4,056 crore, a substantial increase from Rs 1,086 crore in 2006-07 and Rs 1,098 crore in 2007-08, indicated that the borrowings were in excess of requirement. This contributed to a substantial increase in the monthly average daily cash balance as commented in Para 1.6.5 earlier.

1.9.3 Quality of Deficit/Surplus

The ratio of revenue deficit to fiscal deficit and the decomposition of primary deficit into primary revenue deficit and capital expenditure (including loans and advances) would indicate the quality of deficit in the States' finances. The ratio of revenue deficit to fiscal deficit indicates the extent to which borrowed funds were used for current consumption. The bifurcation of the primary deficit **(Table 1.19)** would indicate the extent to which the deficit had been on account of enhancement in capital expenditure, which may have been desirable to improve the productive capacity of the State's economy.

Table 1.19: 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)**
2004-05	29,235	24,400	4,564	1,086	30,050	4,835	-815
2005-06	34,852	27,450	4,054	1,040	32,544	7,402	2,308
2006-07	42,515	32,759	5,952	2,254	40,965	9,756	1,550
2007-08	48,533	36,889	7,462	1,782	46,133	11,644	2,400
2008-09	56,976	47,627	9,104	2,830	59,561	9,349	-2,585

(Source: Finance Accounts of Government of Tamil Nadu)

- During the period 2004-05 to 2008-09, non-debt receipts increased from Rs 29,235 crore to Rs 56,976 crore (94.8 *per cent)* against an increase of 94.18 *per cent* in primary revenue expenditure, 99.47 *per cent* in capital expenditure, 160.6 *per cent* in loans and advances and 98.2 *per cent* in primary expenditure.

- Capital expenditure as a percentage of primary expenditure marginally increased from 15.19 in 2004-05 to 15.28 in 2008-09. Loans and advances as a percentage of primary expenditure increased from 3.6 in 2004-05 to 4.7 in 2008-09.

- The adequacy of non-debt receipts to meet the primary expenditure led to the emergence of primary surplus during 2005-06 to 2007-08. However, the non-debt receipts were not enough to meet expenditure requirements during 2008-09, resulting in primary deficit. The primary revenue expenditure, capital expenditure and disbursement of loans and advances increased by 29 *per cent*, 22 *per cent* and 58.8 *per cent* respectively over the previous year.

1.9.4 State's Own Revenue and Deficit Correction

It is worthwhile to observe the extent to which deficit correction is achieved by the State on account of improvement in its own resources. This is an indicator of the durability of the corrections in deficit indicators. **Table 1.20** presents the changes in revenue receipts of the State and the corrections of the deficit during the last three years.

Table 1.20: Change in Revenue Receipts and Corrections of Deficit

(*Per cent* of GSDP)

Parameters	**2006-07**	**2007-08**	**2008-09**	
			BE	**Actual**
Revenue Receipts (a to d)	16.60	17.00	15.08	16.23
a. State's Own Tax Revenue	11.26	10.61	9.77	9.93
b. State's Own Non- tax Revenue	0.72	0.90	0.97	1.68
c. State's Share in Central Taxes and Duties	2.64	3.63	2.80	2.51
d. Grants-in-Aid	1.98	1.86	1.64	2.10
Revenue Expenditure	15.52	15.37	15.16	15.80
Revenue Deficit/Surplus	1.1	1.6	(-) 0.02	0.43
Fiscal Deficit/Surplus	(-) 1.6	(-) 1.3	(-) 2.89	(-) 2.52

(Source: Finance Accounts of Government of Tamil Nadu)

The State had met the stipulation of the Tamil Nadu Fiscal Responsibility Act, 2003 to eliminate the revenue deficit. The State had achieved revenue surplus from the year 2005-06 onwards. However, the margin of revenue surplus, which was Rs 4,545 crore in 2007-08 decreased to Rs 1,452 crore in 2008-09.

The percentage of revenue receipts to GSDP, which was 17 in 2007-08, came down to 16.23 in 2008-09. The excess of revenue receipts over revenue expenditure led to a revenue surplus of Rs 1,452 crore (0.43 *per cent* of GSDP) as against a deficit of Rs 9,792 crore (2.89 *per cent* of GSDP) envisaged in the budget.

The fiscal deficit at 2.5 *per cent* of GSDP during 2008-09, though within the statutory stipulation of three *per cent* of GSDP, increased from 1.3 *per cent* in 2007-08.

1.10 Conclusion

The State achieved the targets as laid down in the Tamil Nadu Fiscal Responsibility Act, 2003. However, the increasing trend in revenue surplus, witnessed during the last three years, reversed and the quantum of revenue surplus declined from Rs 4,545 crore in 2007-08 to Rs 1,452 crore during 2008-09 due to disproportionate growth of revenue expenditure (25 *per cent)* vis-à-vis revenue receipts (16 *per cent).* The State's own taxes are not keeping pace with its GSDP.

Committed expenditure consumed 65 *per cent* of the revenue receipts as against 59 *per cent* during 2007-08, mainly due to increase in salaries, pension and subsidies. Capital expenditure on asset creation, as a percentage of aggregate expenditure, stood at 13.89 as against the national average of 16.87.

The revenue from irrigation projects was too low to sustain them. Blocking of huge sums in incomplete projects delays and undermines the economic benefits realizable through them. Investments of the Government in statutory corporations, public sector companies and co-operatives continue to yield meagre returns.

The Government of Tamil Nadu has been giving due priority to the social sector. However, compared to the all States' average, there appears to be a need for greater priority to Economic Services and creation of productive assets through greater priority to capital expenditure.

Though the fall in the debt – GSDP ratio is a positive indication, the Government has not curtailed off-budget borrowings. Further, the increase in overall surplus (cash balance) from Rs 1,098 crore in 2007-08 to Rs 4,056 crore in 2008-09 indicated excessive and unplanned borrowings. The trend in cash balance investment shows untapped potential for better returns.

1.11 Recommendations

- Government may institute a mechanism for centralised monitoring of utilisation of funds released directly to State implementing agencies by the Government of India.
- Execution of large projects should be closely monitored to avoid blocking of funds in incomplete projects.
- Government needs to tone up its cash balance management system, ensure proper planning for borrowings and curtail off-budget borrowings.