Chapter 3 Transparency in Budgeting and Financial Management in Indian Railways

3.1 Introduction

Budget is an annual exercise for detailing the roadmap for generating resources and their efficient use. It is a legal document that is passed by the legislature, and approved by the chief executive. It provides a forecast of revenues and expenditures, and allows us to predict our performance financially if certain strategies and plans are carried out. It enables us to determine how well the government has performed against the forecast. Budgets have an economic and political basis. Government budgets are not entirely designed to allocate scarce resources for the best economic use. They also have a political basis wherein different interests push and pull in an attempt to obtain benefits and avoid burdens.

The Constitution of India prescribes vide Article 112(1) of that 'the President shall in respect of every financial year cause to be laid before both the Houses of Parliament, a Statement of the estimated receipts and expenditure of the government for that year' referred to as the "annual financial statement" and popularly called the "Annual Budget". The constitution requires that the 'financial statement' shall contain a statement of the estimated receipts and expenditure for the coming financial year. As a matter of convention, every budget contains three elements-

(a) A review of the preceding year, including the actual receipts and expenditure in that year;

(b) An estimate of the receipts and expenditure of the coming year; and

(c) Proposals, if any, for meeting the requirements of the coming year.

The Railway Budget is presented to both Houses of Parliament separately from and ahead of the General Budget. Though the Railway Budget is separately presented to Parliament, the figures relating to the receipts and expenditure of the Railways form part of the General Budget, since the receipts and expenditure of the Railways are part of the total receipt and expenditure of the Government of India. The provision relating to 'Railway Budget' as contained in Para no. 301 of Indian Railway Financial Code (IRFC) Volume-I interalia states that 'though the Constitution does not provide for the presentation of the annual financial statement or Budget in parts, the Rules of Procedure of Parliament have provided that nothing shall be deemed to prevent the presentation of the Budget to the house in two or more parts and when such presentation takes place, each part shall be dealt with in accordance with the rules as if it were the Budget'. This provision has enabled the Separation of the Railway Budget from the General Budget and the passing of separate Appropriation Acts for each of these Budgets in keeping with the Separation Convention (1924).

To ensure greater equity in Fiscal management and long term Macro-economic stability, the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 was passed by an act of Parliament on August 26, 2003. The Act came into force on July 5, 2004. The main objective of this Act was to ensure inter-generational equity in fiscal management and long-term macro-economic stability. It also aimed at prudential debt management consistent with fiscal sustainability and greater transparency in fiscal management of the Central Government.

Section 6 (1) and (2) of the FRBM Act 2003 prescribes that the Central Government shall take suitable measures to ensure greater transparency in its fiscal operations in public interest and minimize as far as practicable, secrecy in the preparations of annual financial statement and demands for grants. It also committed to make such disclosures as prescribed at the time of presentation of the annual financial statement and demands for grants.

Transparency in the budget processes help instill a sense of accountability in the policy makers, and bring better perspective and strategies and encourage timely and effective implementation of the budget proposals. It also helps to attain greater legislative control over the budget process, and create public confidence in the willingness as well as the ability of the government to work for people.

Transparency in government budgeting could be considered to be based on four principles viz.

- Open budget process,
- Public availability of information
- Clarity of roles and responsibilities and
- Assurance of integrity.

The present chapter examines the extent to which transparency in budgeting and financial management exists in IR.

3.2 Open Budget Process

The budget process and information presented in the budget documentation are central to fiscal transparency. The Annual budget of IR is an occasion on which IR presents its expenditure proposals and the means by which it will finance them. Thus, the information provided at the time of annual budget should cover all financial activities, irrespective of the institutional arrangement under which they take place.

3.2.1 Statements of Fiscal Policy

The FRBM Act, 2003 provides that the Central Government shall lay in each financial year before both houses of Parliament the following statements of fiscal policy along with the annual financial statement and demands for grants, namely:

(a) The Medium Term Fiscal Policy Statement,

(b) The Fiscal Policy Strategy Statement and

(c) The Macro-economic Framework Statement.

- The Medium-Term Fiscal Policy Statement should indicate a three-year rolling target for prescribed fiscal indicators with specification of underlying assumptions. This policy should also include an assessment of sustainability relating to the balances between revenue receipts and revenue expenditure and the use of capital receipts including market borrowings for generating productive assets.

  In the context of IR, the Medium Term Fiscal Policy Statement would indicate a three year rolling target for fiscal indicators like projected net surplus i.e., excess of revenue receipts over revenue expenditure, and its investment strategy for capacity augmentation and means of financing the same. IR would need to indicate its strategic priorities regarding subsidy on passenger services and subsidized freight charges for carrying essential commodities.

- The Fiscal Policy Strategy Statement indicates the policies of the Central Government for the ensuing financial year relating to taxation, pricing of administered goods & services etc. It should also indicate the strategic priorities of the Central Government for the ensuing financial year in the fiscal area. Further, the key fiscal measures and rationale for any major deviation in fiscal measures pertaining to taxation, subsidy, expenditure, administered pricing and borrowings. An evaluation as to how the current policies of the Central Government are in conformity with the fiscal management principles and objectives set out in the Medium-term Fiscal Policy Statement should also be included.

  The Fiscal Policy Strategy Statement of IR would require indication of its policies relating to pricing of services provided, expenditure, investment strategy and use of capital receipts including its internal resources as well as support from general budget and extra budgetary resources for assert creation. IR would need to indicate its strategic priorities regarding its pricing policy, subsidy on passenger services and subsidized freight charges for carrying essential commodious. It would also include a disclosure of any deviation from already spelt out policies in Medium Term Fiscal Policy Statement either for the current year or during the course of previous financial year.

