Report No. 29346-IN

India – Orissa State Financial Accountability Assessment

May 30, 2004

Financial Management Unit
South Asia Region

Public Disclosure Authorized

Document of the World Bank

Government of Orissa

State Financial Accountability Assessment (SFAA)

A Collaborative Study of the Government of Orissa, DFID and The World Bank

May 30, 2004

CURRENCY EQUIVALENTS

Currency Unit = Indian Rupee (Rs.)
US$1 = approx. Rs. 45
1 Crore = 10 million
Rs. 1000 Crores = approx. US$222 million

FISCAL YEAR

April 1 - March 31

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PREFACE

The authors of a 1999 World Bank working paper concluded that there "is new empirical evidence that governance matters, in the sense that there is a causal relationship for good governance to better development outcomes such as higher per capita incomes, lower infant mortality and higher literacy."

In essence, good governance depends on establishing effective checks and balances on the exercise of official power, thereby holding public officials accountable so that they become true servants of the public they are supposed to serve. And transparency is the handmaid of financial accountability and control of the public purse. Too little attention has been paid to this fundamental prerequisite. The performance of public agencies should be publicly tracked and measured against clearly established benchmarks. This Assessment outlines ways to help such accountability mechanisms. It also points to the relationship between fiscal and fiduciary risk in the context of democratic governance.

As an example, the Public Accounts Committee of the United Kingdom noted in their *Report on the Proper Conduct of Public Business* that what was needed was "…a framework … (which) must include effective systems of control and accountability, and above all responsible attitudes on the part of those handling public money. It is important that the drive to provide improved services at reduced costs should be sustained and that this drive should not be stifled by unnecessary bureaucracy. At such time it is even more essential to maintain honesty in the spending of public money and to ensure that traditional public sector values are not neglected in the effort to maximize economy and efficiency."

The Government of Orissa believes that permanent improvements in public expenditure management will become possible only when the current fiscal crisis is resolved, but initial steps are necessary to put in place the foundation for improving the budgetary and financial accountability systems critical for managing the fiduciary risk at Orissa.

The SFAA for Orissa has been prepared for the Government of Orissa in coordination with the Department of Finance at Bhubaneshwar and with the approval of the Government of India. Officials of DFID participated in the key deliberations on this Assessment. Valuable suggestions on an on-going basis were provided by the GoO. The Department of Finance in Bhubaneshwar concurs with the main analysis, conclusions and recommendations of this Report as well as the accuracy of the information provided.

The Assessment includes recommendations which are aimed at assisting the GoO in preparing a Development Action Plan for strengthening public financial accountability.

For more information, please contact Mr. Vinod Sahgal at the World Bank (vsahgal@worldbank.org).

ACKNOWLEDGEMENT

This Assessment has been prepared by a SARFM task team led by Vinod Sahgal and Manvinder Mamak under the overall guidance of Ian Mackintosh (SARFM). The core team comprised of Aruna Bagchee (DFID), Colin Clark (DFID), Supriya Pattanayak (DFID), Ivor Beazely (SARFM), P. K. Subramanian (SARFM), Vinaya V. Vemuri (SARFM), Nisha Peris (SARFM), Marina Wes (SASPR), Mohan Nagarajan (SASPR), Santhanam Krishnan (SARPS) and Upasana Varma (SASPR).

The core team worked with the help of consultants from Orissa, Delhi and Washington. Uche Mbanefo guided the development of this Report. Advisors included Kapil Kapoor, V. J. Ravishankar, Salvatore Schiavo-Campo, Stephen Howes. The Assessment benefited from the peer reviews conducted by Amal Ganguli, John Hegarty, Michael L. O. Stevens, Mozammal Hoque, Nicola Smithers and Sovan Kanungo.

The Assessment benefited from a range of discussions with stakeholders at Orissa including senior officials of the GoO lead by A. K. Tripathy, K.C. Badu, P.K. Mishra and S. S. Patnaik. The Accountants General of the office of the CAG of India located at Orissa were extremely helpful in pointing the team to sources of information included in the annual reports of the CAG of India.

LIST OF ACRONYMS

alphabetically listed

AG	State Accountant General
AP	Andhra Pradesh
BCC	Backward Class Citizens
CAG	Comptroller and Auditor-General
CCA	Common Cadre Audit
CFAA	Country Financial Accountability Assessment
COPU	Committee on Public Undertakings
COSO	Committee of Sponsoring Organization of the Treadway Commission
CPAR	Country Procurement Assessment Report
DDOs	Drawing and Disbursing Officers
DFID	United Kindgdom's Department for International Development
DPCS	Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971
DRDA	District Rural Development Agency
FD	Finance Department
FY	Fiscal Year
GFRs	General Financial Rules
GoI	Government of India
GoO	Government of Orissa
GP	Grama Panchayat: Village-level tier of the Panchayati Raj Institution
IFAC-PSC	International Federation of Accountants, Public Sector Committee
IM	Initiating Memorandum
INTOSAI	International Organization of Supreme Audit Institutions
IPSAs	International Public Sector Accounting Standards
LAD	Local Area Development
LFA	Local Fund Auditor
MINFIN	Department of Finance
MLAs	Members of the Legislative Assembly
MoP	Memorandum to the President
OERL	Orissa Economic Revival Credit/Loan
PAC	Public Accounts Committee
PFA	Public Financial Accountability
PIL	Public Interest Litigation
PRD	Panchayat Raj Department
PRI	Panchayat Raj Institution
PS	Panchayat Samiti: Block-level tier of the Panchayati Raj Institution
RBI	Reserve Bank of India
SC	Scheduled Caste
SFAA	State Financial Accountability Assessment
SLA	State Legislative Assembly
ST	Scheduled Tribe
TI	Transparency International
UC	Utilization Certificate
UP	Uttar Pradesh
U&HD	Urban & Housing Development
ULB	Urban Local Bodies

ZP	Zilla Parishad: District-level tier of the Panchayati Raj Institution

ORISSA STATE: STATE FINANCIAL ACCOUNTABILITY ASSESSMENT (SFAA)

EXECUTIVE SUMMARY

1. The Country Assistance Strategy for India places emphasis on the need for modernizing public financial management and accountability systems and undertaking such diagnostic work as necessary to help build Government's capacity for better public sector management and external scrutiny. It calls for SFAAs to be carried out in all States where programmatic adjustment loans are being prepared in support of reforms associated with the management of the fiscal and fiduciary risks. Where feasible other donors are invited to participate. And Government is encouraged to help formulate a specific time bound development plan for implementing the recommendations of the Assessment.

2. Of India's 14 major States, Orissa has the second lowest per capita income and a growth rate of 3% against the national average of 5-6% per annum. The revenue deficit and fiscal deficit increased significantly over the years and stood, as of March 31/02, at Rs. 28 billion and Rs. 39 billion respectively (in previous year at Rs. 19 billion and Rs. 33 billion respectively) indicating the worsening financial position of the State. Capital expenditure for FY 02 is merely 8% of total expenditure. Interest payments consumed most of the State's own tax revenue. The State's own revenue base, as in the case of other Indian States, is too limited to support major improvement without central government and /or external assistance at least in the short and medium term. The State's own revenue comprises less than half of total revenue receipts.

3. The Debt burden is considered to be excessive. The Government's debt stock is equivalent to more than half of the total annual production of Orissa – for the rest of the country this ratio is below 25%.

4. The trend in growth of the Net State Domestic Product since 1996-97 has been around 12% p.a. whereas the outstanding fiscal liabilities have increased by 19% pa. With the debt burden of Rs. 280 billion at March 31, 2002 (Rs 120 billion at March 31, 1998), it is not an exaggeration to say that Orissa like many other Indian States[1] is in a fiscal crisis. Salaries, pensions and interest payments now more than exhaust total revenues, at 180% of the State's own revenues. The authorities are facing a `financial crunch' in the very practical sense of finding it difficult to pay the government's bills. Liquidity management overshadows almost all development efforts. The need for substantial Debt relief is under discussion with Government of India, as is the need to eliminate the revenue deficit.

[1] Corresponding figures for remaining States in India are not very different. For example, in Karnataka, the trend in growth of the Net State Domestic Product since 1996-97 has been around 12.49 % p.a. whereas the outstanding fiscal liabilities have increased by 18.65 % p.a., as per data published in - State Finances – A Critical Appraisal, A Research Paper Published by International Centre for Information Systems and Audit (iCISA) Office of the Comptroller & Auditor General of India.

5. There is an issue of legislative control of the public purse[2]. An estimated Rs 68 billion of accumulated "excess" expenditure (incurred by the government beyond budget allocations - pointing to excessive mismatch between receipts and expenditures as well as cases of diversion of funds between budget heads) remained to be authorized by the legislature as required by the Constitution of India.

6. Government of Orissa is developing a robust reform programme, several major policy decisions have been taken and implementation has begun in some important areas such as Service delivery and decentralization, anti-corruption, administrative and civil service reform, and public financial accountability. Implementation of certain key reforms will be necessary on a priority basis especially for civil service redeployment and right sizing without which fiscal crisis cannot be properly addressed. Similarly it will be necessary to complete the power sector reforms underway, further rationalize user charges, enhance tax and non-tax revenue and negotiate debt relief with the center. There is now a clear need to formalize a medium term fiscal framework (2002-07) that incorporates the above kinds of measures. It will also be necessary to broaden the reform programme to include a capacity building component under the Chief Secretary's umbrage, on financial management and public accountability.

7. The above reforms on the fiscal side are fully consistent with recommendations for strengthening financial management and public accountability being proposed in this Report. The GoO is aware that financial accountability in Orissa needs to be at par with best performing States. It also recognizes that improved financial control of public finances and capacity for safeguarding its assets will enhance growth and reduce poverty in the years ahead.

8. This Assessment is designed to ascertain and help mitigate the extent to which public funds in Orissa State are exposed to the fiduciary risk[3] of being applied (1) to purposes other than those for which they are intended or (2) without due consideration of economy and efficiency. It is argued that the success of the State's recent reform efforts aimed to improve its fiscal position is linked to the extent to which its fiduciary risk is mitigated.

9. The SFAA was carried out during the period February to May 2003 by the Bank and DFID in consultation with the GoO.

10. The GoO is commended for suggesting that the Assessment be conducted in as open a manner as possible and that the results be disseminated widely.

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[2] Over the last three years the amount of excess increased from Rs 12 billion in FY 98-99 to Rs 39 billion in FY 99-00 and further to Rs 64 billion by FY 00-01.

[3] The Bank's Charter (Article 111 Section V (b) of IDA's Articles of Agreement) specifies that: " The bank shall make arrangements to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other non-economic influences or considerations". In addition, DFID's definition of fiduciary risk refers to value for money as an important consideration.

11. The Indian Constitution and related central government-determined laws, rules and standards govern most of the key areas of public sector financial management and accountability such as budgeting, accounting, reporting and external audit. The State has nevertheless sufficient scope to *manage* and account for its resources, and so to determine the level of fiduciary risk to which they are exposed. Our analysis, as well as our recommendations for improving Orissa's management of public resources, fully reflects this juxtaposition of centrally driven *precept* and state- implemented management *practice.*

12. As a result of the gap between *precept* and *practice* revealed by the analyses in this Report, and illustrated particularly in Chapter XI, the fiduciary risk to public funds in Orissa is considered significant. The GoO concurs with this assessment. The immediate problem is not so much with laws, rules, regulations, and standards, although these are not always in line with the most modern national and international practice. The main problem is the failure to effectively *implement* the spirit behind existing laws, rules and regulations governing *basic* financial management standards and public accountability procedures, such as the preparation of timely accounts and reconciliations and follow up action on known deficiencies, many of which do compare favorably with the recognized principles supporting best practice in India and other commonwealth countries.

13. The SFAA points to the need for capacity building in almost every significant aspect of public financial accountability[4].

Specifically:

14. In **budget preparation and approval** the legal and institutional framework being applied at Orissa compares favorably with international as well as Indian best practice. Strengths include a well-established process, generally timely budget preparation, and an increasingly informative and realistic budget presentation.

15. Orissa's Budget has not been operating as a tool for effective management control. The fiscal deficit for FY 02 was 22% above Budget Estimates.

16. Opportunities for substantial systemic improvement exist in areas of enhancing budget realism, particularly in forecasting of all major sources of revenue and receipts; the need to disclose in the Budget Estimates departmental objectives and outputs in addition to funding requirements, improved disclosure of fiscal risk, major assumptions, and contingent and other liabilities such as pensions; tax expenditures (if significant) and improved legislative scrutiny of the budget *before* it is approved. Sufficient time could be allowed for a more informed debate on the budget and if necessary a vote on account could be obtained for meeting the requirements for the initial months of the fiscal year. The system of budgeting should be capable of fostering not only fiscal discipline, but

[4] The overall concept of Public Financial Accountability has been derived from Study 13 of IFAC - Governance in the Public Sector: A Governing Body Perspective; August 2001. IFAC endorses principles of governance including openness, integrity and accountability.

“allocative” and “use” efficiency as well – which calls for immediate improvements to the management and control processes.

17. In **budget implementation and monitoring**, the legal and regulatory framework is reasonably sound; systems and structures are well established; the GoO has sufficient access to technical and financial assistance; ongoing revenue monitoring has commenced, and so have proactive debt management and controls, in particular, the issuance of guarantees.

18. The implementation of the budget is marked by numerous distortions, many of which are traceable to the lack of realism in budget preparation, particularly revenue estimation. The central problem is shortfall in receipts leading to a liquidity crunch. Budget vs. Actual variation is significant.

19. Opportunities for further improvement remain in the areas of revenue assessment and collection; cash management; reporting on departmental outputs linked with budget inputs; promotion of departmental ownership of budgets; incidence of large “overspending” and “under-spending” in appropriations; and evaluation capacity for lessons learned.

20. The legal/ regulatory/ institutional framework for **internal control and internal audit** also compares favorably with the rest of India, but less so with international best practice. For instance, cash inflows are difficult to predict, and risk management has not in the past been a driving force for control over transactions with major financial implications. And most importantly, payments are made without reference to the availability of budget.

21. There is room for improvement in control over tax assessment and collection. Inputs rather than outputs, and outcomes are over emphasized in the day-to-day operating environment. Control of the payroll may be one area of risk that warrants attention given overstaffing across the government. Strict control over transactions and Civil Deposits in the Public Account is another. Control over guarantees however has been tightened recently. A concerted effort is being made to reduce unnecessary new hirings. Responsibilities of controlling officers and their Financial Advisors are well defined, and Secretaries (departmental heads) visit districts and projects. There is increased emphasis on the disclosure of physical progress in utilization certificates supporting claims for reimbursement of funds.

