

Executive Summary

Background

In February 2004, Government of Uttar Pradesh responded to the Twelfth Finance Commission's recommendation by legislating its "Fiscal Responsibilities and Budget Management Act" (FRBM) setting out a reform agenda through fiscal correction path in the medium term with the long-term goal of securing growth with stability for its economy. The State Government's commitment to carry forward these reforms is largely reflected in certain policy initiatives announced in the budgets subsequently. While the benefits of FRBM legislation have been realised to a great extent already, in terms of key fiscal indicators, the policy initiatives to augment its resources by implementing VAT, bringing new items in tax net and according priority to capital expenditure will go a long way in building up the much needed 'fiscal space' for promoting fiscal stability and improving quality of public expenditure.

C&AG's reports have been commenting upon the Government's finances since the FRBM legislation of 2004 and have since then published three reports. As these comments formed part of the civil audit report containing audit findings on compliance and performance audit, it was felt that the audit findings on State finances did not get proper attention of the stakeholders. In recognition of the need to bring State finances to centre-stage, it was thought appropriate to bring out a separate report on State Government finances to highlight these findings.

The report

Based on the audited accounts of the Government of Uttar Pradesh 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 1 is based on the audit of Finance Accounts and makes an assessment of Uttar Pradesh Government's fiscal position as on 31 March 2009. It provides an insight into trends in committed expenditure, borrowing pattern, besides a brief account of Central funds transferred directly to the State implementing agencies through off-budget route.

Chapter 2 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 3 is an inventory of Uttar Pradesh Government's compliance with various reporting requirements and financial rules. The report also has an appendage of additional data collected from several sources in support of the findings.

Audit findings and recommendations

Return to fiscal correction: Uttar Pradesh Government's fiscal gains of 2007-08 showed deterioration in the year 2008-09. The Sixth Pay Commission award also put pressure on the committed expenditure. The fiscal position will be strengthened through concerted efforts in tax compliance focusing on regaining tax arrears, recovery of the cost of maintenance of the irrigation projects, timely completion of projects of Irrigation and Public Works departments and making these projects a source of revenue, cutting non-productive expenditure and discouraging market borrowings (Paragraph 1.9.1).

Greater priority to public expenditure: In comparison to the National average, although the Government gave adequate fiscal priority to the capital expenditure during 2008-09, *per capita* capital expenditure was below the National average. Greater priority needs to be given to development and social sector expenditure to bring UP at par with other States. *Per capita* expenditure in UP on developmental and social sector expenditure is lower than the all States average. In view of this, the Government may consider re-prioritising its public expenditure (Paragraph 1.5.1).

Review of Government investments: The average return on Government's investments in Statutory corporations, Government companies, joint stock companies and co-operatives was 0.007 *per cent* in the last three years, whereas its average interest outgo was 6.49 *per cent* (Paragraph 1.6.3) on its borrowings during the corresponding period. This is clearly an unsustainable proposition. The State Government should, therefore, seek better value for money in investments. Otherwise, high-cost of borrowed funds invested in projects with low financial return will continue to strain the economy. Projects which are justified on account of low financial but high socio-economic return may be identified and prioritised with full justification for the high-cost borrowings. The working of State-owned public sector undertakings, incurring huge losses may be reviewed and appropriate decision for their closure or otherwise may be taken depending on their strategic value and revival potential.

Prudent cash management: The cost of holding surplus cash balances is high. In 2008-09, interest received on investment of cash balances in RBI's Treasury Bills was only 4.08 *per cent* while the Government borrowed at interest rate of 6.06 *per cent* (Paragraph 1.6.6). Proper debt management through advanced planning could minimise the need to hold large cash surpluses.

Debt sustainability: The Government of Uttar Pradesh should endeavour to achieve the

normative debt-GSDP ratio as specified in Fiscal Reform legislation so that the total liabilities at the end of the financial year 2018 do not exceed 25 per cent of the estimated GSDP (Paragraph 1.7.3). About 96 to 97 per cent of borrowed funds were used for discharging debt liabilities in last two years, leading the State to a debt trap. The Government should use borrowed funds as far as possible only to fund capital expenditure. The revenue expenditure should be met from revenue receipts. Besides, maintaining a calendar of borrowings to avoid bunching towards the end of the fiscal year and a clear monitoring of the maturity profile of debt payments will go a long way in prudent debt management.

Financial management and budgetary control: Overall savings of Rs 17,437.70 crore was the result of savings of Rs 21,790.88 crore offset by excess of Rs 4,353.18 crore (Paragraph 2.2). The departments of Planning, Women and Child Welfare, Home (Police), Finance (Debt Services and Other Expenditure) posted large savings persistently for the last five years (Paragraph 2.3.2). Excess of Rs 3,399.42 crore requires regularisation under Article 205 of the Constitution of India (Paragraph 2.3.5). There were also instances of unnecessary/inadequate supplementary provision and excessive, unnecessary re-appropriations of funds. Besides, there were many cases of substantial surrenders/non-surrender of anticipated savings. Rush of expenditure at the end of the year is another chronic feature noticed in the overall financial management (Paragraph 2.3.12). Detailed bills were not submitted for large amount of advances drawn on abstract contingent bills (Paragraph 2.4). The position of the Personal Ledger Accounts was also unsatisfactory as huge amounts were parked therein against the principle of legislative financial control.

Budgetary control should be strengthened in all Government departments particularly in four departments where savings occurred persistently during the last five years. Excessive/unnecessary re-appropriation of funds should be avoided and reasons for additional provision/withdrawal of provision in re-appropriation order should be explained therein. Unit-wise control over expenditure should be exercised and the savings anticipated should be surrendered to the Finance department so that the funds could be utilised for development purposes. The re-appropriation of the funds at the close of the financial year should also be minimised.

Financial reporting: State Government's compliance with various rules, procedures and directives was lax as evident from delays in furnishing utilisation certificates against the loans and grants by various grantee institutions. Delays were also noticed in submission of annual accounts by some autonomous bodies and departmental undertakings. There were instances of losses and misappropriations (Paragraph 3.4). Departmental enquiries in such cases should be expedited to bring the defaulters to book. Internal controls in all the organisations should be strengthened to prevent such cases in future.