- The Marco-economic Framework Statement of the Central Government contains an assessment relating to growth of gross domestic product, the fiscal balance of the Union Government as reflected in the revenue balance and gross fiscal balance and the external sector balance of the economy as reflected in the current account balance of the balance of payments.

  In the context of IR, this statement would need to indicate an assessment of the growth strategy of the IR with specification of the underlying assumptions. The balances under various railway reserve funds needed to sustain its replacement/renewal expenditure need to be delineated along with investments required for creation of new assets for achieving the targeted growth rate. More specifically, the dependence of IR on the general budget and extra budgetary resources for financing its plan expenditure would need to be delineated in such a statement.

Ministry of Railway does not lay any of these Statements in Parliament. In response to an audit query[26], Ministry of Railways stated that the fiscal policies of the government are in the domain of the Ministry of Finance and it being only a department of the Government of India, IR does not present any such statements. The response of the Ministry is not acceptable as FRBM Act, which extends to the whole of Government of India, is equally applicable to IR. Moreover, since the budget of the Ministry of Railways is a part of the budget of Government of India it must fulfill the requirements of the Act in the same manner as the Ministry of Finance.

In the absence of these statements, an analysis of information provided in the annual budgetary documents indicated that following aspects of the financial performance of IR remain undisclosed:

- Changes in freight and fare structure brought out during the year.
- Investment strategy for the short and medium term including means of financing the same.

[26] ***Consolidated reply to Chapter-3 from Railway Board is still awaited.***

- Provisions for fund to finance assets due for replacement/renewal that is essential to maintain operational safety. Presently, contribution to Depreciation Reserve Fund (DRF) is being made on need and availability basis instead of actual requirement as per life and physical condition of the asset.

In the absence of a Medium Term Fiscal Policy Statement (MTFP), IR failed to assess and make sufficient provisions for expenditure on account of implementation of recommendations of 6th CPC. This led to adjustment of accounts by transferring fund from Depreciation Reserve Fund, which was already underfunded, to Pension Fund in 2009-10, to absorb debits from pension payment authorities received at the end of the year. This was necessary to keep expenditure within available resources. The operating ratio which showed continuous improvement from the year 2003-04 to 2007-08 with the remarkable achievement of 75.94 *per cent* in 2007-08, deteriorated sharply to 95.28 *per cent* during 2009-10. Such sharp fluctuation in the financial performance could have been evened out if requirement of presenting MTFP had been adhered to.

3.2.2 Extra Budgetary Activities

Plan expenditure of IR is financed partly by extra-budgetary support from Indian Railway Finance Corporation, State Governments (Metropolitan Transport projects), Public Private Partnership activities etc. Activities financed through extra-budgetary funds need to be integrated into the budget process, so that overall fiscal control is maintained. Such activities should be indentified in the annual budget, along with a statement of the purpose or policy rationale. By keeping these proposals outside the Budget Estimates a significant part of IR's financial activities has not been subject to Parliamentary Approval.

Ministry of Railways, in response to an audit query, stated that while formulating the Railway Plan these projections are discussed with Planning Commission. The estimates for the extra budgetary resources are part of the budget proposals that is approved by Minister of Railways and Finance Minister. After that, these figures are mentioned as a footnote in the Demands for Grants which is presented to Parliament.

The reply is not tenable in view of the following:

1) Footnote in the Demands of Grants merely discloses the amount proposed to be raised through borrowings by IRFC, RVNL, and funding through Public Private Partnership etc., but fails to disclose the funds raised from

state governments to meet Capital Expenditure from the funds outside the budget, in respect of the following projects.

- Belapur-Seawood-Uran (27 KM) project-sanctioned in 1996-97 (costing ₹ 495.44 crore) with cost sharing between Railways and City industrial Development corporation in 1:2 ratio.
- Mumbai Urban Transport Project Phase-I - sanctioned in 2003-04 at an anticipated cost of ₹ 4,174.40 crore with cost sharing between Railways and State Government of Maharashtra in 1:1 ratio.
- Mumbai Urban Transport Project Phase-II - sanctioned in 2008-09 at an anticipated cost of ₹ 5,300 crore with cost sharing between Railways and State Government of Maharashtra in 1:1 ratio.
- Extension of Mass Rapid transport System Phase-II from Velachery to St. Thomas Mount (5 km.)- sanctioned at a cost of ₹ 495.74 crore with cost sharing between Railway and Statement Government in 1:2 ratio.

By not disclosing this capital expenditure, the actual assets created by IR remain understated.

2) Further, a reference is invited to Budget Documents namely 'Explanatory Memorandum on the Railway Budget- Table VI' and 'Outcome and Performance Budget of Railways - Box-2', which contain the information relating to physical targets vis-à-vis achievement of IR with respect to rolling stock for the year and the total assets of IR respectively. It is seen that these documents do not disclose the information regarding the number of rolling stock added to the fleet of IR through funding from IRFC.

3.2.3 Budget Execution, Monitoring and Reporting

Clear procedures for budget execution, monitoring and reporting need to be laid down to ensure financial transparency. This includes a good Accounting system (which can effectively track revenues, commitments, payments and arrears) and presentation of audited final accounts and audit report to the legislature within a year. Transparent budget execution relies on having an accounting system with comprehensive coverage of all transactions relating to government expenditure and revenue collection, and a system of effective internal controls. Even if the accounting system is cash-based, fiscal transparency requires that the system records commitments as well as payments in order to effectively monitor arrears.

3.2.3.1 Assessment of Arrears/Liabilities

Government accounting systems should be able to provide sufficient information to assess arrears in expenditure/revenue receipts. Cash accounting in government understates the real financial status of the government to the extent that government has substantial or persistent payment arrears to supplier, employees, or pensioners etc. Thus, for transparency, cash accounts should be supplemented by accounts-based reports of bills due for payment to assess total liabilities.