22. The institution of “Financial Advisors” in individual Departments has become largely ineffective. The incidence of internal control weaknesses is reported to be largely unchecked. There is, inadequate articulation and disclosure of specific departmental goals and objectives and how well they are achieved, lack of formal risk management through computerized integrated financial management information systems including exception reporting for high risk areas such as cost and productivity associated with the payroll; no departmental audit committees to mitigate fiduciary risk; internal audit does not report directly to the departmental heads; and departmental accounts are often not

reconciled monthly. In addition, asset management is very rudimentary across the government and the public sector.

23. **Accounting and financial reporting rules** comply with well-established national requirements, but not with International Public Sector Accounting Standards (IPSAS) for cash based accounting and financial reporting. Assets and Liabilities are not fully recorded. As a result the true and fair financial position of the State is not being presented to the public in the State's Annual Accounts. The GoO has full authority to improve its *internal* accounting and financial reporting arrangements. The State is encouraged to promulgate its standards of accounting in line with its requirements for decision making at each major department. 'Accounts at a Glance' – a recent innovation in public disclosure of the State's finances– is reasonably informative on trends in government expenditure. It is an important step in the right direction. Financial reporting formats are however unnecessarily complex. The information could be presented in a more simplified manner for Orissa's citizens. The current practice of reporting the State's deficit using numerous indicators reduces the overall understandability of this document. For example, providing four indicators for deficit may be more than necessary, i.e., Primary Deficit, Fiscal Deficit, Revenue Deficit and Budgetary Deficit (refer 'Accounts at a Glance')

24. There is room for improvement in the whole area of net-worked computerization across departments linked to the Accountant General (AG); discontinuance of the practice of holding funds outside the consolidated fund of the State to avoid their lapsing; providing explanations for large "overspending" and "under-spending"; more timeliness in financial reporting; and the need to place simplified monthly departmental and aggregate quarterly financial statements on the web.

25. The legal/ regulatory framework for the financial management of **State Owned Enterprises** (SOEs) is reasonably sound, but again, as in so many other links in the financial accountability chain, is not functioning as intended. Information on the status and needs of the SOEs including those that should be privatized has been compiled, and a reform process has been commenced. Its progress however is somewhat mixed. The will to enforce accountability is not evident. There is much room for improving corporate governance and public accountability.

26. The autonomy of the SOEs that will remain in the public sector is not fully assured. This is a serious limitation. Boards do not meet modern requirements of corporate governance and members are often appointed based on political affiliation rather than business competence[5]. The tenure of senior managers is also a consideration. The frequency of changes at senior levels is perceived to be unnecessarily high. Business plans are not readily accessible; performance reporting including reporting against established benchmarks is often lacking.

[5] Some believe that there is serious doubt on whether people with business competence can be persuaded to join such Boards unless the entire way of operating these enterprises is changed. Further, there would seem to be major constraints on the remuneration that can be paid to attract and compensate the right kind of people. Overcoming this requires serious political as well as bureaucratic commitment.

27. There are audit committees in high risk areas such as the power sector, but they do not adequately pursue issues relating to serious audit qualifications and their impact on the financial statements, nor do they focus the State's attention on the extensive weaknesses in internal control and internal audit at SOEs. Further, there are no periodic reports for the legislature on the extent to which SOEs meet their performance goals and the objectives of public policy; annual audited financial statements are often incomplete and grossly in arrears, despite increasing computerization; audit reports are nearly all heavily qualified; and executive response and follow up to external audit and the Committee for legislative oversight viz. the Committee on Public Undertakings (COPU) recommendations is not timely. The recommendations of this Assessment, if implemented, would strengthen the quality of corporate governance and operating performance of these entities. For example, the importance of more timely and proper accounting and auditing arrangements.

28. While the State has passed the requisite supporting legislation for the functioning of **Rural Local Bodies (Panchayat Raj Institutions)** (RLBs or PRIs in Hindi), the State's excessive involvement in their operations and unavailability of adequate financial resources is slowing up the pace of devolution relative to other Indian States such as Karnataka.

29. Financial accountability is getting due attention through on-going field visits; but resources available to PRIs to manage their affairs are inadequate to handle all the functions delegated to them by the State; there is an inadequate data base to determine PRIs aggregate financial position, or their operational outputs; external audits are heavily in arrear; there is a great need for training and computerization; and more importantly government officers, even in areas such as health and education, are not held fully accountable for their performance to locally elected representatives of the communities they serve.

30. **Urban Local Bodies** (ULBs) are self-governed, but not self-financed. Information with the State on the functioning of ULBs in terms of their operating performance is sparse. This may be because the ULBs themselves do not have such information readily available. Basic accounting records and formats have been established, so have detailed procedural controls for incurring and recording transactions. Many ULBs are however not using prescribed records/formats and are not adhering to detailed procedural controls. Budgets are normally prepared annually.

31. The ULBs own revenue base is very weak; the transparency of their financial position is hampered by the lack of audited financial statements showing their assets and liabilities; and there are arrears in independent auditing of their cash transactions. Auditors' reports indicate high fiduciary risk. There is considerable scope for training and computerization of accounting records and the need to introduce double entry accounting and more modern management practices is widely accepted.

32. **External Audit** of GoO accounts (as of all government accounts in India) is carried out by the CAG – an independent constitutional authority. The legal framework for

external audit is sound, and assures a level of independence and objectivity, comparable with some of the best systems in the world. Reports are increasingly relevant, objective, material, comprehensive and accurate. These reports, as in the case of other States, point towards high fiduciary risk to public funds on account of weakness in internal control including those associated with poverty reduction programs in rural areas.

33. Opportunities for further improvement exist in areas of timeliness, constructiveness, balance, greater emphasis on systems rather than individual transactions, and on preventive rather than solely detective measures. The Reports are not having the desired impact on the quality of Orissa's management of public resources. The greatest weakness is poor follow up and response to audit findings by the Executive. In addition there is a perceived lack of sufficient civil society interest in or debate on audit findings, and insufficient ongoing dialogue between the auditors and the departmental heads on concrete ways to improve public sector management and reduce fiduciary and fiscal risks. The GoO has indicated that the CAG should encourage a more modern approach to public audit reporting that requires the auditor's overall opinion on areas covered by audit to be stated along with individual irregularities in line with the evolution in international practice.

34. **Legislative Scrutiny** of public finances is based on an established institutional framework that is well implemented in a non-partisan, independent, and unanimous manner. Media coverage has been increasing. Its impact is, however, severely limited by the failure of the Executive to respond to the Public Accounts Committee (PAC) and the Committee on Public Undertakings (COPU) in a timely manner, the often dated subject matter reviewed by the Committees and reported upon by these Committees, limited research capacity for analyzing the cause of the problems uncovered, and most importantly, the *in camera* hearings with limited civil society or presence of technical expertise at their proceedings. Capacity building of the Committee's research support is a high priority.

35. **Access to Financial Information**. The functioning of the Government and its agencies has been characterized by lack of transparency and accountability across India partly due to the entrenched culture of bureaucratic secrecy underpinned by a long standing Official Secrets Act (OSA) and the government's detailed rules and limited public pressure for improving the quality and cost of service delivery. In this environment a system of governance and accountability prevails where sharing of financial information, on matters such as procurement and tax collection, among others, with civil society is often limited. It is in this context that the need to enhance public's ability to access Government financial information is crucial for ensuring participatory, transparent and accountable governance.

36. Speedy public access to financial information electronically has been widely accepted as a basic prerequisite for the effective functioning of good governance in democratic societies; there would be lessons to be learned from other Indian States such as Andhra Pradesh and Karnataka as well as the central government that are gradually moving forward in this relatively new area of public governance.

37. We believe that substantive improvements in implementation suggested in this Report will depend as much on technical improvements to systems that clearly require immediate bureaucratic attention, as on the *demand* from the public for better performance in terms of cost effective service delivery - whether in the State's power, health and education sectors or other local government services such as clean water, public distribution of food to the poorest of the poor, mass education and transportation.

38. To reflect India's centrally-mandated, but State-implemented fiduciary and management framework, the recommendations to strengthen Orissa's capacity for the management of its public resources and at the same time reduce fiduciary risk can be divided into four categories as follows:

- Category A: Five key themes that cut across government which we believe would have the greatest impact in improving public financial management and accountability. Pursuit of these Category A areas is recommended as areas that require the highest priority attention.
- Category B: Actions the GoO can take within 1 year to 3 years, without the need for Central Government approval.
- Category C: Other actions that could take 2 years or longer which do not require Central Government approval.
- Category D: Actions that would require Central Government approval or concurrence.

Pursuit of the above approach (Category A themes) cuts across practically all the aspects of public financial accountability and fiduciary risk discussed in this Report. They, and Categories B, C and D recommended actions are included in the list of main recommendations attached to this summary.

Strategy for the Development Action Plan (DAP)

39. The Orissa SFAA team encourages the GoO to take the next step to formulate the Development Action Plan (DAP) resulting from this assessment. This approach has the following advantages:

- The GoO is more likely to own the DAP it has prepared;
- The DAP is more likely to take account of any on-going public financial management reform program;
- The DAP is more likely to take full cognizance of the implementation capacity available in the GoO, especially with regard to realistic time estimates; and
- The DAP is more likely to be actually implemented, instead of remaining just a plan on paper.

40. Like almost all similar Assessments this SFAA has given rise to more than 70 recommendations. The Orissa SFAA team has in consultation with GoO, identified the

five most critical cross cutting themes from this study likely to have the most profound impact on public financial management and fiduciary risk in the State, and strongly recommends them to GoO for early consideration. These are the Category A items. Categories B, C, and D recommendations (also attached to this Executive Summary), are provided to assist the GoO establish priorities and plans for implementation. This step is expected to be completed by the GoO by September of 2003.

Cross cutting Themes

Integrity and Financial discipline – *Enforcement*

- Enforce more consistently and effectively prevailing laws, rules, & regulations pertaining to public sector financial management

Improve enforcement of existing laws and regulations relating to assessment and collection of revenue, expenditure, timely finalization of accounts at all levels of government including for example response to inspection reports and audit paragraphs, PAC and COPU requests, and recommendations and enforcement of penalties for non-compliance where appropriate. However, responses should be directed towards overcoming and preventing repetition of shortcomings cited, and not merely defensive explanations of commissions and omissions. Reward those public servants that do regularly comply with the spirit of the laws and regulations governing public expenditure management. They should be encouraged with appropriate incentives, sufficient resources and full public acknowledgement of their performance.

Quality of Financial Information – *Computerization*

- Prepare, and begin to implement, a step-by-step program designed to create computerized accounting and management information systems to support performance based accounting, tracking, monitoring, reporting and evaluation across government departments and agencies

Elements of this program might include, for example: investment in modern computerized accounting and management information systems across departments and agencies; computerization and net-working of the treasuries accounting and management information systems of the State Government, linking them with the AG's accounting and financial reporting system; and computerization of the accounting systems of PRIs, ULBs and SOEs as necessary.

Mind set that accepts openness – *Transparency*

- Open government's financial information and decision-making processes to civil society in line with evolving best practice in other Indian States.

Provide Orissa's civil society greater and more speedy access to financial information in line with evolving best practice in States such as Rajasthan, Delhi, Karnataka and

Maharashtra. Implement greater transparency, disclosure, performance orientation, and openness in both reporting and dissemination of financial and physical outputs' information across all the major areas of financial accountability discussed in this report (budgeting, accounting, financial reporting, internal control and audit, external audit, legislative scrutiny, and the management of PRIs, ULBs, and SOEs).

Accountability of Secretaries to the Government[6] – *Chief Accounting Officers*

- Hold "controlling officers" answerable for the operating performance of their departments, including action taken in response to public audit and legislative scrutiny, in line with the stated responsibilities of secretaries to the government.

Make all controlling officers (Secretaries to the Government) fully answerable to the public for mitigating fiduciary risk associated with all material transactions under their jurisdiction. Increasing the personal accountability of departmental secretaries is crucial not only as an incentive to their own better performance, but as protection against the occasional political pressures. This would involve for example clarifying the accountability of the bureaucracy as distinct from Ministers for meeting departmental objectives with due regard for economy and efficiency over and above the meeting of spending limits. In addition, build trust among all the key stakeholders involved with the management of public resources. For example, by the State Government relaxing its operational control over PRIs, with commensurate improvements in capacity for managing fiduciary risk so that devolution to the third level(s) of government may proceed as intended. The Chief Secretary is seen as the source for future leadership in this area[7].

Capacity Building – *Ability & willingness to accept change and move forward with conviction*

- Develop a dedicated capacity building program for implementing the recommendations of this Report

Design and implement a dedicated capacity building program (under the leadership of the Chief Minister) for strengthening public financial accountability of controlling officers and the quality of their management of resources. This would include clarification of accountability relationships and reporting requirements and simplification of existing rules and regulations, management and staff training programs, provision of appropriate tools for implementation of new information systems etc. with support from national and if necessary international resources, to implement all the four areas listed above. The state would benefit from the lead being taken by other Indian States that are in the

[6] Research Paper on Accountability of Secretary to Government of India prepared by the Consortium for Financial management of Public Systems, New Delhi India - 2003

[7] The Transaction of Business Rules point to the involvement of the Chief Secretary in crucial decision making areas of the Government. His role as the Head of the Administrative Cadre as well as Secretary to the Cabinet places him in a position of privilege to exercise control and promote public financial accountability. The Chief Secretary could lead an institutionalized review mechanism in the matters such as financial discipline, performance monitoring, response to external audit and improved functions of Financial Advisors.

process of modernizing their public financial accountability systems and related incentive structures.

41. A substantial commitment and sustained effort over several years will be required with the backing of strong political and administrative will. An effective focal point for capacity building within GoO needs to be identified by the Chief Minister in consultation with the Chief Secretary to facilitate the development and implementation of a time bound action plan (DAP) for implementing the recommendations of this Assessment, including, the five key themes identified and described in detail above as Category A items emerging from this SFAA.

Attachment to the Executive Summary

Action Plan

The prevailing system of accountability of the Executive to the Legislature, and of the Legislator to the people needs strengthening, to ensure adequate compliance with principles of sound financial management to secure optimal utilization of public funds. The success of the action plan proposed below will depend on the support provided by the Chief Minister, the Speaker of the Assembly and the Chief Secretary of the State of Orissa.

