Executive Summary

1 Background

Government of Andhra Pradesh enacted the "Fiscal Responsibility and Budget Management (FRBM) Act" in October 2005, setting out a reform agenda through a fiscal correction path in the medium term with the long-term goal of securing growth stability for the State economy. The State Government's commitment to carry forward these reforms is reflected in policy initiatives announced in the subsequent budgets. While the benefits of FRBM legislation have been realized to a large extent in terms of reduction in major deficit indicators etc., the State Government's switchover to VAT, introduction of New Pension Scheme, ceiling on Government guarantees and a host of other institutional and sectoral reform measures are expected to facilitate building up the 'fiscal space' needed for improving the quality of public expenditure and promote fiscal stability.

2 The Report

Based on the audited accounts of the Government of Andhra Pradesh for the year ended March 2012, this report provides an analytical review of the finances of the State Government. The report is structured in three Chapters.

Chapter 1 is based on audit of Finance Accounts and makes an assessment of the Government's fiscal position as on 31 March 2012. It provides an insight into trends, *among others*, in State Government's resources and their application, developmental expenditure, borrowing pattern, sustainability of debt etc., besides a brief account of central transfers – both to the State Government, and to the implementing agencies through off-budget route. It also assesses the adequacy of the State's fiscal priorities.

Chapter 2 is based on audit of Appropriation Accounts and reviews the allocative priorities of the State Government and the manner in which the allocated resources were managed by the service delivery departments.

Chapter 3 gives an overview of the State Government's compliance with various reporting requirements and financial rules. The report also has an appendage of additional data collated from several sources in support of the findings.

3 Audit findings and recommendations

3.1 Fiscal consolidation

Government of Andhra Pradesh has been achieving the fiscal reform targets every year in the post FRBM legislation period. The State registered revenue surplus for the 6^{th} consecutive year during 2011-12, and fiscal deficit, despite a marginal increase over the previous year, was well within the ceiling prescribed by the FRBM Act. The total liabilities as a percentage of GSDP stood at 22.27 *per cent* at the end of the current year, against a ceiling of 29.60 *per cent* prescribed in FRBM Act for the year 2011-12.

In line with the FRBM Act, the State Government established Sinking Fund for reduction/ avoidance of debt and Guarantee Redemption Fund and has been contributing to these funds at the rates prescribed by the RBI. However, adverse balances existed under debt head (₹ 3,732 crore), due to wrong booking of assistance to various SPVs as repayment of the latter's debt, which led to understatement of revenue expenditure and thereby, affected the fiscal indicators of the State.

***Recommendation:* Government needs to take a closer look at the factors that affect its fiscal indicators and ensure that proper accounting treatment is given to various transactions, especially those relating to its debt.**

Revenue receipts registered a growth of over 15.50 *per cent* during the current year (₹ 12,558 crore) over the previous year, due to growth in own tax and non tax revenue by ₹ 9,119 crore. Revenue expenditure increased by 15.13 *per cent* (₹11,881 crore) over the previous year, due to increase in both plan and non-plan expenditure. The increase in revenue expenditure is attributable to interest payments and increased assistance to local bodies in education.

While capital expenditure increased by 23 *per cent* and its ratio to total expenditure has also increased significantly to 18.43 *per cent* from 12.28 *per cent* during previous year, it was not up to the level envisaged in the Macro Economic Framework Statement for the year. Capital works/projects in irrigation and roads sectors were not completed on time, which led to cost escalation on these projects without achieving the desired benefits. The investment blocked in such incomplete works/projects as of March 2012 was ₹ 49,516 crore (previous year ₹ 46,330 crore).

***Recommendation:* Government needs to prepare an action plan to complete all the projects in the pipeline for several years, especially those relating to irrigation, within a specified timeframe, so that the envisaged benefits accrue to the targeted beneficiaries. Also, Government should prioritize the areas that need capital expenditure, especially in socio-economic sectors.**

Although the State Government accorded adequate fiscal priority to development expenditure during 2011-12, it did not ensure that allocated funds were fully utilized for the intended purpose. Funds earmarked for specific social sector activities were not always released on time/ not released at all, thereby negating the objective of allocating these funds. State outlay on education in particular, was way behind (13.80 *per cent*) that of the General Category States (17.18 *per cent*). Further, the share of capital expenditure in Social Sector (12.58 *per cent* of aggregate expenditure) was also lower in the State, compared to the General Category States (13.71 *per cent*).