IR has an established accounting system based on financial rules and Codes. Though, it has a system to account for un-realized revenue but it does not provide for assessment of liabilities. It also does not capture information at the commitment stage. Issue was taken up with the Ministry of Railways, which stated that there is no separate head/primary unit for capturing the arrear payments due. However, broad assessment of arrears is made for budgetary purposes on the basis of parameters available for payment of such arrears as per the policies/sanctions issued, base year data and other information available.

The reply is not tenable as it was seen that system of assessment even for salaries and pension payments was not realistic as there were substantial variations between both original and revised estimates and actual expenditure reported in 2008-09 and 2009-10. These variations were stated to be on account of implementation of 6^{th} Central Pay Commission recommendations. It was also seen that unexpected debits on account of payment of arrears to pensioners were received from pension payment authorities at the close of 2009-10, which forced the ministry to increase availability of finances in Pension Fund. Thus it is essential to amend the codes and manual of IR so as to assess the arrears of salary/pension as also other liabilities at the end of financial year.

3.2.3.2 Mid-Term Assessment

FRBM Act 2003 provides that the Minister-in-charge of the Ministry of Finance should review every quarter, the trend in receipts and expenditure in relation to the budget and place before both Houses of Parliament the outcome of such review. The issue was taken up with the Ministry, which stated that review of receipts and expenditure is done regularly on the basis of trend available as per the monthly account current vis-à-vis the budget proportions. Quarterly financial progress of the railways is also reported to the Finance Minister. The midterm review of Railway receipts/expenditure is also conducted through the August Review Estimates, which form basis for finalizing the Revised Estimates presented to Parliament along with the Budget Estimates for the next year.

Audit observed that the trends in receipts and expenditure in relation to the budget are discussed only internally. No midterm review of receipts and expenditure is placed by Minister-in-charge of Railways before Parliament as required under the FRBM Act. This keep the Parliament informed of current

Fiscal developments of IR. Further, placing this report before Parliament, if done, would enable the Government to take appropriate corrective measures to increase the revenue or reduce the expenditure to the pre-specified levels mentioned in the fiscal policy strategy statement during the course of the year. Such reporting to Parliament would also set the stage for policy corrections at the stage of presentation of Railway budget.

3.2.3.3 Supplementary Budget

An important feature of transparent budgeting is that supplementary expenditure proposals during the financial year should be presented to the legislature in a manner similar to the original budget. Moreover, provisions of Indian Railways Finance Code (Volume-I) also stipulate that estimates of supplementary grants/Appropriations submitted by the Ministry of Railways to the vote of Parliament/President in the same way as the original 'Demands for Grants/Appropriations'.

It was, however, seen that IR does not present supplementary grants/ appropriations in the same format as the original Demand for Grants presented to Parliament. The supplementary demand for grants presented by the Ministry indicates only the Railway-wise allocations against each grant. This results not only in violation of the codal provision prescribed in IRFC Volume-I but also leads to lack of control over allocations/expenditure of supplementary grant.

3.2.3.4 Expenditure in excess of Parliament Authorization.

Fiscal management requires that no public funds are spent without appropriation sanctioned by the legislature. It should be ensured that authorization is comprehensive and should include all government transactions, including those through extra-budgetary funds.

Despite a clear regulatory fiscal management system IR has been incurring expenditure more than that authorized by legislature which is later being regularized. It could be seen from the table below that the percentage of excess expenditure to the effected Grants is continuously on the increase.

Table 3.1- Expenditure in excess of Authorization

Year	Excess expenditure (₹in crore)	Excess expenditure as percentage of sanctioned grant
2008-09	519.81	1.88
2009-10	1,929.61	3.19
2010-11	3,052.78	4.14

3.2.3.5 Audited Accounts and Report

The budgetary documents placed in parliament by IR generally include the following documents;

- Budget Speech
- Budget Statement
- Demands for Grants
- Explanatory memorandum on Railway Budget
- Works, Machinery and Rolling Stock Programme
- Outcome and Performance Budget
- Appropriation Bill

Good practices of transparency require that the government should prepare year-end report to demonstrate key results achieved and to outline a comprehensive overview of the government's financial assets and liabilities and contingent liabilities. The year-end report should explain any deviation from compliance with the level of revenue and expenditure authorized by the legislature in the budget. Further, final accounts should explain any deviations from the budget as adopted by the legislature.

The issues as discussed in the preceding section were raised with Ministry of Railways which stated that assessment of physical targets and financial outlay in the budget are reviewed at the revised estimates stage. Information relating to certain salient works relating to safety, capacity enhancement, etc is printed both for the budgeted and the revised targets in the budget documents like "Explanatory Memorandum" and "Outcome Budget" which form part of the budget documents presented to Parliament.

The reply is not tenable as the budget documents do not indicate reasons for deviation from compliance with the level of revenue and expenditure authorized in the budget. Similarly, there is no disclosure in the budget papers of modifications introduced during the course of financial year in the freight and fare structure after the presentation of the previous year's budget. In the absence of such a disclosure financial performance of IR as shown in the budget statements would not meet the standard of 'fair presentation' as an upward revision in fare structure would have led to improvement in financial performance even though the physical targets may remain the same.