The GoO is requested to prepare and implement a Development Action Plan (DAP), duly prioritized, time-framed and costed, with implementation responsibility for each action assigned to a specific office. The five themes listed below as Category A are recommended to the GoO for consideration in the preparation of the DAP.

Category A

Cross cutting themes: Improvements expected to have the Highest Impact on Financial Accountability and Fiduciary Risk

Recommended to the GoO as core to the Development Action Plan (DAP)

- ③ Improve the enforcement of existing laws and regulations, including, for example, response to inspection reports and audit paragraphs, PAC and COPU requests, recommendations and enforcement of penalties for non-compliance.

- ③ Prepare and implement a program for the step-by-step computerization and networking of the accounting systems of the State Government, the PRIs, ULBs and SOEs, and linking GoO with CAG systems.

- ③ Implement greater transparency, disclosure, result and performance orientation, and openness in both reporting and dissemination of financial and output information across all the areas of financial accountability discussed in this report: budgeting, accounting, financial reporting, internal control and audit, external audit, PAC and COPU activities, PRIs, ULBs, and SOEs.

- ③ Hold “controlling officers” answerable for the operating performance of their departments, including action taken in response to public audit and legislative scrutiny, in line with the stated responsibilities of secretaries to the government.

- ③ Implement a capacity building program, including staff training, support with consultants, and other resources to implement the DAP prepared by the GoO as a result of this SFAA.

Category B

Actions Orissa State Government Can Initiate Immediately Without Central Government Approval.
1 year to 3 years

BUDGET PREPARATION & APPROVAL

1. Ascertain what specific progress has been achieved in implementing the government measures described in the White Paper of October 2000, specifically:

   a) present annual expenditure projections for the medium term to the Legislature;
   b) ensure that enhanced revenue forecasting procedures are instituted; and
   c) train State Government officers in budget formulation, tax administration and budget monitoring;

2. Ensure that all central government funds destined for projects in Orissa State (including official external funding) have started flowing through the Orissa Government budget and are being managed by the State;

3. Initiate the procedure of involving the line departments, including the financial advisers in the budgetary process more intensively, in order to share the ownership of the budget;

4. Forecast realistically on the following when preparing the Budget Estimates, while recognizing the constraint imposed by the Centre:

   a) external assistance; and
   b) tax and non-tax revenue receipts;

5. Suggest to the Speaker of the Assembly that Subject Committees in the Assembly are made more effective by endowing them with the attributes of Standing Committees in the Central Government, as described in this chapter. Departments of Education, Public Health & Works may also be brought in for examination by the Subject Committees; and

6. Provide sufficient time for a more informed debate on the budget and if necessary a vote on account could be obtained for meeting the requirements for the initial months of the fiscal year.

BUDGET IMPLEMENTATION & MONITORING

1. Train and build awareness to replace budgetary optimism with a more conservative approach;

2. Set up a tax research unit in the Department of Finance, to enable the introduction of a more scientific method for forecasting State revenues;

3. Train staff in the specific areas of mid term forecasting of revenues, scientific revenue estimation, and preparation of performance budgets and performance reports;

4. Enhance revenue by better enforcement. Further, tighten the assessment procedures, fix responsibility on the officers and take action against officials responsible for specific cases of underassessment pointed out in the CAG's reports;

5. Reduce incidence of Excesses and Savings; and

6. Disclose major assumptions and high risk areas, and also fully disclose contingent liabilities and the actuarial evaluation of pension obligations in the years to come, as a part of the budget document.

7. take steps to prevent deficient asset management, which leads to infructous/wasteful expenditure, which may be caused by inefficiency as much as being an indicator of corruption.

INTERNAL CONTROL & INTERNAL AUDIT

1. Speed up the review of rules and regulations as proposed by the Orissa Government White Paper of 2002;
2. Implement faithfully the existing rules and regulations, while awaiting the results of the review;
3. Introduce more Formal Risk Management through exception reporting for high risk areas;
4. Prepare Quarterly Analysis and Reports on variations between Budget and Actuals (Physical and Financial);
5. Involve Financial Advisors in all significant financial management decisions;
6. Make Internal Audit report directly to the Secretary; and
7. Provide proper orientation and regular training on modern internal audit technique.

ACCOUNTING & FINANCIAL REPORTING

1. Monthly accounts should be provided on each department of the Government, and a consolidated statement on the Government as a whole showing both actual and budget information within 6 weeks of the close of the month;
2. Define within six months how to reconcile or write off unreconciled differences between departments, treasuries, and others agencies or offices;
3. Discontinue unnecessary transfers from the Consolidated Account to "Deposits" in the Public Account;
4. Issue Annual Financial Statements of the State within six months following the end of the fiscal year and place monthly Financial Statements on the net;
5. Disclose in the Annual Appropriation Accounts Explanations for Savings and Excess (Grants); and
6. Include comparative information for the preceding year in all annual financial statements.

RURAL LOCAL BODIES (PRIs)

1. Expedite audits, start clearing arrears and take follow-up action.

URBAN LOCAL BODIES

1. Implement the format recommended by the CAG, as the accounts of the ULBs are maintained on cash basis and do not reflect the accrued liabilities. In this regard, improve completeness and timeliness of Cash Accounts and account for the assets of these bodies in a manner consistent with the requirements for sound asset management;
2. Place the audit reports before the Council on a timely basis and avoid future delay in audit of the ULBs; and
3. The Housing and Urban Development department should present a consolidated picture of the financial and physical performance of the ULBs. This report should be tabled in the legislature on an annual basis.

STATE OWNED ENTERPRISES
1. Define clearly the specific objectives of the companies and corporations. When these include the achievement of certain social goals, there should be a clear recognition and statement of the related costs for the proper appreciation of the financial and operating performance of the enterprise; 2. Make business plans visible and available on a timely basis for state government review; 3. Monitor the SOEs more effectively. Key performance indicators should be identified and periodical reports obtained and reviewed. The number of such performance indicators should be kept small. Review meetings should be chaired by the Secretary of the line department, at which the representative of the Department of Public Enterprises should be a regular invitee; 4. Launch a crash programme to bring the accounts of the entities up to date. The accounts that are produced and presented should be transparent, any tendency towards proliferation of notes should be discouraged. The notes should generally state the accounting policies adopted, deviation therefrom and such other matters as need explaining; 5. Insist that the effect of any qualifications, observations and comments of external auditors on the working results and financial position should be clearly stated. When such qualifications, observations and notes render the external auditors opinion ineffective, there should be no hesitation in denying an opinion on the accounts; 6. Establish effective audit committees as mandated by the recently proposed amendment to the Companies Act; 7. Discourage and curb the practice of appointing Members of the Legislative Assembly (MLAs) to the office of Chairperson; this has the potential to erode the autonomy of the Government companies and blurs the lines of accountability; 8. Respond better to external audit as well as the recommendations of the legislative committee. Individuals should be held accountable for their action. Senior Government functionaries should be held accountable for failure to enforce accountability; 9. Cause managements to introduce greater transparency in the Annual Reports to the shareholders which should be a candid assessment of the achievements and failures, strengths and weaknesses of the enterprise, and its systems along with measures that are being taken to improve the organization's financial and operating performance; 10. Publish an annual public enterprise survey. This should inter alia give the extent of Government financial involvement in the Government companies and corporations, their state of accounts and working results, achievement of objectives, results of external audit, recommendations of the legislative committee and follow up action taken. The survey should be a public document freely available and also put on the State Government website; and 11. Appoint Chief Executives and directors through transparent selection process with a 3-5 years tenure in order to induct professionals with proven track record.

EXTERNAL AUDIT

1. Senior officers should review the progress of settlement of outstanding inspection reports and paragraphs during their inspection of subordinate offices;

2. Empower Financial Advisors to comment on responsiveness of departmental officers to audit in the Annual Confidential Reports of the latter;

3. Officers of the Accountant General (Audit) and the Government departments should jointly review the pre-2000 inspection reports and consider whether these still need to be pursued;

4. Individuals should be held accountable for their acts of omission and commission; and action should be taken which is prompt, visible, and acts as a deterrent against similar lapses and wrong doings;

5. The AG (Audit) should write management letters to the Secretaries of the Government departments every quarter pointing out the cases of serious financial irregularities and system failures noticed during inspections. The management letter(s) should include the adequacy of follow up action taken on previous audit observations. Additionally, quarterly meetings should be held based on a structured agenda, between the AG (Audit) and each of the involved departmental Secretaries; and

6. Strengthen relationship with AGs in order to:

    - Improve constructiveness and timeliness of external audit report;
    - Ensure emphasis on systems rather than individual transactions; and
    - Initiate preventive rather than detective measures.

LEGISLATIVE SCRUTINY

1. Encourage enlargement of the role of AG (Audit) in following up cases of previous Audit Reports which the Committees may not like to pursue for detailed examination. In such cases the Committees may obtain specific recommendations of the AG (Audit) whether the departmental replies are acceptable and thereafter decide the further course of action. A stringent time schedule needs to be laid down and followed for this exercise;

2. Suggest to the Speaker that Committees may consider adoption of a similar procedure of examination of selected paragraphs even of current Reports. The Committee should discuss the most recent reports of the CAG as a matter of priority. The principle of "last in first out " is one way to address the issue;

3. Include in the annual confidential reports of the departmental officers, an assessment of the quality of response to the audit reports and recommendations of the Committees;

4. Provide the Committees with secretarial assistance at sufficiently superior levels commensurate with the nature, variety, and complexity of issues dealt with by them; appointment of experts on short term contracts may be considered;

5. Suggest to the Speaker that members of the Committees should have longer tenure; continuity and change can be ensured by stipulating that one third of the members retire every year; and

6. Civil society should be sensitized and involved in the accountability process. Transparency has its undoubted advantages. In more developed democracies the hearings of the Committees are open to the public. A beginning may be made by issuing a detailed press release at the end of each sitting of the Committee. An annual report of the work done by the Committees could also be presented to the House listing the accomplishments of Committee members and any constraints faced by them. Both these measures will ultimately promote greater involvement of the civil society in ensuring public accountability.

Category C

Other Actions Which do not require Central Government Approval, but which may or may not require External Assistance.
2 years or longer

BUDGET PREPARATION & APPROVAL

1. Introduce output/results information and accounting for results to complement the current, purely financial budgeting, to facilitate the assessment of the extent to which results of public expenditure are being achieved; and

2. Disclose in the Budget Estimates:

    a) intended outputs in the Demands for Grants;
    b) tax expenditure (if significant); and
    c) assessment of Fiscal Risk including impact of delayed decision making at the Centre..

BUDGET IMPLEMENTATION & MONITORING

1. Document the reasons for the many budget implementation distortions and problems associated with cash management, with a view to gradually removing them;

2. Further, build evaluation capacity for lessons learned;

3. Relax political pressure on the staff involved in the preparation of the budget; and

4. Prepare and disseminate performance budgets and mid-term reports on budget implementation at least once every 6 months in a more user-friendly format

INTERNAL CONTROL & INTERNAL AUDIT

1. Require all finance cadre officers to spend some time in their career working as finance advisers or heading internal audit units; and

2. Introduce a system of rewards for merit, and take timely action in cases of negligence or dereliction of duty.

ACCOUNTING & FINANCIAL REPORTING

1. Computerize the State's accounting system and network it with the AG's office; and

2. Provide training for existing staff.

RURAL LOCAL BODIES (PRIs)

1. Transfer all State Government functionaries working on PRIs to the PRIs; and in the interim make State officials answerable to local elected representatives;

2. Provide PRIs with the funds commensurate with the functions and augment the capacity of the PRIs to:

   - raise their own levels of revenues; and
   - learn from the experiences of other States, where the accountability of PRIs is increasingly defined in terms of sector outcomes and increased delegation of planning, implementation, monitoring and evaluation to the local governments;

3. Computerize data base on Aggregate Financial Position and Operational Outputs of PRIs and provide on-line public access to this data base; and

4. Review the need for and simplify the accounting, controls, reporting, auditing arrangements and training requirements of the accounting staff with a view to improving the effectiveness of the financial management system. Further, evaluate the viability and cost effectiveness of introducing computerization at each level.

URBAN LOCAL BODIES

1. Generate greater internal revenues to narrow the tax gap. In addition, the option of periodical revision of rates of the property tax should be exercised;

2. Enhance own revenue base;

3. Introduce accrual based accounting;

4. Computerize the accounting system and records of the ULBs; and

5. Train employees of ULBs in more modern financial management techniques associated with the need for more cost effective service delivery.

STATE OWNED ENTERPRISES

1. Establish an arms length relationship between the Government and the companies and corporations. The latter should have complete operational freedom in return for full public financial accountability operating on a timely basis;

2. Allow the managements sufficiently long tenures to perform effectively and to be held to account. The role of Government nominee directors should be clearly spelt out for determining the accountability of such directors; and

3. Cause the managements to introduce modern management practices, strengthen internal controls including internal audit and bring them on par with the best national practices.

EXTERNAL AUDIT

1. Clarify the financial accountability of Ministers as distinct from the Controlling Officers of departments and agencies of the GoO.

Category D **Actions Which Require Central Government Approval or Concurrence**
BUDGET PREPARATION & APPROVAL
1. Forecast realistically on the Central Assistance for State Plan when preparing the Budget Estimates.
EXTERNAL AUDIT
1. Addition of a clause in the CAG's (DPCS) Act, 1971 to make it obligatory for departmental officers to reply to draft audit paragraphs within the stipulated time frame.

CHAPTER I

INTRODUCTION AND BACKGROUND

A. INTRODUCTION

1. The Country Assistance Strategy for India places emphasis on the need for modernizing public financial accountability and undertaking such diagnostic work as necessary to help build the country's capacity for better public sector management and public scrutiny. It calls for State Financial Accountability Assessments (SFAAs) to be carried out in all states where programmatic adjustment loans are being prepared. Similar SFAAs are being undertaken in Uttar Pradesh (UP), Karnataka and Andhra Pradesh (AP).

2. A primary purpose of this SFAA is to explore avenues for capacity building in areas of public financial accountability[8] of greatest relevance to the State's reform agenda. This Assessment is designed to ascertain and help mitigate the extent to which public funds in Orissa State are exposed to the fiduciary risk of being applied (1) to purposes other than those for which they are intended or (2) without due consideration to economy and efficiency. It is argued that the success of the State's recent reform efforts aimed at improving its fiscal position is linked to the extent to which its fiduciary risk is mitigated.

3. Fiduciary risk and financial accountability in Orissa State are governed by centrally-determined laws and rules in such key matters as budgeting format, classifications and procedures; accounting regulations; financial reporting formats and conventions; and external audit. Yet the State, by the way it implements the centrally-determined structure and norms, has full powers to manage its resources, and so to determine the level of fiduciary risk to which they are exposed.