***Recommendation:* Government needs to re-prioritize the outlay in respect of social sector and ensure that funds are released based on approved outlays and spent for the purpose sanctioned. Greater fiscal priority needs to be accorded to education and health sectors. Besides, capital expenditure needs to be increased to create adequate asset back up for increasing liabilities.**

Government had not estimated the yearly pension liabilities on actuarial basis for the ensuing years, as stipulated in the FRBM Act. The State Government's progressive liability with regard to its share in the Contributory Provident Fund scheme as of 31 March 2012 was ₹ 894 crore, which has not been transferred to the Fund Manager, as required by the Pension Fund Regulatory Authority. In fact, during the current year, Government provided ₹ 100 crore less in the budget, as compared to the contribution of the employees during the year.

Recommendation: ***Government should review its budgetary allocation for pension and provide for its liability on this account on the basis of actuarial valuation. Further, it should transfer the accumulated fund amount immediately to the Fund Manager.***

Return on investment in Companies/Statutory Corporations continued to be poor and the rate of return on investment was 0.85 *per cent* during 2011-12, while the rate of interest paid by the Government during the year was 7.40 *per cent.* The accounts of several of these companies/corporations have been in arrears and up to the year of accounts finalized, the accumulated losses of 11 entities alone amounted to ₹ 5,979 crore, with AP State Housing Corporation (₹ 3,554 crore) and APSRTC (₹ 1,984 crore) leading the list.

The current level of recovery of loan is abysmal, with the gap between disbursement (₹ 4,983 crore) and recovery (₹ 164 crore) widening. In fact, confirmation of balances on loan amount of ₹ 17,337 crore was yet to be received from the entities, which were the recipients of these loans.

Recommendation: ***The losses of State Public Undertakings (PSUs) are attributable to a large extent to deficiencies in project implementation and operational and financial management. The State Government needs to draw up a roadmap for closure of loss making PSUs in non-commercial areas, in keeping with the recommendation of the 13th Finance Commission. Government also needs to follow up with the recipient entities to confirm the loan amount balances with them and pursue for repayment of both principal and interest in a time bound manner.***

(Chapter 1)

3.2 Financial Management and Budgetary Control

As with 2010-11, there were several lacunae in the budgetary processes of the State Government. There were errors in budgeting, several misclassifications continued to exist, lumpsum provisions were made without clarity of purpose (only to be surrendered later), excess expenditure over allocation, expenditure without budget provision etc. Financial rules were flouted by several departments by drawing funds in excess of requirement, resorting to re-appropriations without proper explanations and expending without provision of funds. Persistent savings in certain Grants and huge savings of over ₹ 500 crore and over 20 *per cent* of budgetary provision in certain other Grants, indicate inaccurate budgetary assumptions.

Saving of about one sixth of the budgetary allocation and non-utilisation of funds allocated for various developmental programmes raises serious questions about the budget formulation exercise. While this could show a healthy picture as far as fiscal indicators are concerned, it has had an adverse impact on implementation of various policy initiatives announced/taken up by the Government.

Recommendation: ***Government should ensure that budgeting process is more transparent and result oriented. Basic assumptions in budgetary formulation have to be more accurate and efforts should be made by all the departments to submit realistic budget estimates, keeping in view the past trends in receipts and expenditure in order to avoid large scale saving/excess, re-appropriations and surrenders at the fag end of the year.***

(Chapter 2)

3.3 Financial reporting

Several State Government departments were not compliant with the applicable rules and regulations, especially those relating to compilation and submission of accounts for audit and reporting utilization of funds placed at their disposal for implementation of various socio-economic developmental schemes. Internal controls were not functioning as envisaged, as evidenced from non-reconciliation of receipts and expenditure with those booked by the Principal Accountant General (A&E), irregular and unauthorized parking of funds in various deposits outside Government accounts, non-adjustment of advances drawn on AC bills with the relevant DC bills for prolonged periods etc. Adequate attention was not given by the Government to ensure that relevant vouchers/missing documents were provided by the concerned authorities to adjust the amounts held in suspense heads. **Operation of over one lakh Personal Deposit (PD) accounts and locking up of about ₹ 23,483 crore in these accounts, affected the transparency of Government accounts.** Classifying large amounts and important items of expenditure like ‘subsidies’ under omnibus Minor Head 800 affected transparency in financial reporting.

Recommendation: ***Government needs to strengthen financial management and reporting, especially in areas such as timely compilation of accounts by Government undertakings and bodies, adjustment of funds drawn through AC bills and correct classification of expenditure at the Minor Head level. Government should initiate stringent measures to streamline the system of PD Accounts and ensure that these are operated in a transparent manner in accordance with the letter and spirit of the relevant instructions and rules.***

(Chapter 3)