It was further seen that IR did not prepare a year-end report demonstrating key achievements on measures proposed in the Railway Minister's Budget Speech. A test check of the last three years' Railway Minister's budget speech and Outcome Budget revealed the following:

Table 3.2- Status of implementation of Budget Announcements

Reference no. of Budget Speech Year (Para No.)	Brief of Budget Announcements as made in Budget Speech	Status of Implementation as given in Outcome Budget[27] of relevant year	Remarks
2008-09 (15), 2009-10 (23)	**Tickets booking through UTS (Unreserved Ticketing System) and Automated Vending Machine (AVM)** **2008-09-**UTS counters were announced to be increased in next two years from 3000 to 15000, AVM from 250 to 6000. **2009-10-**UTS- to be increased from 5000 to 8000, AVM would be installed at 200 large and medium size stations.	**2011-12-** With a view to facilitate issuing of un-reserved tickets, Jansadharan Ticket Booking Sewaks (JTBS) are being appointed in city areas. They are provided UTS terminals and are allowed to realize commission from the passengers. At present around 438 JTBS have been appointed on different Zonal Railways.	These two pronouncements have no clarity/ transparency as no list of stations which were identified for installation of UTS have been submitted in the budget. The outcome listed has no correlation with the targets announced in the budget speech.
2008-09 (22), 2009-10 (20) 2010-11 (79)	**Provision of Green Toilets** **2008-09-** provision of green toilets in all 36000 coaches by the end of 11th plan period **2009-10-**field trials are being conducted for green toilets and also for vacuum toilets similar to aircraft **2010-11-**introduce at least 10 rakes with green toilets	**2010-11 and 2011-12-**Different designs/technologies for 'green toilets' have been put to field trials for performance evaluation before considering adoption as a regular measure.	(i) Despite being announced in three years consecutively still at an experimental stage. (ii) The announcement made on February 25, 2008 for provision of green toilets in all 36000 coaches without completing field trials was unrealistic.
2008-09 (26), 2009-10 (15)	**On board cleaning of passenger trains** **2008-09 -** On board cleaning on all Rajdhani, Shatabdi and Superfast	**2010-11** The scheme has been implemented in 110 pairs of trains. Action is underway to	There is no clarity in the Outcome budget as to whether targets indicated in the

[27] ***Outcome and Performance Budget of Railways placed for any particular budget year, bring out the achievements/highlights that the railway has tried to deliver up to two years preceding the budget year.***

	Mail and Express trains will be carried out through trained manpower of professional agencies using modern machines and material **2009-10** - During current year On Board House Keeping Scheme (OBHS) will expand to cover 200 additional pairs of trains	further proliferate the scheme to all other identified trains. **2011-12** the scheme has been implemented in 290 pairs of trains. Action is underway to further proliferate the scheme to all other identified trains.	budget speech have been completed.
2008-09 (71), 2009-10 (29) 2010-11(34)	**Anti Collision Device (ACD)** **2008-09** – pilot project started in NEFR, encouraging results yielded, this will be extended on three railways- SR, SCR and SWR in the next two years. **2009-10-** made operational on 1736 RKm in NEFR, 1700 RKm on three railways - SR, SCR and SWR planned to complete in two years. **2010-11-** already installed in NEFR, and is now proposed to extend to three more zonal railways,	Status not furnished in Outcome Budget of both years.	The announcement has been made in three years consecutively. Status of implementation of these proposals has still not been furnished.
2009-10 (12) 2010-11 (24)	**World Class Stations** 2009-10- to develop about 50 stations as world class stations (list of 35 such stations furnished) 2010-11- 10 more stations identified to be converted into world class stations (list of 10 stations given.)	**2011-12-** the fifty railway stations in Metro and Mini metro cities have been identified for development as World Class Stations.	Status of progress in development of the stations has not been indicated.
2009-10 (13), 2010-11 (23)	**Adarsh Stations** **2009-10-** to develop 375 stations as Adarsh stations (list of 309 such stations identified and	**2011-12** In order to develop stations as Adarsh Stations, **584** stations have been identified. Out of 584	. The information relating to no. of stations contained in two budget

	given in Budget speech), **2010-11-** 94 more stations identified to be developed as Adarsh stations (list of 94 such stations given)	identified stations, work of development as 362 Adarsh stations has been completed by January 2011.	documents is in consistent with each other.

During test check it was also noticed that the Status of implementation of Budget proposals/Announcements made in Budget speech was not indicated in the outcome budget in respect of the following Projects/Schemes:

Table 3.3- Budget Announcements where implementation status not disclosed

Reference no. of Budget Speech Year (Para No.)	Brief of Budget Announcements as made in Budget Speech	Status of Implementation as given in Outcome Budget of relevant year
2008-09	Provision of on-line monitoring of Rolling Stock (OMRS) through acoustic bearing detectors and wheel impact load detector (WILD)	Status not furnished in Outcome Budgets of relevant years.
2009-10 (24), 2010-11(31)	Introduction of Mobile ticketing vans - “Mushkil Aasaan”	Status not furnished in Outcome Budgets of relevant years.
2009-10	Running of Special trains to carry perishable products like fruit and vegetables, fish etc	Status not furnished in Outcome Budgets of relevant years.
2009-10	Running of superfast parcel trains on 3 routes	Status not furnished in Outcome Budgets of relevant years.
2010-11	Provision of automatic fire and smoke detection system in 20 pairs of long distance trains - a Pilot project	Status not furnished in Outcome Budgets of relevant years.
2004-05, 2005-06,2009-10	Setting up of Rail Wheel Factory - Chhapra	Status not furnished in Outcome Budgets of relevant years.
2007-08	Setting up of Electric Locomotive Factory - Madhepura	Status not furnished in Outcome Budgets of relevant years.
2008-09(97),2009-10 (47), 2010-11(65)	Setting up of Rail Coach Factory - Kerala	Status not furnished in Outcome Budgets of relevant years.
2010-11	Setting up of Rail Coach Factory - Kancharapara	Status not furnished in Outcome Budgets of relevant years.
2010-11	Setting up of Diesel Multiple Unit - Sankrail	Status not furnished in Outcome Budgets of relevant years.
2010-11	Setting up of Rail Axle Factory - New Jalpaiguri	Status not furnished in Outcome Budgets of relevant years.