4. To reflect the co-existence of centrally-determined precept and locally-implemented practice noted above, our analysis will, wherever possible, try to distinguish between those factors within the State's control and those which are not. Similarly, our recommendations, and particularly the approach to the development of an Action Plan resulting from them, will respect this important distinction.

5. The specific objectives of the SFAA as defined in the Initiating Memorandum of January 2003 are:

- Provide systematically conducted analytical work and enhance the knowledge base on the public accountability arrangements in the State;
- Provide a forum for informed debates and discussions and thereby build a common understanding of the key fiduciary and development issues, and facilitate informed decision making on the improvement programs; and

[8] The overall concept of Public Financial Accountability has been derived from Study 13 of IFAC - Governance in the Public Sector: A Governing Body Perspective; August 2001. IFAC endorses principles of governance including openness, integrity and accountability.

- Support the exercise of Bank's fiduciary responsibilities by identifying the strengths and weaknesses of accountability arrangements in the public sector and the risks they pose to the use of public and Bank/ donor funds in the context of investment and adjustment lending.

6. The IM was approved by Bank management in January 2003. It was based on (1) a preliminary assessment of the systems of financial accountability[9] undertaken in August 2002, (2) subsequent discussions on the preliminary assessment with the Government of Orissa (GoO), (3) ongoing collaboration with DFID and (4) consultation with a number of stakeholders in Orissa including the accounting professions, officials of the Comptroller and Auditor General (CAG) of India located in Orissa and selected State legislators including the Speaker of the Assembly. The approval for the IM was based on the implicit understanding that the Assessment should be concluded in the WB fiscal year (FY) 03 on a phase one basis with a follow up in FY 04 to include "drill downs" as necessary in areas of highest risk such as the power sector, health, payroll, etc.

7. A Special Secretary in the Department of Finance was appointed by GoO to lead the Assessment on behalf of the State. This Assessment was undertaken with the consent of the Government of India (GoI). Officials provided advice to the SFAA team on an on-going basis during the conduct of the Assessment. The WB and the United Kingdom's Department for International Development (DFID) recommended to the GoO that a stakeholders workshop be held with private sector and civil society participation to guide the SFAA and assist the formulation of GoO's Development Action Plan. The detailed work for the SFAA was undertaken by SARFM with the assistance of local and national consultants selected in consultation with GoO and one international consultant[10]. The Assessment was carried out during the period February to May 2003. The work represents a collaborative effort of GoO, DFID and the WB[11].

8. The GoO is commended for suggesting that the Assessment be conducted in as open a manner as possible and that the results be disseminated widely.

9. The main sources of information for this Assessment include the (1) the Constitution of India (2) Legislation governing the powers, duties, etc, relating to the role of the CAG of India; (3) Rules of Procedure and Conduct of Business in The Orissa State Legislative Assembly (SLA) relating to legislative scrutiny of the public purse; (4) Subordinate legislation, and financial rules and regulations governing the raising, use, accounting and internal control of public funds and related responsibilities of officials regarding financial transactions incurred by the State and its autonomous bodies such as the public sector undertakings and enterprises; (5) legislation, rules and regulations governing rural and urban local government bodies; (6) Review of public documents and previous studies available at the Bank and other donor studies, as well as publications

[9] Draft Fiduciary Note SARFM November 2002

[10] The core SFAA team consisted of: Vinod Sahgal, Manvinder Mamak, Nisha Peris (SARFM), Colin Clarke (DFID), Dharam Vir, Rajagopalan Ramanathan, Pakanati Rao, Rama Rao, Nyayapathy Rao, Ullal Bhat, Vikesh Mehta, Seema Sachdev (Indian national Consultants) and Uche Mbanefo (international consultant).

[11] There are no other major international donors at Orissa, apart from DFID.

such as periodic white papers provided to the Bank by public sector officials; and (7) Discussions with stakeholders including concerned senior officials on procedures followed for budget preparation, budget execution, financial management, reporting, audit and subsequent scrutiny arrangements.

B. THE STATE OF THE STATE

10. Located on India's east coast, between West Bengal and Andhra Pradesh, Orissa is today the poorest of India's 14 major states, despite its rich endowment of mineral wealth, forests, lakes, rivers and lengthy coastline, and a rich and ancient history with vast untapped potential for both cultural and eco-tourism. With a population of 35 million, almost half of who are below the official poverty line, annual per capita income in the state today (about US$250 compared with all India's US$480) is the same as in Rajasthan and Madhya Pradesh 15 years ago, and Uttar Pradesh almost 10 years ago. Orissa has fallen behind the rest of India, experiencing slower economic growth since 1970, and especially in the 1990s. The poverty headcount (FY 00 47% compared with India's 26%) declined by 10 percentage points between 1987 and 1993, but progress slowed down between 1993 and 1999, in sharp contrast with developments in India as a whole. The poor in Orissa suffer from a dearth of income earning opportunities, inadequate basic public services, frequent natural disasters, and entrenched relations of social exclusion. The Scheduled Tribes (STs) constitute 22% of the total population in Orissa (compared to 8% in India) and 40% of the poor in the state. Regional disparity is marked, with a relatively well-off coastal area, having historically benefited more from trade and public investment, and an extremely poor and isolated interior, populated largely by tribal forest dwellers.

Figure 1: Total Receipts for FY 2001- 02 (Actuals) - Rs 112 billion

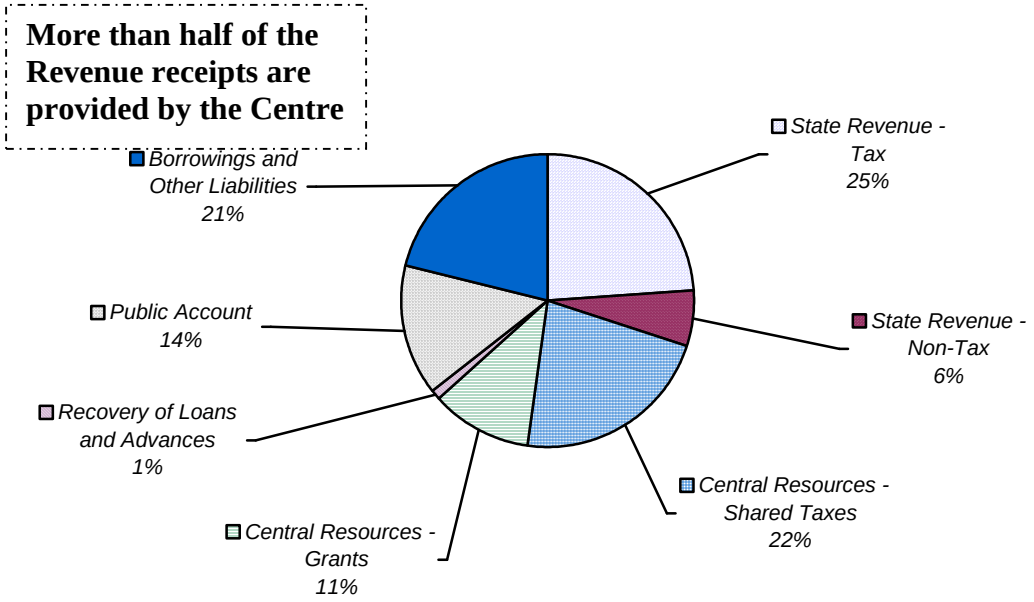


Table 1: Rupee Comes From (Consolidated Fund) 2001-2002

		Amount (Rupees in billions)	**Percentage**
1.	Central Resources – Shared Tax	24.67	22
2.	State Revenue - Own Tax	26.49	25
3.	Non – Tax	6.92	6
4.	Grants-in-aid from Centre	12.40	11
5.	Borrowings and Other Liabilities	23.52	21
6.	Public Account	16.16	14
7.	Recovery of Loans and Advances	1.32	1
T O T A L -		**111.48**	**100**

Source: Government of Orissa 'Accounts at a Glance 2001-2002'

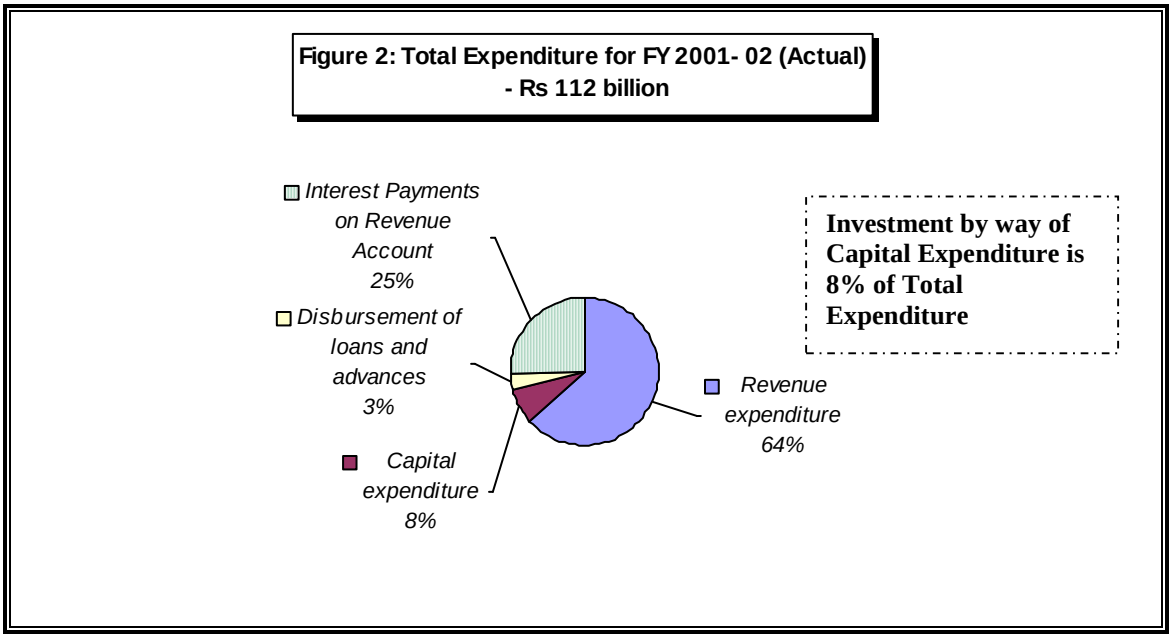


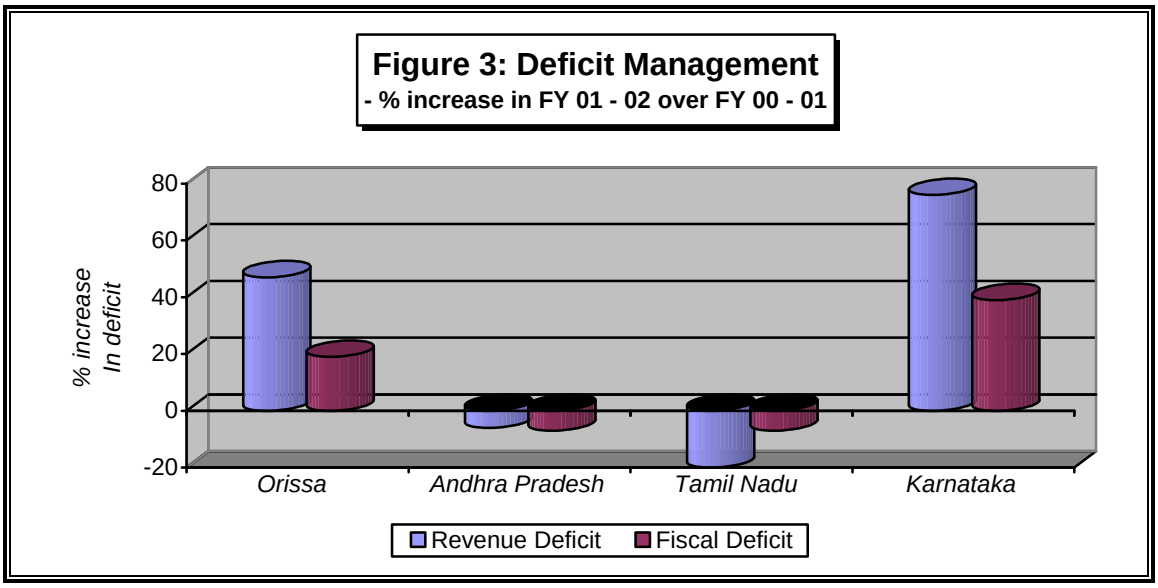
Table 2: Rupee Goes Out (Consolidated Fund) 2001-2002

		Amount (Rupees in billions)	**Percentage**
1.	Revenue expenditure	70.47	64
2.	Capital expenditure[12]	8.87	8
3.	Disbursement of loans and advances	3.79	3
4.	Interest Payments on Revenue Account	28.35	25
T O T A L -		**111.48**	**100**

Source: Government of Orissa 'Accounts at a Glance 2001-2002'

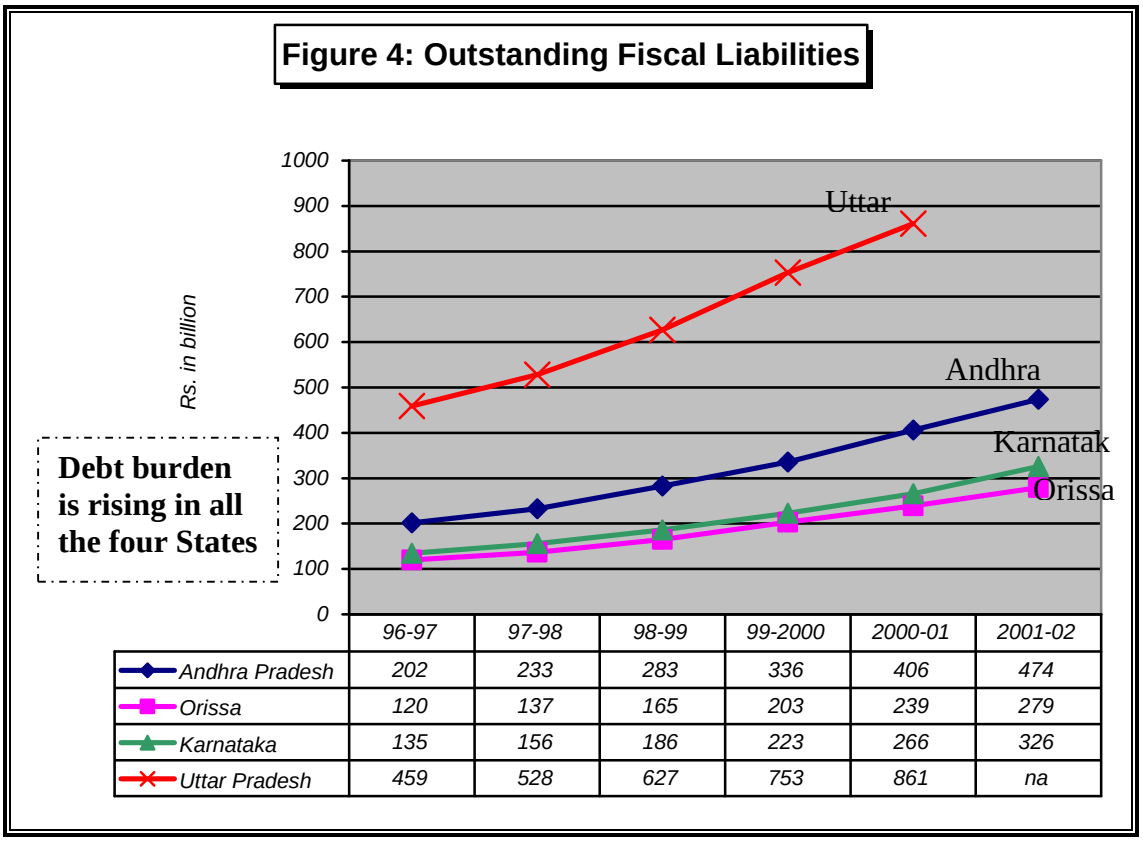
[12] Definition of 'Capital Expenditure' as given in Para 297 of Chapter 16, Section II of The Orissa General Financial Rules: "Expenditure of a capital nature is broadly defined as expenditure incurred with the object of increasing concrete assets of a material and permanent character. Expenditure on a temporary asset can not ordinarily be considered as expenditure of a capital nature".

11. It is necessary to have some basic idea of the fiscal position of the state to appreciate the financial accountability systems obtaining in the State of Orissa. The fiscal position of the State of Orissa is in a very bad shape. While it is true of most Indian States, the position in Orissa is significantly worse than most States. The State is in constant distress on liquidity front. Frequent resort is taken to Ways and Means Advances and Overdrafts. In the year 2001-02, these facilities were availed on 364 days. The expenditure on salaries, pension, interest payments and loan repayments exceeds total revenue by more than Rs. 7 billion per annum; growth of Revenue Expenditure is more than the growth of Revenue Receipts; assistance to grant-in-aid institutions has increased manifold. The salary and pension amounting to Rs. 1.58 billion was 59.36% of State's own revenue in 1980-81. It has now increased to Rs. 49 billion (156.04% of State's own revenue Rs. 32 billion) in 2001-02. The salary and pension and debt servicing add up to 110.03% of the State's Total Revenue, including receipts from the center. The huge revenue deficits lead to large borrowing to meet Revenue Expenditure crowding out investment needed for development and anti poverty programs. Capital investment has declined to 8% of total expenditure and 3.29% of GSDP in 2001-02 from 20.73% of total expenditure and 5.77% of GSDP in 1980-81.



Source: Data published by the Comptroller and Auditor General of India for FY 01 – 02
Note: Comparable Data for U.P. not available

12. The fiscal deficit of Orissa reached 10% of GSDP in 1999-00, the highest among India's major states, a result of lower-than-average revenue as well as higher than average expenditure (mainly on account of salaries and interest). The structural roots of the fiscal crisis in Orissa, as identified by the World Bank's analytical reports in 1996 and 1999, are: (a) an excessively large, ineffective and unaffordable civil service - a result of government acting as a de facto job creation agency in the past, (b) an excessive number of inefficient public enterprises, (c) large debt overhang resulting from central loan financing of successive state development plans and (d) inefficient revenue system with widespread tax evasion and low cost recovery for public services.



	96-97	97-98	98-99	99-2000	2000-01	2001-02
Andhra Pradesh	202	233	283	336	406	474
Orissa	120	137	165	203	239	279
Karnataka	135	156	186	223	266	326
Uttar Pradesh	459	528	627	753	861	na

Source: Data published by the Comptroller & Auditor General of India.

13. The debt burden has reached unsustainable proportions. The loans outstanding as on 31.03.2002 are Rs. 279 billion[13] which is 74% of GSDP compared to around 30% for all States average. (Even 30% level is considered unacceptable). In the year 2002-03, the estimated payment of interest (Rs. 29 billion) and repayment of loan (Rs. 8 billion) is 99.75% of State's estimated Own Revenue and 38.58% of the estimated Total Revenue.

14. In this deteriorating fiscal position, the State drew up a Medium Term Fiscal Plan (2000-01 to 2004-05) and signed a Memorandum of Understanding (MOU) with Government of India in October 2001 containing a series of measures that need to be taken to contain the fiscal deficit to reasonable proportions. The Eleventh Finance Commission devised an incentive scheme for the States to progressively achieve fiscal stability. The performance of the States is to be monitored by a single parameter for this purpose. The States are required to achieve a minimum improvement of 5% in Revenue Deficit (Surplus) as a proportion of their Revenue Receipt each year till 2004-05, the base year being the financial year 1999-2000.

15. The State of Orissa is serious about adhering to the commitments given in the MOU. It earned its share of incentive from Government of India for the year 2000-01, after achieving the desired fiscal parameter given by the Eleventh Finance Commission. But, it failed to meet the said criterion for the next year 2001-02. The bold fiscal

[13] CAG Audit Report (Civil) for year ended 31 March 2002.

measures[14] include surrendering all unfilled posts, freezing further recruitment in all departments except a few, cutting down non-plan expenditure by 10%, raising user charges, introducing new taxes like professional tax, widening the tax base, where possible, introducing zero based review[15] of projects costing more than Rs. 40 million and tightening the norms for giving guarantees. Suffice it to say that the State has initiated many positive fiscal measures, including some unpopular ones. The State has, however, a long way to go to achieve a modicum of fiscal stability and it cannot be achieved unless financial accountability issues are addressed adequately.

16. A preliminary Assessment conducted by the Bank in conjunction with preparatory work carried out in relation to the Orissa Economic Revival Credit/Loan[16] in 2002 indicated that the fiduciary risk in this State is on the high side despite the existence of a reasonably sound financial accountability structure in line with the one prevailing across India. The annual Reports of the Comptroller & Auditor General of India and periodic reports of the Public Accounts Committee of the State legislature provide considerable information on the need to substantially improve the management and control of public resources and return on public investment. Such reports also point towards the need for stronger *preventive* controls and public awareness of the costs of mismanagement and irregularities. Many public and private officials hold the same view.

Table 3: Fiscal Imbalances-Basic parameters

(Values Rupees in billion and Ratios in per cent)

	1997-98	1998-99	1999-2000	2000-01	2001-02	Average
Revenue deficit	(-) 9	(-) 23	(-) 26	(-) 19	(-) 28	(-) 21
Fiscal deficit	(-) 18	(-) 29	(-) 38	(-) 33	(-) 40	(-) 32
Primary Deficit	(-) 5	(-) 14	(-) 25	(-) 10	(-) 11	(-) 13
RD/GSDP	3	7	7	5	8	6
FD/GSDP	6	9	10	9	11	9
PD/GSDP	2	4	7	3	3	4
RD/FD	50	78	69	58	71	65

Source: Data published by the Comptroller & Auditor General of India - Audited Report (Civil) for the year ended March 31, 2002

[14] As the PREM team is monitoring the fiscal issues, it is not dealt with in detail in this paper.

[15] GoO has a Planning Department headed by a Senior official, that assesses all capital projects for their viability on a zero-based analysis.

[16] The proposed Orissa Economic Revival Credit/Loan (OERL) is the fourth World Bank sub-national operation in support of fiscal, governance and structural reforms by states of India. It is the first in a proposed series of 3 such operations during 2002-07 to support the medium-term program for economic revival by the GoO, India's poorest state with 35 million population.

17. The trend in growth of the Net State Domestic Product since 1996-97 has been around 12% p.a. whereas the outstanding fiscal liabilities have increased by 19% pa. With the debt burden of Rs. 280 billion at March 31, 2002 (Rs 120 billion at March 31, 1998), it is not an exaggeration to say that Orissa like many other Indian States[17] is in a fiscal crisis. Salaries, pensions and interest payments now more than exhaust total revenues, at 180% of the State's own revenues. The authorities are facing a `financial crunch' in the very practical sense of finding it difficult to pay the government's bills. Liquidity management overshadows almost all development efforts. The need for substantial Debt relief is under discussion with Government of India, as is the need to eliminate the revenue deficit.

18. The audited accounts of the State's finances show that all key fiscal indicators improved in 2000-01 (Table 3), but the improvement was not sustained in 2001-02, a year when central tax devolution fell seriously short of budget targets. Revised estimates published by GoO, and preliminary data at the Finance Department indicate a significant improvement in 2002-03, with the State's own revenues exceeding original budget estimates. The primary deficit (around 2% of GSDP) and the overall fiscal deficit (around 7.5%) are estimated to have declined significantly below their average level of the previous five years, according to unaudited information available in June 2003. The State Government's objective is to improve the fiscal situation further, to achieve a primary surplus and a declining debt ratio by FY 2006[18].

C. BACKGROUND

19. **Constitutional Relationships Between Jurisdictions.** India is a Union of States with well-defined distribution of legislative powers between different jurisdictions. The Constitution of India specifies the 'matters' on which the Union of India has exclusive powers to make laws (List I in the Seventh Schedule), the 'matters' on which States have exclusive power to make laws (List II in the Seventh Schedule) and the 'matters' on which both the jurisdictions have the powers to make laws (List III in the Seventh Schedule), with overriding powers in favor of the Union Government in the last case. The residuary powers rest in the Union Government.

20. The Union Government and the State Governments, each has its own separate funds, classified into:

> Consolidated Fund into which all revenue receipts and capital receipts are credited and from which all expenditure is to be met.
>
> Contingency Fund which is in the nature of an imprest account with the Union President or the State Governor to meet temporary and unforeseen expenditure pending its authorization by the concerned legislature.
>
> Public Account into which other moneys are credited and from which disbursements are made. This is in respect of moneys for which Government acts as a banker.

[17] Corresponding figures for remaining States in India are not very different. For example, in Karnataka, the trend in growth of the Net State Domestic Product since 1996-97 has been around 12.49 % p.a. whereas the outstanding fiscal liabilities have increased by 18.65 % p.a., as per data published in - State Finances – A Critical Appraisal, A Research Paper Published by International Centre for Information Systems and Audit (iCISA) Office of the Comptroller & Auditor General of India.

[18] Information relayed by the Bank's PREM team.

21. No amount can be withdrawn from the Consolidated Fund except under the authority of the concerned legislature by way of an Appropriation Act. Any amount taken as advance from the Contingency Fund shall be recouped to it. Audit of the Accounts of the Union and the States is a matter included in the Union List; hence there is a common Supreme Audit Institution called the Comptroller and Auditor General of India, for the audit of the accounts of the Union and State Governments.

22. The powers to levy taxes and raise revenues flow from the distribution of legislative powers between the Union and the State Governments. No tax can be levied except by law made by the appropriate legislature.

23. In terms of the powers to raise resources, the Centre has a predominant position. Taxes on income both for individuals and corporate entities, vast majority of excise duties and tax on import and export of goods, service taxes etc., are within the domain of the Union. Taxes on consumption, trade and profession, registration and transfer of property are assigned to the States. The taxes assigned to the Union are comparatively more elastic and buoyant and yield higher revenues creating a vertical resource imbalance between the Union and the States.

24. Recognizing the asymmetry in the assignment of tax powers and expenditure responsibilities, the Constitution has envisaged a transfer of resources from the Union to the States. This structured revenue sharing arrangement not only attempts at vertical equity, it also provides States with additional resources to meet their expenditure obligations.[19]

25. The Constitution of India prescribes the transfer of Funds from the Union Government to the State Governments by way of: devolution of a prescribed percentage of the net proceeds of specified Central Taxes; grants-in-aid to the State Governments to meet the costs of approved schemes; non-plan assistance as recommended by the Finance Commission. The Union Government also provides assistance for the State Plans and assistance for the centrally sponsored schemes. The allocation of funds between States is governed by a number of considerations, including equity and performance. Of late, equity considerations have been given significant attention[20].

26. Both the Central and the State Governments have the powers to borrow on the security of their respective Consolidated funds, but a State Government requires prior permission of the Union Government to raise any loan if it has any outstanding Union Government loan or guarantee. Both the jurisdictions are empowered to give guarantees. Although the constitution envisaged the imposition of ceilings on the amounts of loans

[19] Source: Page 1, Paras 1.3-1.4, State Finances – A Critical Appraisal, A Research Paper Published by International Centre for Information Systems and Audit (iCISA) Office of the Comptroller & Auditor General of India.

[20] "…In the last twenty years, however, covering five Finance Commissions, efficiency has generally been ignored and equity considerations have had the precedence. Tenth Finance Commission for the first time accorded a weight of 10 per cent to tax effort as an efficiency recognizing parameter, which again got reduced to 5 per cent by the Eleventh Finance Commission." Source: Page 2, Para 1.7, State Finances – A Critical Appraisal, A Research Paper Published by International Centre for Information Systems and Audit (iCISA) Office of the Comptroller & Auditor General of India.

and guarantees, no such ceilings have been prescribed so far. The States cannot borrow outside the territory of India.

27. The GoI has floated several small savings schemes. Eighty per cent (sometimes even 100%) of the collections under these schemes are passed on to the State Governments by way of loans. The GoI has also established a National Calamity Relief Fund from which funds are provided to the State Governments to meet expenditure on major calamities such as floods, cyclones, drought, etc.

28. By amendments to the Constitution, Urban Local Bodies (ULBs), and Rural Local bodies (RLBs) (Panchayat Raj Institutions), assisted by the State Governments, have also been given recognition, with powers to raise their own resources.

CHAPTER II

BUDGET PREPARATION AND APPROVAL

A. INSTITUTIONAL FRAMEWORK

1. Article 202 of the Constitution of India requires a statement of the annual receipts and expenditure of the State to be laid before the State Legislature. This Annual Financial Statement, popularly known as the budget, includes receipts and payments of the ensuing year, as well as a revised budget for the current year. The Orissa Budget Manual, although outdated (see below), is a good comprehensive document, with definitions and instructions for budget preparation, legislative approval, control of expenditure, re-appropriations, supplementary estimates, and procedures for after the close of the year. It also contains appendices dealing with procedures in the Orissa Legislative Assembly, list of items charged on the Consolidated Fund, budgetary provisions of the Constitution, etc. In addition, the State issued supplementary guidelines on October 31, 2002, for formulating the budget for 2003-2004[21].