It is thus seen from Table 3.2, that proposals were announced repeatedly in Budget speeches in one form or the other, without indicating actual status of their implementation in the Outcome Budget. Further, in the outcome budget there was no clarity on the status of implementation of the budget announcements made.

Audit observed that the Government of India budget documentation includes a separate document called 'Status of Implementation of Announcements made in Finance Minister's Budget Speech of the previous financial year'. However no such document is placed before Parliament along with the budget documents by the Ministry of Railways.

3.3 Public Availability of Information

Making fiscal information available to the public is a defining characteristic of fiscal transparency. It requires provision of comprehensive information covering past, recent and future performance, fiscal risk, contingent liabilities, quasi-fiscal activities, revenue resources, debt and financial assets, and fiscal risk.

3.3.1 Past, Present and Future Performance information

For a more complete picture of the current fiscal position, information on past fiscal performance should be presented in the annual budget. Transparency in budgeting requires that original and revised budget estimates for at least two preceding years together with the actual expenditure should be included with the annual budget. Forecasts for at least two years beyond the budget year should also be included based on realistic assumptions about growth in GDP and consistent with stated policy objectives over the medium term.

IR budget provides information only on Budget estimates of the ensuing budget year, budget estimates and revised estimates of the year preceding the budget year and actual of the year immediately before the preceding year. Audit observed that the Medium Term Fiscal Policy Statement placed by Government of India in Parliament provides targets for two successive years beyond the budget year. This statement indicates the major fiscal indicators of the Government as a percentage of GDP. The basis of making these projections for the future are also discussed in the statement.

In the context of IR this would require indication of targets for net surplus i.e. excess of revenue receipts over revenue expenditure, dependence on the general budget and extra-budgetary resources in the next two years.

3.3.2 Concession, Contingent Liabilities, Subsidy and Fiscal Risk

To ensure greater transparency in fiscal operation the concessions granted by the IR, their contingent liabilities and fiscal risk should be part of the budget documentation. IR budget does not disclose the following information:-

- Concessions given by IR is a form of revenue foregone and can be regarded as a targeted subsidy. IR provides free railway travel passes to its employees, concessions to various categories of passengers like senior citizens, physically handicapped persons, student, freedom fighters etc. as well as to essential commodities of freight traffic like fruits and vegetables, paper, bamboo, cotton etc. Though the cost of concessions given on movement of freight traffic (commodities carried below cost) are disclosed in the supporting documents to the budget, the cost of concession given to the various categories of passengers/employees are not disclosed.
- Contingent liabilities are costs that the government will have to pay if a particular event occurs. Under the cash accounting system, contingent liabilities are recognized only when the contingency actually occurs and payment is made. No disclosure of any contingent liabilities like pending court cases, arbitration cases, disputed claims etc are disclosed by IR in budget documents or final accounts.
- The financial arrangements entered into by Ministry of Railways with IRFC and RVNL indicate the existence of implicit guarantee. The details are discussed below:-.

  - IRFC has been borrowing from the market for creation of rolling stock assets for the Ministry of Railways. Borrowings of ₹ 9,017.79 crore in 2009-10 and ₹ 9,680.29 crore in 2010-11 were made for purchase of rolling stock to be used by IR. Repayments to the tune of ₹ 5,367.24 crore in 2009-10 and ₹ 6,338 crore in 2010-11 were made. These carry an implicit guarantee of Ministry of Railways as IRFC has first charge on the rolling stock acquired by the Railways through IRFC borrowings. As on 31 March 2011 Ministry of Railways owes IRFC ₹ 36,182.68 crore.

  - RVNL has been allowed by IR to take loan from IRFC for financing project execution of IR. The principal and cost of borrowings, on the borrowings from IRFC are repaid by MoR through RVNL. Amount of such loan, for which MoR is committed to make repayments to IRFC on behalf of RVNL, stood at ₹ 1,871 crore as on 31st March 2010 in the books of RVNL. Though these loans do not carry any explicit guarantee of IR, these are being repaid by them through their budgetary allocations.

3.4 Clarity of Roles and Responsibilities

Transparency requires that government sector should be distinguished from the rest of the public sector and from the rest of the economy. Administrative framework clearly defines role and responsibilities of various wings to promote accountability and good governance.

3.4.1 Relationships between the Government and Public Corporations/Undertakings owned in whole or in partly by the government need to be clearly stated to ensure transparency

Financial Relationships between the government and public corporations/undertakings owned in whole or in partly by the government need to be clearly stated to ensure transparency. During Audit of Accounts of IR for the year 2010-11 it was observed that the relationship between MoR and its PSUs was not clearly delineated. The major issues are discussed below:-

- Statement no. 11 regarding the Investment of the Union Government in Statutory Corporations, Govt. Companies, other joint stock companies, co-operative banks and societies, etc. forms part of the Finance Accounts of IR. It contains the details of total investment of IR with respect to number, type, face value of shares along with the percentage of shareholdings in each public sector undertaking. However for the year 2010-11, this statement is depicting an inadequate picture in respect of its investment in PSUs. During audit of accounts of IR, the following shortcomings accounting of equity/bonus/preference shares have been noticed:-
  - Equity Shares numbering 4935600, 40999900 and 39900000 amounting to Rs. ₹ 85.83 crore allotted to IR as Bonus shares by Ircon International Limited (IRCON), Container Corporation of Indian Limited (CONCOR) and RITES Limited (RITES) respectively in the previous years have neither been depicted in statement no. 11 nor accounted for in the accounts of IR in the respective years.
  - Equity shares numbering 305938400 amounting to ₹ 305.94 crore issued to Railways 'For consideration other than cash' by RailTel Corporation of India Limited (RCIL) have neither been depicted nor accounted for in the accounts of IR. Further, the value of assets transferred by IR in lieu of equity and the year of transfer required to be disclosed have also not been depicted.
  - Equity shares numbering 27350100 amounting to ₹ 27.35 crore issued to IR by RVNL 'For consideration other than cash' has wrongly been reflected as cash investment of IR.