2. The legal and regulatory framework is very good, and compares favorably with good international and Indian practice. It is transparent, provides for effective participation by all line departments, and makes it obligatory for them to own the budget and implement it faithfully. The budget manual is very clear about the role of all the parties in framing the budget and implementing it. The laws and regulations are also faithfully observed in practice. The Budget Manual, however, is badly in need of updating. Numerous additions have been made over the years, but obsolete provisions, such as references to relations with England, which seem to date back to colonial times, have not been deleted.

B. BUDGET CONSTRUCTION AND APPROVAL

3. As in most countries, the budget is put together through a combination of a “top down” and a “bottom up” approach. The Finance Department fixes the budget ceiling for both plan and non-plan expenditures, but the line departments prepare their own budgets, which they forward to the Finance Department, for consolidation into the State budget. The Finance Minister presents the budget document to the Assembly on a date prior to the start of the fiscal year, and determined by the Governor. After a period of not less than two days, the Assembly discusses the issues of principle in the budget. Not less than ten days thereafter, the Speaker allots not less than 14 days for discussion of all the demands for grants. At the end of the allotted period, the Speaker puts to the vote all remaining issues. The Finance Minister then moves an Appropriation Bill, seeking the legislature’s approval for the withdrawal of the money from the State’s Consolidated Fund.

[21] The Orissa State fiscal year, as for all governments in India, runs from April 1 to March 31

C. LEGISLATIVE SCRUTINY AND APPROVAL

4. The State Legislature has many committees to examine many issues in depth. Two types of committees deal with budgetary issues. They are **Subject Committees** and the **Estimates Committee**. Four Mohan Nagarajan (PREM), have been formed dealing with high spending departments, namely Agriculture, Water Resources, Rural Development and rural local bodies (Panchayati Raj). They scrutinize budget allocations, and review plans or projects referred to them by the House or its Speaker.

5. The seven-member Subject Committee is not permitted to examine or investigate matters of day-to-day administration. It can recommend re-allocations within a budget ceiling, or reductions in allocations, not an increase in an allocation. It is chaired by the Minister whose budget is under review; has only ten days to review the budget, and no secretariat; receives minimal information from the department being reviewed; and is generally ineffective from the point of view of budgetary control or accountability. By contrast, Standing Committees of the Central Government are reported to be more effective. They send out an exhaustive questionnaire seeking information on all aspects of functioning of the department. They are chaired by a Member of Parliament (not the Minister); hold comprehensive and intensive discussions for which four weeks are available; are serviced by a good secretariat, and the intensity of their discussions forces the Secretaries to own the budget and feel responsible for implementing it. The Orissa State Subject Committees would be far more effective if they functioned more like the central government Standing Committee.

6. The twelve-member **Estimates Committee** is elected by the Assembly every year, and reports on possible improvements in the organization, efficiency or administrative reform consistent with the policy underlying the estimates; suggests alternative policies to promote efficiency and economy; examines budgetary layout; and recommends form of budget presentation. No minister can be a member of the committee. The committee can continue examination of the estimates throughout the year and passing of the budget is independent of this committee's examination. The examination is in depth but more useful from the policy and performance point of view than from a budgetary perspective.

D. CHARACTERISTICS OF THE BUDGET

The budget consists of three parts namely; Consolidated Fund, Contingency Fund; and Public Account (all defined in Chapter I above)

7. All expenditures are classified as under:

- revenue (i.e., recurrent) and capital (i.e., investment);
- voted (i.e., subject to legislative assembly vote), and charged (i.e., not subject to legislative assembly vote, for example, salaries of State Governor, Speaker of the SLA, and other specified officials); and

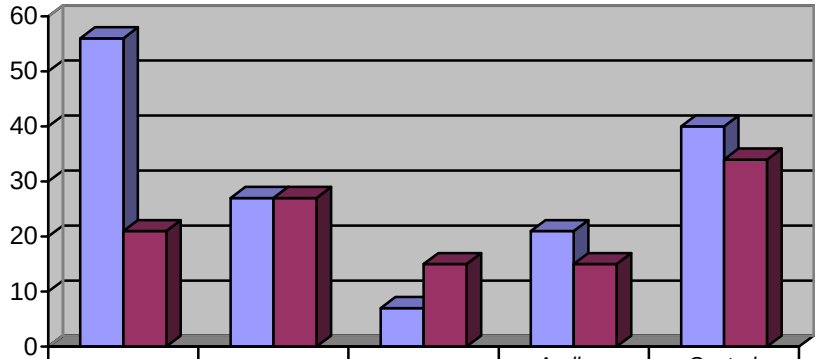
- plan (i.e., included in the development plan), and non-plan[22] (i.e., not so included).

E. COMPREHENSIVENESS

8. Until now, the main exclusions from the State budget have consisted of funds paid directly by foreign donors (increasing from about Rs120 million[23] in 1996/97 to more than Rs 870 million in 2002/3), as well as the central government (about Rs 6 billion a year) to entities within the State. This bypassing of the State budget was done in an effort to prevent the funds from being diverted to other uses, given the State's serious liquidity problems. The Central Government has decided to pass all its funding through the State budget, with effect from April 1, 2003. It has not been possible at this time, however, to confirm whether this is actually happening or not.

F. REALISM

Figure 5: Deficit Management FY 01 - 02
Actuals - % increase over budget estimates



	Orissa	Tamil Nadu	Karnataka	Andhra Pradesh	Central Government
Revenue Deficit	56	27	7	21	40
Fiscal Deficit	21	27	15	15	34

Source: Data published by the Comptroller and Auditor General of India for FY 01 - 02

9. Lack of realism has been one of the weakest characteristics of the budget. There seems to be a compelling wish to expand the size of the Plan every year, without reference to the availability of resources. This is said to be driven by the political masters and encouraged by the members of the Legislative Assembly, as more expenditure is

[22] the 'Plan/ Non-plan distinction' has been introduced by Indian national polity, and applies to all States and the Central Government.
Note: This is an All-India issue not dealt with in this SFAA
[23] Source: Pg 17, Table on "Receipt of External Assistance of EAP implementation in Orissa without being routed through State Budget from 1996-97 to 2002-03 (as on 31.12.2002)" Orissa Budget at a Glance, 2003-04, Finance Department, Government of Orissa

associated with more development (not true in most cases). The ambitious Plan size makes the budget unrealistic and causes undue stress to the fiscal position.

10. Another example of this lack of realism is the inclusion in the budget of many projects for which external funding has been requested, but not confirmed. The budget document for 2003-2004 mentions that some (10 out of 20) of the projects are in the pipeline (36.7% in value). Some of them were stated to be in pipeline the previous year as well. "Savings" are shown against these projects when they do not materialize within the year. Of the Rs. 10.5 billion of external assistance budgeted in 2002/03, only Rs. 4.3 billion was actually received by end of February 2003 (one month to the end of the fiscal year). The average external assistance received in the last five years has been around Rs.4.2 billion, and yet the budget for external assistance in 2003/04 is Rs.11.7 billion, clearly an over-estimate. This could be avoided by including only those projects in the budget, which have reasonable chances of being approved in the current year.

11. The Audit Report for the year ending 2001 mentions the case of the Department of Water Resources where the budget of the entire department was finalized, even though the concerned department failed to send its budget proposals to the Department of Finance. A similar instance involving the Works Department was observed in the subsequent year. This was done to avoid holding up the entire budget of the State, but it points to a certain lack of discipline in the budgetary process

12. Other examples of unrealistic budgeting include:

- over-estimation of the share of central government taxes that will be received by the State; (for example in 2001/02 about Rs. 32 billion were budgeted, but only about Rs. 26 billion received; in 2002/03 Rs. 35 billion budget was revised downwards to Rs. 31 billion); and

- finalizing the State plan (by the central Planning Commission) during the course of the fiscal year instead of prior to the presentation of State budget, thus leaving open-ended the amount of that plan that would actually be included in the current year's budget.

13. The above factors make the budget unrealistic, and impossible to implement as passed.

G. OTHER BUDGET PREPARATION ISSUES

- Lack of a Medium Term Framework

14. The budget is still prepared as an annual exercise, and is not directly related to any ongoing plan of receipts and payments. A rolling budget covering a minimum of three years, of which the current year's budget is the first year, is preferable.

- Need for Output or Results Information

15. All budgeting is still done in purely financial terms, with no related information disclosed on expected outputs or results. The State should introduce, at least for its major departments and its capital budget, disclosure of performance or output targets, which would enable the State to judge the extent to which it is achieving departmental objectives of expenditures.

H. STAFFING ISSUES

16. Over-staffing in overall numbers is the issue across the entire public sector. However, appropriate expertise is not always available at the right place at the right time. There would appear to be a need for training in budget planning techniques, especially in the area of accurate forecasting of receipts and payments. It is unclear, however, how much of the unrealistic budgeting has been due to lack of training, how much due to political pressure and how much due to insufficient timely information from the Centre.

I. ORISSA STATE BUDGET REFORMS

17. In an October 2000 "White Paper on Expenditure Management and Administrative Reforms" the GoO admits that "problems exist at all stages of the budget and expenditure management processes". The White Paper proposes the following remedies to the budgeting problems identified:

- The State has adopted a medium term framework approach, whereby an expenditure projection is formulated for the next five years, updated annually, and presented to the Assembly at the same time as the annual budget. It has not been implemented so far.

- The State claims to have "started introducing realism in revenue forecasting in the budgetary process, leading in 2003 and beyond to a systematic improvement in the accuracy of the forecasts". This is borne out by the revised estimates figures for FY 2002 – 03 for receipts which is in excess of the budget estimates by Rs. 2 billion. This excess amounting to about 5 % of total revenues reflects a more accurate and conservative original estimate. This has to be checked with actual figures when the accounts for the year are ready.

- The State also proposes to set up a training program for orienting the State Government officers in budget formulation, tax administration, and budget monitoring. GoO is said to have applied to DFID and the WB for assistance with this.

J. CONCLUSIONS AND RECOMMENDATIONS

20. Budget preparation and approval are based on a fairly good and comprehensive legal and regulatory framework, but the process still results in a budget whose

persistently over-optimistic projections of both capital expenditures and revenues, vitiate its chance of getting implemented as designed. To the extent that this lack of realism reflects political pressure, if any, rather than weak technical capacity, training alone will not solve the problem. There is therefore a need for better understanding between the politicians and the bureaucracy on the implications of unrealistic budgeting. What is needed is greater motivation and desire to improve current practices. The Controlling Officers have primary responsibility for improving budget realism.

21. To the extent that the inadequacies described above have a technical origin, the following measures are recommended:

i. ascertain what specific progress has been achieved in implementing the government measures described in the White Paper of October 2000, specifically:

   a) present annual expenditure projections for the medium term to the Legislature;
   b) ensure that enhanced revenue forecasting procedures are instituted; and
   c) train State Government officers in budget formulation, tax administration and budget monitoring;

ii. ensure that all central government funds destined for projects in Orissa State (including official external funding) have started flowing through the Orissa Government budget and are being managed by the State;

iii. Initiate the procedure of involving the line departments, including the financial advisers in the budgetary process more intensively, in order to share the ownership of the budget;

iv. introduce output/results information and accounting for results to complement the current, purely financial budgeting, to facilitate the assessment of the extent to which results of public expenditure are being achieved;

v. forecast realistically on the following when preparing the Budget Estimates, while recognizing uncertainty of Central flow:

   a) external assistance;
   b) tax and non-tax revenue receipts; and
   c) Central Assistance for State Plan;

vi. disclose in the Budget Estimates:

   a) intended outputs in the Demands for Grants;
   b) tax expenditure (if significant); and
   c) assessment of Fiscal Risk including impact of delayed decision making at the Centre;

vii. suggest to the Speaker of the Assembly that Subject Committees in the Assembly are made more effective by endowing them with the attributes of Standing Committees in the Central Government, as described in this chapter. Departments of Education, Public Health & Works may also be brought in for examination by the Subject Committees; and

viii. provide sufficient time for a more informed debate on the budget and if necessary a vote on account could be obtained for meeting the requirements for the initial months of the fiscal year.

CHAPTER III
BUDGET IMPLEMENTATION AND MONITORING

A. INSTITUTIONAL FRAMEWORK

1. The Budget Manual prescribes the norms for expenditure control, including the prohibition of any expenditure above appropriations. The Orissa General Financial Rules contain detailed internal control regulations, including a requirement to spend funds judiciously and to identify surpluses. Surpluses not re-appropriated to other expenditures within the same approved budget heading, must be returned to the Finance Department for the use of other departments, after legislative approval through supplementary budgets. Any excess spending is reported upon by the CAG, reviewed by the Public Accounts Committee (PAC), and regularized by the State Legislative Assembly. These regulations are in tune with the best international practices of reporting back to the legislature any deviation from the approved amounts.

B. BUDGET IMPLEMENTATION

2. The implementation of the budget is marked by numerous distortions, many of which are traceable to the lack of realism in budget preparation, particularly revenue estimation, discussed in the preceding chapter. For example, in 2001/2002 the State's share of central taxes was budgeted at nearly Rs.32 billion, but the State received only Rs. 26.5 billion. The 2002/2003 budget of almost Rs.35 billion has had to be revised downwards to about Rs.31 billion. But despite these experiences, the 2003/2004 budget still provides for anticipated receipts of Rs.34.3 billion from this source. It is to be noted that these likely figures are indicated by the central government to the state governments based on the central budget figures of receipts.

3. Lack of liquidity is a constant worry. The Finance Department (FD) controls the release of funds to the other departments strictly based on the availability of cash. This kind of constant cash rationing upsets the priorities fixed in the budget. It also causes Secretaries to disown responsibility for implementing the budget as passed. Other distortions in budget implementation may be summarized as follows:

- Resource-linked projects, accorded priority in cash rationing receive an initial installment, they have to give a Utilization Certificate (UC) for earlier installments before they can receive further releases of funds. Frequent inability to provide the UCs means the cash flow gets impeded.

- The money is received from central government mostly towards the end of the year. Unable to spend the money in a short time, and fearing lapse of funds, the unspent amount is kept in Civil Deposits Head in Public Account, and subsequently spent without legislative clearance thereby vitiating legislative control. Closing balances held in such accounts have grown from almost Rs. 2 billion in March 1997 to more than Rs. 6 billion in March 2001.

- The severe cash shortage is one of the reasons for large variations between approved and actual expenditure every year. These "savings" amounted to more than 10% of total budget allocation in 27 out of 42 budget heads in 2001-02[24].
- In 2000/2001, 14 line departments, which had "savings" of Rs. 19 billion surrendered only Rs. 5.6 billion. On the other hand, in 56 individual sub-heads, the entire allocations were surrendered, indicating slackness in budgeting.

- Starting of works for which funds fail to materialize, results in arrears in payment due to contractors and presumably in stoppage/delay of the work. The size of the problem is reported to be large, though no reliable data are available.

- Re-appropriation of allocation from one budget head to another within the same Grant, introduced to enable the government to change its priorities during the year, appears to be excessive in both amounts involved and number of grants, thereby contravening the legislative intent.

- Supplementary budgets, often two in a year, represent another abuse of flexibility. The supplementary budgets as a percentage of the original budgets were 24 (1998-99), 22 (1999-2000), 16 (2000-01), suggesting poor budgeting.

- According to an external audit report: "Controlling Officers are responsible for ensuring that the control over expenditure is effective and to guard against rush of expenditure in the month of March. Test check by audit disclosed that in 19 cases, 52 per cent to 100 per cent of the total expenditure for the year 2000-2001 was incurred during the month of March 2001."

- The line departments do not receive from the State Accountant General (AG) timely or useful figures.

- Instead of monthly reconciliation of the departmental figures with AG's accounts required by regulations, most departments now perform the reconciliation only once a year. Furthermore, in 2000-01, 11% of all expenditures by value, representing 61 departments out of 377, remained unreconciled, even after the year-end, according to the Audit Report on Orissa[25].

C. CASH MANAGEMENT

4. Cash flow planning has been very poor. The Reserve Bank of India (RBI) allows each state (including Orissa) to draw funds up to specified limits as Ways and Means Advances to meet temporary cash shortages. When the limit is exceeded, the state goes into overdraft; and, if the overdraft is not repaid within 12 days, the RBI can stop all payments on behalf of the state. During the first ten months of 2002/2003 Orissa State was in Ways and Means status for 137 days, and in overdraft status for another 164, for a

[24] Source: Pg. 29, Report of the Comptroller and Auditor General of India, for the year ended 31 March 2002 (Civil), Government of Orissa
[25] In fiscal year 2002, 16% of the accounts were unreconciled.

total of 301 days out of 306, during which the State's receipts were insufficient to cover its payments. The constant liquidity crunch diverts the energies of senior state officials from creative and constructive activities to trying to get enough funds to pay salaries, pensions, and other urgent obligations.

5. Even the forecasting of the Ways and Means advance requirements is poor. For example, in 2001/2002, the State forecast Ways and Means requirements of only Rs. 20 billion, but ended up requiring more than Rs. 64 billion. The 2002/2003 forecast of Rs. 15 billion had to be revised upwards to Rs. 65 billion. In spite of this, the requirements for 2003/2004 are again budgeted at Rs. 15 billion. One gets the impression that the persons preparing these forecasts are in denial, and perpetually optimistic. Lessons learnt need to be recorded. Other examples of unrealistic optimism have been discussed above and in Chapter II. We recommend a two-pronged attack to solve this problem:

- a political decision to remove (or at least limit) political pressures on the staff involved in the preparation of the budget; and
- training and awareness building designed to replace budgetary optimism with a more conservative approach.

D. REVENUE ISSUES

6. Largely due to its agrarian economy, and the non-taxation of agricultural income across the whole of India, the State of Orissa does not generate its own tax revenue to the extent that many other States in India do. This situation makes it doubly important for the State to ensure efficient tax assessment, collection, and follow up of arrears.

Revenue Estimation

7. Until recently, revenue forecasting left much to be desired. Expenditure requirements were first worked out and thereafter the resources were estimated to service the expenditure. The receipts never materialized as estimated. The Finance Department (FD) now tries to work out the revenue estimates independently of the expenditure requirement by adding a "buoyancy factor" to the previous year's realization. The revenue estimates for the year 2002-03 have proved accurate, with actual receipts marginally higher than estimate. Apart from better estimation, widening of tax base, increasing user charges and better tax administration also helped. The following table illustrates the improvement in revenue (tax and non tax) collection with reference to estimate.

Table 4: Improvement in revenue (tax and non tax) collection

(Billion Rupees)

	Budget	Actual
2000-01	3.2	2.9
2001-02	3.7	3.2
2002-03	3.7	3.9*

* Revised Estimates based on GoO's internal figures

Despite the improvement noted above, the current methodology for forecasting revenues, based on applying a "buoyancy factor" to the previous year's receipts, is still more rule of thumb than scientific. We recommend that the GoO create, as soon as possible, a tax research unit, one of whose first priorities will be the introduction of a more scientific method for forecasting State revenues.

Revenue Monitoring

8. The State has a good system of monitoring the revenue streams. Every month the receipts of the previous month are compiled and reviewed by the Chief Secretary. The statement for the month of December 2002 showed revenues higher than forecast, and also higher than in December of the previous year. The external audit report for 2000/2001, nevertheless, revealed an underassessment of nearly Rs. 1.8 billion, about 6% of the State's total own revenue. We recommend a tightening of the assessment procedures, and action against officials responsible for specific cases of underassessment.

E. ASSET MANAGEMENT

9. The Orissa General Financial Rules give exhaustive directions on asset management procedures. However, it was not possible to do any field study on the asset management practices. The Audit Reports are replete with cases of poor maintenance of asset registers, particularly in the field offices. Good asset management requires maintenance of appropriate records and regular reconciliation with the books of account.

Box 1

Asset Management in GoO

By way of example, the following instances of deficient asset management are reproduced from CAGs Audit Report 2001-02

i) 1982 Indira Awas Yojana houses (for the rural poor) taken up for construction during 1990-99 remained incomplete rendering the expenditure of Rs. 22.2 million incurred thereon infructuous.
ii) Out of 29,458 houses reported complete under Credit-cum-Subsidy Scheme (for the rural poor), 23,307 houses were actually incomplete.
iii) Non-utilization of the available machinery due to improper planning led to loss of Rs. 52.9 million besides unproductive expenditure of Rs. 116.3 million due to poor inventory management in the Works Department.
iv) Abandonment/ non-completion of works led to wasteful expenditure of Rs. 259.5 million in the Works Department
v) Spare parts and stores valued at Rs. 98.6 million were procured by a Public Health Mechanical Division without tender and without actual requirements.

F. DEBT MANAGEMENT

10. The GoO is heavily indebted. According to the budget document for the year 2002-03, the total debt of the government is about Rs. 282 billion, more than half of it due to the Central Government. Between 2001-03 the debt grew by Rs. 35 billion – a clearly unsustainable rate of growth. The State does, however, have very good debt management

systems, in so far as repayment is concerned. Debt and repayment due dates are noted and followed up diligently. While the Accountant General automatically pays the loans of GoI without reference to the State on the fifteenth of every month, the State has also been paying back the other loans on time. This is very creditable, considering the perennial liquidity crunch.

G. CONTINGENT LIABILITIES

11. The State of Orissa has huge contingent liabilities[26] arising out of the guarantees it has given to many public undertakings, autonomous bodies and urban municipal bodies. As of February 28, 2002, the maximum amount guaranteed was Rs. 85 billion, while the outstanding guarantees were estimated at Rs. 53 billion. As many of these institutions are not financially healthy, there is a real risk of these contingent liabilities turning out to be real liabilities. The State has recognized this danger and has initiated many positive corrective steps, including the following:

- issuing comprehensive guidelines on guarantees;
- limiting guarantees to a few institutions meeting specified criteria;
- requiring Cabinet approval of any new guarantee;
- requiring every beneficiary to have finalized and audited its accounts for the two preceding years;
- embarking on a program to scale down the guarantees to 80% of their current level over a period of 5 years;
- recalling unused guarantees;
- providing detailed formats for reporting guarantees to the legislature;
- publishing details of guarantees in "Budget at a Glance" – a document tabled with the budget at the legislature; and
- setting up, with an initial contribution of Rs. 200 million, a Guarantee Redemption Fund to be managed by RBI.

H. BUDGET DOCUMENTATION AND REPORTING

12. Budget documentation has improved substantially, especially the 'Budget At a Glance'. The data on outstanding debt, guarantees, various financial ratios, social indicators and comparison with other States, are useful pieces of information. There is scope for including many other parameters, including for example physical progress along side the promises made in the budget at least on a few selected parameters. GoO's White Paper on the fiscal reform (see Chapter II) contains an honest appraisal of the problems, the causes and possible solutions, including the tough measures needed. The publication of the White paper required official honesty and political courage which should be acknowledged.

[26] Contingent Liabilities include liabilities arising out of arbitration proceedings/awards in respect of major works contracts. They also include Letters of Comfort, if any.

13. The budget and all the associated documents are placed in the official website of the State. They are, however, difficult for a common man to understand. Also, as pointed out in the preceding chapter, they contain only financial figures, with no indication of physical achievements, results, or any other performance indicators. Furthermore, effective monitoring of budget implementation requires reporting more frequently than once a year.

Box 2

Innovation from Karnataka

A recent but important innovation introduced in Karnataka is the 'Action Taken Reports' (ATRs) on promises made in the previous years budget speech.

14. We recommend that the government provide performance information for all the departments in a more user-friendly form, and report, at least once every 6 months to enable the legislature, as well as the average reader, to understand, and meaningfully discuss the purpose of proposed expenditures and have meaningful discussions on policies and programs.

15. External reporting, external audit, and other aspects of transparency are discussed in subsequent chapters of this report.

I. STAFFING ISSUES

16. As pointed out in the preceding chapter, the issue in GoO is over-staffing. 1.6% of the State's population work for the State, compared with 0.8% for the whole of India. However, we recommend training for the staff in specific areas, such as mid term forecasting of revenues, scientific revenue estimation, and preparation of performance budgets and performance reports.

J. CONCLUSIONS AND RECOMMENDATIONS

17. The unrealistic budget preparation practices noted in the preceding chapter, have, until now, resulted in a budget implementation experience bordering on the dysfunctional. The State Government has, however, initiated many bold measures to try to redress the situation. In addition to the Government measures mentioned in the preceding chapter, and those discussed above with regard to loan guarantees, GoO has (according to its White Paper) established a Fiscal Reform Cell in the FD to monitor the budgetary reform process. The Government has also introduced such measures as zero-based review of projects, whereby all projects costing above a certain amount are reviewed in a one-off exercise, and all those found incapable of yielding returns above a certain threshold are closed down.

18. In addition to the above measures, and others announced in the GoO 2002 White Paper, we recommend the following actions in conjunction with recommendations in the previous chapter:

i. document the reasons for the many budget implementation distortions and problems associated with cash management, with a view to gradually removing them.

ii. Further, build evaluation capacity for lessons learned;

iii. relax political pressure on the staff involved in the preparation of the budget;

iv. train and build awareness to replace budgetary optimism with a more conservative approach;

v. set up a tax research unit in the Department of Finance, to enable the introduction of a more scientific method for forecasting State revenues;

vi. train staff in the specific areas of mid term forecasting of revenues, scientific revenue estimation, and preparation of performance budgets and performance reports;

vii. enhance revenue by better enforcement. Further, tighten the assessment procedures, fix responsibility on the officers and take action against officials responsible for specific cases of underassessment pointed out in the CAG's reports;

viii. reduce incidence of Excesses and Savings;

ix. prepare and disseminate performance budgets and mid-term reports on budget implementation at least once every 6 months in a more user-friendly format;

x. disclose major assumptions and high risk areas, and also fully disclose contingent liabilities and the actuarial evaluation of pension obligations in the years to come, as a part of the budget document; and

xi. take steps to prevent deficient asset management, which leads to infructous/wasteful expenditure, which may be caused by inefficiency as much as being an indicator of corruption.

CHAPTER IV
INTERNAL CONTROL AND INTERNAL AUDIT

A. INTERNAL CONTROL

1. GoO has a very elaborate and detailed system of internal control, which is documented in the Budget Manual, General Financial Rules, Delegation of Financial Power Rules and Treasury Codes, as well as in various office procedure manuals. Financial Advisors are located in every government department as guardian of internal control. They report to the Secretary of the Department.

2. The GoO has not articulated its standards for internal control. The International Organization of Supreme Audit Institutions (INTOSAI)[27] has developed standards for use in designing internal control systems, and as a guide for auditors in assessing these controls. These standards include:

- documentation, and recording, of all transactions and significant events, and the ready availability of such records and documents for examination;
- restriction of the authorization of transactions and significant events to only persons acting within the scope of their authority;
- no one person to be responsible for more than one of the following: authorization, processing, recording, or reviewing of transactions or events;
- competent supervision to ensure that management control objectives are achieved;
- limitation of access to resources and records to only authorized individuals accountable for their custody or use; and
- periodical comparison of resources with recorded amounts, to ensure accountability, the frequency of such comparison being determined by the vulnerability of the asset.

COSO standards go a step further, by stressing ethical values, competence, and self-discipline of staff at all levels.

3. In comparison with the international standards indicated above, the GoO regulations provide for:

- at least one supervisory level staff in even small offices;
- separation of responsibility for the ledger from responsibility for the cash book;

[27] Source: www.intosai.org/3_ INTCOe.html

- physical verification of cash, at least once a month, by someone other than the cashier;

- periodical inspection of field offices by controlling officers;

- quarterly visits of all districts and project inspection by the Secretaries;

- routine Treasury check of all bills for salaries, contingencies, and other office requirements;

- checks of Public Works Department accounts by Accounts Officers whose cadre is controlled by the Accountant General;

- field inspection of works by Chief Engineers;

- elaborate procedures and conditions to be satisfied before any work can commence;

- elaborate provisions in the General Financial Rules (GFRs) and other departmental manuals relating to the purchase, receipt, issue, and physical verification of stock and stores;

- proper maintenance and valuation of stores;

- verification and reconciliation of departmental figures with those maintained by the Accountant General;

- individual responsibilities to implement various internal controls, of which the following from Rule 12 of the GFRs is typical: "every officer must satisfy himself not only that adequate provisions exist within the departmental organization for systematic internal checks calculated to prevent and detect errors and irregularities in the financial proceedings of his subordinate officers and to guard against waste and loss of public money and stores, but also that the prescribed checks are effectively applied"; and

- other rules provide for personal responsibility for any loss sustained by the Government through fraud or negligence, as well as procedures for writing off losses.