- Preference Shares numbering 40795100 amounting to ₹ 4,079.51 crore were allotted to IR by Konkan Railway Corporation Limited. These were allotted by converting the existing loan from IR into preference shares. The effect of this conversion has not been reflected.
- The face value of equity shares owned by IR in RITES and Dedicated Freight Corridor Corporation of India Limited (DFCCIL) has been shown incorrectly as ₹ 100 each in place of ₹ 10 and ₹ 1000 respectively.

➢ Every year IR is taking Rolling Stock Assets on lease from IRFC. The leased Rolling stock forms part of the fleet of rolling stock in operation on the IR network. Leased assets are operated and maintained in the same manner as IR – owned assets. However the values of the assets taken on lease from IRFC have not been included in the balance sheet of IR. These assets amount to ₹ 69,795.43 crore.

In reply, the Ministry stated that a footnote regarding disclosure of rolling stock assets taken on lease from IRFC has been shown in Balance Sheet printed as part of the Appropriation Account Part-I-Review (This is a separate publication issued by the Railway Board). The reply is not tenable as this publication is an internal document of the IR and is not certified by audit.

3.4.2 Responsibility and Accountability

Transparency requires that financial information should be prepared in a way that facilitates policy analysis and promotes accountability. Budget transactions need to be able to be reviewed from the perspective of their economic impact, the form of appropriation, administrative control, and their purpose. A recording and classification system that meets these needs provides the foundation for the presentation of the budget, final accounts, and other fiscal reports. A classification by Administrative category is important for internal control purpose. It should allow clear tracking of responsibility for the collection and use of public funds.

IR has a well defined system of classification where the expenditure is classified under demands for grants. These are activity-wise categorized like General Superintendence and Services, Repairs and Maintenance, Operating Expenses, Staff Welfare and Miscellaneous Expenditure. However, the classification system does not allow administrative wise clear tracking of responsibility and accountability as expenditure under a grant is controlled by one or more administrative heads. For instance:-

- Grant no. 5 deals with Repairs and Maintenance of Locomotives. IR runs mainly diesel and electric locomotives. Thus repair and maintenance of diesel locomotives is controlled by Member (Mechanical) whereas repair and maintenance of electric locomotives is controlled by Member (Electrical).

- Grant no. 8 deals with Operating Expenses – Rolling Stock and Equipment. This grant includes operating expenses relating to steam, diesel, and electric locomotives, electric multiple unit coaches and signaling and Telecommunications etc. Operating expenses relating to steam and diesel locomotives are controlled by Member (Mechanical). However operating expenses relating to EMU coaches and signaling and telecommunications are controlled by Member (Electrical).
- Similarly, Grant no. 10 deals with expenditure on fuel on diesel and electric traction. Thus this grant is again controlled by both Member (Mechanical) and Member (Electrical).

Thus it is not possible to centrally monitor expenditure incurred under various grants. This problem is further aggravated by the fact that re-appropriation is permitted from allocation under the control of one administrative head to another administrative head. As discussed in para above monitoring of expenditure is weak.

3.5 Assurance of Integrity

The quality and integrity of fiscal data reported by the government is critical for claiming fiscal transparency. It is essential that there should be a mechanism in place that provides assurances to the legislature and the public on data integrity.

3.5.1 Realism of Budget Data

Budget forecast and updates should reflect recent revenue and expenditure trends, underlying macroeconomic developments, and well defined policy commitments. The assumptions underlying trends need to be clearly explained. Poor budget preparation leads to problem in implementation due to of sudden claim arising on resources and need for large scale re-appropriations and frequent supplementary budget etc.

Forecasting by IR of their revenue and expenditure has not been realistic. Reliability of budget estimates has regularly been commented upon in the Reports of Comptroller and Auditor General of India Union Government (Railways)[28]. Due to variation in revenue receipts and expenditure, net surplus of IR was less by 62 *per cent* in 2008-09 and around 100 *per cent* in 2009-10

[28] **CA No. 19 of 2008-09 (paragraph 1.2), CA-11 of 2009-10 (paragraph 1.2) and no. 33 of 2010-11 (paragraph 1.2).**

as compared to the budget estimates of the respective year. Unrealistic budget estimations also led IR to seek number of supplementary provisions which too proved to be either inadequate or excessive.

3.5.2 Accounting Standards

The annual budget and final accounts should indicate the accounting basis used in compilation and presentation of fiscal data. Transparency requires the annual budget and final accounts should indicate the accounting basis and standards used in compilation of accounts. Any change in revision in accounting methodology and practices should be disclosed together with the reasons for the changes and an indication of their impact on fiscal aggregates.

3.5.3 Follow up action on Audit Report

A reference is invited to Chapter-3 of the Report of Comptroller and Auditor General of India, Union Government (Railways) - no. 33 of 2010-11 on Railways Finances. This Report highlighted the following:

- IR being a Departmental Undertaking does not disclose significant accounting policies that are being followed in preparation of financial statements like profit and loss accounts and balance sheets. This included accounting of Fixed Assets, Depreciation, Provisioning of liabilities for pension, Revenue Recognition etc. For instance Depreciation represents reduction in value of an asset on account of wear and tear. It is charged to the P&L account. In IR an adhoc sum is charged to the working expenditure towards contribution to the depreciation reserve fund. This appropriation was done on need-cum-availability basis instead of in a scientific manner taking into account the historical cost, expected useful life and expected residual value of the asset. This gave leverage to IR to manage its net revenue surplus at the desired level. Further, adhoc provisioning for depreciation did not give a fair view of the working results of IR.
- Further a cash flow statement which records the amount of cash/cash equivalent entering and leaving the organization was not being prepared.
- Financial statements normally include Schedules and Notes to the Balance-Sheet and Profit & loss account. IR did not prepare these to the major items of its assets, liabilities, revenue and expenditure except the statement of Block Assets.

  No Action Taken Note on the above has yet been received.

3.5.4 Data Consistency and Reconciliation

Data of the fiscal reports should be internally consistent and reconciled with relevant data from other sources. Transparency requires final accounts should be fully reconciled with subsidiary records maintained by the organization. Maintenance of basic records is a systematic way of tracking and recording changes in debt and assets and can provide a mean of checking overall data reliability. During certification of accounts of IR for the year 2010-11, Audit observed the following deficiencies:

- Total value of Railways Assets (excluding only the value of assets created from revenue) under various categories, whether financed from capital, Depreciation Reserve Fund, Development Fund or Capital Fund is shown in Appendix VII of Explanatory Memorandum on Railway Budget. On the other hand the Block Account – forming an annexure to the Annual Appropriation Accounts for the Indian Railways indicate the total including the value of assets financed from the Development Fund and Revenue as also the improvement element of the cost of assets financed from the Depreciation Reserve Fund. However on test check a mismatch amounting to ₹ 1427 crore (approx.) under the value of Land has been noticed in these set of Accounts.
- A report on the balances under the 'Debt Heads' forms part of the Finance Accounts. This report depicts the year end balances under 'Small Savings, Provident Fund', 'Deposits and Advances', 'Loans and Advances' and 'Remittances Inter-Government Adjustment accounts'. These heads are also depicted in the Balance Sheet of IR which forms part of the Appropriation Accounts. Audit observed that the balances for the year ended 31 March, 2011 shown in these two accounts do not tally and therefore need reconciliation. A disclosure to this effect is also required to be made.

  In response to Audit observation, IR stated that these differences would be reviewed. As Finance and Appropriation Account are the two main Accounts of the same organization, the differences in the two sets of accounts need to be recognized and reconciled.
- Audit observed that the principal component of Lease charges amounting to ₹ 2,793.38 crore was repaid to IRFC for leased assets during the year 2010-11 and was accordingly capitalized in the Block Account. However, instead of booking the entire expenditure to Rolling Stock Assets, it was bifurcated and booked to various Sub-heads namely Preliminary Expenses and Misc., Structural Engineering Works, Equipment Plant and Machinery, General Charges, Investment in Government Commercial Undertakings/Road Services etc. This resulted in the understatement of Capital Expenditure under Rolling Stock by ₹ 1,650.33 crore.

3.5.5 Internal Control System

Internal control system can be defined as a process by which an organization accomplishes specific goals or objectives. It is a means by which an organization's resources are directed, monitored, and measured. It plays an important role in preventing and detecting fraud and protecting the organization's resources, both physical and intangible. At the organizational level, internal control objectives relate to the reliability of financial reporting, timely feedback on the achievement of operational or strategic goals, and compliance with laws and regulations.

Audit observed that inadequacy and failure of internal control led to persistent irregularities in the accounts of IR. Some of these issues are discussed below:

- Ministry of Finance, (Budget Division), in May 2006, clarified that no expenditure can be incurred from the Consolidated Fund of India on a 'New Services'/'New Instrument of Service' without prior approval of Parliament through supplementary demands for grants.

  Construction of New Lines in Indian Railways is an independent activity and is charged to plan-head "New Lines". It was, however, seen that Railways were frequently undertaking construction of New Lines works as 'Material Modification' to already on-going works of New Lines as well as material modification to Gauge Conversion or Doubling, which are entirely a different activity, instead of getting them sanctioned as "New Services" in the budget. Review of on-going works revealed that 40 sections of New Lines Works (including 26 works pertaining to Eastern Railway), ranging between 5 km to 281 km (a total length of 1321.40 km as detailed in Appendix-3.1) which should have been got sanctioned as 'New Service'/'New instrument of Service' were being executed as material modifications to on-going works of New Lines as well as Gauge Conversion or Doubling or New Lines works. Besides this, 11 sections of Gauge conversion works with total length of 412.50 km and 74 km of doubling works in two sections were also taken up as material modification to works already under execution.

  IR failed to take approval of Parliament for new activity. This action of IR not only violates the procedure laid down for approval of new projects but also prevents their proper appraisal both economic and technical.
- Reimbursement of operating losses on Strategic lines- A reference is invited to Audit observation no. 3.6.2 (a) of Chapter 3 of C&AG of India's (Union Government) Report no. 33 of 2010-11 on Railways Finances wherein it was stated that Indian Railway has been claiming subsidy on five sections of Northeast Frontier Railway considering those as 'Strategic

Lines' without any notification.IR in response to audit observations had stated that necessary action was being taken to get the specific notification issued for these sections as strategic lines.
However during the audit of accounts of IR for the year 2010-11, it was again observed that the notification of these lines as strategic lines is still pending despite being pointed out by audit continuously for the last three years. Further, IR was still claiming "Reimbursement of losses on strategic lines" from Ministry of Finance considering these lines as 'strategic lines.'

IR in response to audit observation stated (March 2012) that the matter has been taken up with the concerned authorities and is expected to be resolved shortly.

- Subsidy claim on New Lines – Railway Convention Committee 1954 and subsequent Committees recommended that a moratorium should be granted in respect of the dividend payable on the capital invested on the New Lines during the period of construction and up to the end the fifth year of their opening for traffic. The dividend due on capital-at-charge has to be paid in full and exemption from dividend on this account is to be recorded as "Subsidy Received from General Revenues" under 'Miscellaneous Receipts' in the Accounts of the Railways. Thus, any unjustified deferring of dividend on New Lines results in unjustified claim and receipt of subsidy of the equivalent amount in the books of the Railways.

  A reference is invited to Audit observation no. 3.6.2 (b) of Chapter 3 of C&AG of India's (Union Government) Report no. 33 of 2010-11 on Railway Finances where in the excess claim of subsidy amounting to ₹133.45 crore by four Zonal Railways (SWR, NCR, ECoR and WR) in respect of ten lines in the year 2009-10. These claims were contrary to the mandatory recommendations of Railway Convention Committee regarding subsidies on new lines.

  IR in response to audit observations had stated that adjustment of subsidies would be carried out in the accounts of 2010-11. However during the audit of Finance Accounts of IR for the year 2010-11, it was observed that Zonal Railways did not comply with the assurance given during the previous year regarding reversal of excess subsidy. In fact they continued to claim subsidy on ineligible lines during the current year also. In response to audit observations South Western Railway and East Coast Railway stated that the adjustment of subsidy amounting to ₹ 614.01 crore in respect of six lines and one Road-over-Bridge pertaining to the period upto March 31, 2011 would be carried out in the year 2010-12.

- Audit observed that the IRFC (Volume-I) was needed to be updated/modified in a number of cases.
  - The Block Account is not being prepared in the format prescribed in IRFC (Volume-I). In reply, Ministry stated that the proforma of Block Account was revised in 1980. Since then the Block Account is being prepared in accepted form. The reply is not tenable as the revised proforma of Block Account has still not been revised/updated in provision of para 429 of IRFC (Volume-I) after the lapse of more than three decades.
  - City and Industrial Development Corporation of Maharashtra Limited (CIDCO) incurred an expenditure of ₹ 964.00 crore on Mankhurd-Belapur Railway Project upto 2010-11. The tripartite agreement entered into by IR with CIDCO and the state government of Maharashtra stated that these assets will form part of the assets of IR. Audit however observed that instead of opening a new head for accounting for creation of assets not financed directly through their own funds, this expenditure has been mis-classified.

In reply the Ministry stated that the expenditure not incurred by Railways should not be reflected in the Block Account and the matter was being examined. The reply of the Ministry is not tenable as the accounting for the asset created out of funds contributed by CIDCO is in accordance with the clause 11.11 of Tripartite agreement and needs suitable amendment in codal provision.

3.6 Conclusion and Recommendations

The FRBM Act, 2003 was passed to ensure transparency in budgeting. It was seen that IR was not following the FRBM Act and did not present any of the Statements of fiscal policy in Parliament as defined in the FRBM Act. It also failed to place a quarterly assessment of trend of receipts and expenditure before Parliament.

Part of the plan expenditure of IR is financed through extra-budgetary resources. This includes procurement of rolling stock through loan from IRFC. However the sources and uses of these funds is not clearly indicated in the budget documents.

It is seen that IR has made a number of implicit commitments to its PSUs. These commitments need to be disclosed as they have a significant impact on the liabilities of IR.

Audit observed that follow-up action on the announcements made in the Railway Minister’s budget speech were weak. No proper monitoring system appears to have been set in place, as seen from the gaps in the Outcome Budget. Further, the status of implementation of Railway Minister's budget announcements does not form part of the budgetary documents.

The accounting system followed by IR failed to provide an accurate assessment of arrear payments due. Further it is seen that the Codes and Manuals followed by IR needs to be updated. The classification system of IR did not allow administrative wise clear tracking of responsibility and accountability as use of resources in a grant is controlled by more than one administrative head leading to poor monitoring and control of expenditure.

Vide chapter 3 of Report of C&AG of India, Union Government (Railways) No. 33 of 2010-11, Audit had pointed out that IR failed to disclose significant accounting policies, while preparing financial Statements like Profit & Loss Account and Balance Sheet. No follow up action on this Audit Report has been taken.

Recommendations:

- ***IR should ensure that the FRBM Act is implemented. This would include presenting the following statements along with the budget :-***
  - ***Medium-Term fiscal Policy Statement indicating three-year rolling targets and policy regarding key fiscal indicators like revenue surplus i.e. balance between receipts and expenditure;***
  - ***Fiscal Policy strategy Statement for the current year indicating the policies relating to the prices of services provided , investment strategy for achieving the targeted growth rate,***
  - ***Macro-economic Framework Statement containing assessment of growth and revenue strategy and the amount of balances available under various Funds for maintaining /replacement of assets and achieving the targeted growth rate,***
  - ***A mid term review of receipts and expenditure incurred needs to be placed in parliament,***
- ***Supplementary budget should be presented in the same format as the original budget.***
- ***Follow up action on Railway Minister's speech on the budget needs to be strengthened. Further, the status of implementation of Railway Minister's budget announcements should form part of the Budgetary Documents.***
- ***The implicit commitments made by IR need to be disclosed in the budget as they have a significant impact on Railway finances.***

- ***To track administrative wise responsibility and accountability, a statement of authorization and expenditure under the control of each of the administrative head should be made a part of the budget document.***
- ***Complete information on funds raised through Extra Budgetary Resources needs to be disclosed so as to depict the actual capital expenditure incurred on creation of Railways' Assets.***
- ***Follow up action on audit observations pointed out in Chapter-3 of Audit Report no. 33 of 2010-11 has not yet been received. This would require IR to adopt standard based financial reporting for improved public accountability. To ensure transparency in reporting and proper presentation of financial statements, IR should prepare a road map for transition towards a system of accrual based general purpose financial reporting.***

(B. B. PANDIT)

New Delhi **Deputy Comptroller and Auditor General**

Dated

Countersigned

(VINOD RAI)

New Delhi **Comptroller and Auditor General of India**

Dated