4. The GoO internal control system described above complies, by and large, with the standards recommended by INTOSAI but not the more modern set of standards (COSO) governing performance and integrity of information. COSO emphasizes the need for a strong control environment and 'tone at the top'. The role of the Chief Secretary becomes crucial for providing the leadership for financial accountability.

5. There is too much reliance on control of individual transactions rather than systems based on delegation of authority and performance based incentives. Discussions with GoO officers also indicated that the detailed regulations are generally complied with at the 'transaction' recording level. Compliance with the spirit behind the system of internal control is neither complete nor perfect, however. For example, despite the requirement for every department to reconcile its accounts monthly with the Accountant General, and have face to face discussions on a quarterly basis, if there are still unresolved issues, more than 15% of the accounts requiring reconciliation have been left unreconciled every year between 1996/97 and 2001/2002. It would also appear that, in those cases where the rules are not obeyed, there is a reluctance to assign blame or responsibility to any individual. This practice is not only contrary to the regulations, but is also believed to act as a disincentive for staff to comply with the requirements of the system.

6. Audit reports are replete with instances of fraud, waste and abuse of public funds. A review of these reports points to numerous deficiencies in internal control associated with revenue and expenditure including procurement, asset management, and control over the payroll[28].

7. The Government may be annually incurring large expenditure to meet liabilities arising out of arbitration awards. There appears to be no focal point to account for such contingent liabilities, nor does any Department maintain a register regarding pending arbitration cases and the amounts that may be involved.

8. Financial Advisors need to be empowered by measures such as financial incentives in the form of Special Pay. Furthermore, if all "sanctions" carried the message that they have been scrutinized by Financial Advisors that would further enhance their position.

9. There is a belief among many in the public service at Orissa that the excellent intention behind the largely sound institutional and legal framework for ensuring internal control has been slowly undermined by years of indifferent and negligent implementation, the reasons for which are complex. It is also believed that there is no reward for financial discipline and no adverse consequence for irresponsible discharge of fiduciary responsibilities.

B. INTERNAL AUDIT

10. Orissa Government has an internal audit system of long standing. It is manned by Orissa Finance Service Officers, Orissa Subordinate Finance Service Staff and Orissa Service of Auditors. It consists of four wings:

i. Common Cadre Audit (CCA);
ii. Efficiency Audit;
iii. Local Fund Audit; and
iv. Gram Panchayat Audit.

[28] This SFAA report does not list all the individual weaknesses identified in the C&AG's Reports. These reports are available on the web.

The first and second wings are dealt with in this chapter.

11. Common Cadre Audit, is undertaken in all departments, except in departments like public works, irrigation, which have a Divisional Accountant attached to them. Each Department has a financial advisor under the secretary, who controls the internal audit. All internal audit staff is under the control of the respective department, with the finance department looking after establishment matters only. Internal audit parties inspect all offices under the administrative control of the Department and issue reports, somewhat similar to those issued by the Accountant General. Points raised in the reports are pursued until finally settled.

12. Efficiency Audit is directly under the control of the finance department. Its services may be requisitioned by a Department in a special case, or the finance department may initiate an investigation on its own accord. During 2000-01 and 2001-02 about forty special audits were conducted by the efficiency audit units relating to eleven departments.

13. Regardless of the type of audit, the response to internal audit reports from the offices inspected is poor. In several cases, first replies have not been received for years. No steps have been taken to rectify the irregularities pointed out in the reports. Even where a special audit was initiated by a Department, there are no subsequent steps to rectify the irregularities brought to notice.

14. In addition to serving as financial advisors (heading up internal audit units) officers in the finance service cadre may also serve as treasury officer or in commercial tax offices. Most officers seem to find these other options more attractive than financial adviser's work. There is a widespread perception that the rewards are higher for working in the treasury department and/or tax department. This situation can be improved if all finance service cadre are required to work for a time as financial advisers as part of their career development.

15. The Treasury does not exercise budgetary control while making payments. Treasuries do not have budget information at hand nor up-to-date data on expenditure previously incurred. The GoO has recognized this major weakness. This problem can be addressed through the computerization programme underway. There is a proposal to provide on-line information to the treasuries on cumulative expenditure against departmental budget.

16. Audit reports suggest, however, that the good legal framework and elaborate institutional framework for internal control and internal audit are not having the desired impact. The following examples illustrate the problems:

- The CAG report for the year ended March 31, 2002 showed avoidable irregular expenditure cumulatively amounting to Rs. 3.3 billion; excess payments to firms Rs. 3.1 billion, etc. Irregularities pointed out indicate a failure in the internal control system, particularly related to cash and materials management.

- The audit report for the year ended March 31, 2002, gives a list of major and medium capital works, involving expenditures of nearly Rs. 40.52 billion, which had been going on without completion for many years, some for as long as thirty years.

- Arrears of revenue (i.e., taxes assessed but not collected) have been a regular feature of the annual audit reports. While the percentage of cumulative arrears to tax collected has been reduced steadily over the last six years, there is still a substantial amount to be collected.

C. STAFFING ISSUES

17. There is enough staff in the Government to permit a wide distribution of duties, and a good system of internal control. Technical capacity for internal audit also does not appear to be a major barrier to performance. What may require additional attention is the need for appropriate incentives for increasing productivity. The training proposed in the Orissa Government White Paper on Public Expenditure Management and Administrative Reforms will probably suffice for now, although it needs to be elaborated in far more detail than is described in the White Paper.

D. CONCLUSIONS AND RECOMMENDATIONS

18. The legal and regulatory framework for internal control and internal audit are good in principle. Yet the application of the framework results in many weaknesses in practice, due mainly to the failure to attach personal responsibility, or apply sanctions that are provided for in existing regulations. The informal systems do not match the formal systems[29]. What is needed, therefore, is not the introduction of new laws or regulations, but the updating and faithful application of the regulations that already exist.

19. If budgeting is made realistic and monitoring of budget implementation is streamlined, a well structured internal audit deployed purposefully with well defined mandate can be of great help in toning up financial management provided, senior officials are made to realize that audit, both internal and external, is an important aid to administration rather than a mere fault finding exercise. Internal Audit Reports should be of a quality that can promote this attitude. This is an area where proper orientation and regular training are extremely important but often overlooked.

20. The above conclusion is in line with the findings of the Orissa Government White Paper of 2002, which, while acknowledging some of the existing weaknesses, calls for a review of existing laws and regulations with a view to removing obsolete and unnecessarily complicated procedures.

[29] Source: Pg 15, 19 May 2003, Opinion: Business Standard: Douglas C. North, a renowned economic historian and Nobel prize winning economist defines institutions as ‘formal’ (constitutions, laws and property rights) and ‘informal constraints’ (sanctions, taboos, customs, traditions and codes of conduct) on political, economic and social interactions.

21. In view of the above analysis, we recommend:

i. speed up the review of rules and regulations as proposed by the Orissa Government White Paper of 2002;

ii. implement faithfully the existing rules and regulations, while awaiting the results of the review;

iii. introduce more Formal Risk Management through exception reporting for high risk areas;

iv. prepare Quarterly Analysis and Reports on variations between Budget and Actuals (Physical and Financial);

v. involve Financial Advisors in all significant financial management decisions;

vi. require all finance cadre officers to spend some time in their career working as finance advisers or heading internal audit units;

vii. make Internal Audit report directly to the Secretary;

viii. provide proper orientation and regular training on modern internal audit technique; and

ix. introduce a system of rewards for merit, and take timely action in cases of negligence or dereliction of duty.

CHAPTER V
ACCOUNTING AND FINANCIAL REPORTING

A. INSTITUTIONAL FRAMEWORK

1. Under Sections 10 and 11 of the Comptroller and Auditor General's (Duties, Powers and Conditions of Services) Act 1971[30] (CAG's Act) enacted by the Parliament under Article 149 of the Constitution of India, the CAG compiles accounts of all the States of India except Goa, from the initial and subsidiary accounts rendered by treasuries and other departments. From these compiled accounts, he prepares annually Finance Accounts and Appropriation Accounts, which together with the audit report thereon, are submitted to the Governor for being laid before the legislature. There is an enabling provision[31] for the State Governments to take over the accounting function from the CAG, but this option has not yet been exercised by any of the State Governments. Article 150 of the Constitution empowers the Central Government to lay down, on the advice of the CAG, basic rules regarding forms of accounts of both Central and State Governments. In Orissa, CAG performs the accounting functions through the Accountant General (Accounts and Entitlements). The issue of the State Government taking over the compilation of accounts is a complex nation-wide issue[32]. Separation of audit from accounts is consistent with international best practice. Given capacity constraints at Orissa this matter is not an immediate concern.

2. The two issues of: (a) whether government accounting and auditing at the state level in India should be completely separated in accordance with good international practice and as implemented at the central level and (b) whether the States should take over full responsibility for their accounting, in order to promote their ownership of, and responsibility for, this function, are controversial. Some argue that the CAG responsibility for both accounting and auditing has not, in practice, resulted in any loss of independence or conflict of interest, in addition others argue that most of the States are not yet fully equipped to handle their own accounting. In any case, both are national rather than state issues, which could be revisited in the context of a Country Financial Accountability Assessment (CFAA) for India.

B. ACCOUNTING AND REPORTING PROCEDURES

3. Government revenues are received either by treasuries and sub-treasuries or by notified banks. Payments are made against bills drawn by Drawing and Disbursing Officers (DDOs) and presented to the treasuries. Certain departments such as Public Works and Forest are empowered to receive revenues directly, which are remitted to the

[30] Source: http://cag.nic.in/about_dpc3.htm Chapter III, Section 10 & 11, Duties and Powers of the Comptroller and Auditor-General

[31] "…Provided further that the Governor of a State may with the previous approval of the President and after consultation with the Comptroller and Auditor-General, by order, relieve him from the responsibility for compiling- (i) the said accounts of the State (either at once or gradually by the issue of several orders); (ii)…. Source: http://cag.nic.in/about_dpc3.htm Chapter III, Section 10, Duties and Powers of the Comptroller and Auditor-General.

[32] This issue involves the GoI, GoO, the staff unions, the RBI and others. This issue is not dealt with further in this Report.

treasuries or bank in lump sum and they draw funds through cheques. Monthly accounts submitted to the AG by the treasuries and the departments are supported with requisite schedules and vouchers. From these, the AG compiles monthly accounts for the entire State, showing receipts and payments classified under relevant heads, which closely follow the budget classification. The various departments of the government also maintain their own accounts for control over expenditure and monitoring of revenue collection. These accounts have to be reconciled with those compiled by the AG to ensure accuracy. The monthly cash balances in the books of the AG are to be reconciled with those shown in the treasuries and in the books of the Reserve Bank of India.

4. **Appropriation Accounts** show the accounts of sums expended in a financial year, compared with the sums specified in the schedule appended to the relevant Appropriation Act, authorizing the executive to draw funds out of the Consolidated Fund. These Accounts show the savings and excesses under each grant and appropriation, with reasons provided by the Executive. In practice, however, the explanations for savings and excesses are not forthcoming in many cases, and to that extent transparency is lost. Excesses have to be regularized by the Legislature. It is through these accounts the Legislature oversees the legality of the expenditure.

5. **Finance Accounts** show receipts and expenditures from the Consolidated Fund, Contingency Fund and the Public Account, classified under the major and minor heads[33]. In addition, they show loans granted and investments made in public sector undertakings, loans to local bodies, and loans received from Central Government, Life Insurance Corporation, etc. They include all deposit, reserve and sinking funds transactions, showing opening and closing balances. Guarantees given by the Government for loans raised by local bodies, Government commercial concerns and others are enumerated in detail, even though they represent only contingent liabilities. A statement is prepared by summarizing all the debit and credit balances at the end of the year linked to the cash position to "prove" the accuracy of the Accounts.

Box 3

Civil Deposits in the Public Account – Rs 8 billion[#]

The increasing Civil Deposits in the Public Account is a matter of concern. There is no cash to support these amounts. These deposits distort Annual Accounts by showing major expenditure against grants, although in fact there was under-expenditure. An age analysis of these deposit accounts and assessing the desirability of retaining items is required.

Audit Report

6. In his audit report, the CAG certifies, not that the financial statements show a true and fair view, but that both the Appropriation Accounts and the Finance Accounts are prepared and examined under his direction in accordance with the CAG's (Duties, Powers and Conditions of Service) Act 1971 and they are correct statements, subject to his

[33] Chapter I provides and explanation of these terms.

The balance increased from Rs 4 billion in FY 97-98 to Rs 8 billion in FY 01-02. In FY 00-01 the balance was Rs 6 billion.

observations in the Reports themselves or in the Audit Reports. There is no law specifically laying down the form of certificates in the case of Government Accounts in India (including Orissa State).

C. ACCOUNTING STANDARDS

7. The GoO accounts are maintained on a single entry cash basis, and therefore do not show accrued expenses, or accrued income. They also do not show total assets or their depreciation. Accounts for commercial activities of departments, however, are required to be maintained in proper commercial form under special rules issued by the Government on the advice of the AG.

8. Since government accounting standards and practices are centrally determined for application throughout the country, their thorough and critical review is best reserved for the Country Financial Accountability Assessment (CFAA) for the whole of India. It is, nonetheless, interesting to observe how the current application of existing national standards compares with the practice and standards recommended by the International Federation of Accountants, Public Sector Committee (IFAC-PSC). Financial statements may not be described as complying with the standard unless they comply with all the requirements of Part 1. Part 2 sets out additional disclosures that IFAC[34] encourages governments to make. It also encourages governments to progress to the accrual basis of accounting, for which different standards apply.

9. Even within the limitations imposed by the centralized accounting standards, certain current practices could be improved. For example:

- **Reconciliations**: There are large unreconciled differences between treasuries and many public works departments, some dating back to 1964/65. Similarly, 827 loan accounts balances as of March 31, 2002[35], relating to Urban Development and Village and Small Industries, amounting to about Rs. 316 million, the earliest dating back to 1968/69, had not been accepted by the concerned officers. We recommend that the GoO appoint a small committee to determine within less than six months how to reconcile or write off these differences. Such differences are an aggregate of account maintained by the AG and the detailed accounts maintained by the departments.

- **Timing of Annual Reporting:** The current period from year-end to the issue of the AG's accounts (currently about 12 months) could be considerably shortened. Presentation of accounts need not await the submission of the audit report to the Legislature. The State of Karnataka, for example, is said to have issued its latest annual accounts in four months. We recommend that efforts be made to issue audited accounts of the State earlier than at present.

[34] Draft: Financial Reporting under the Cash Basis of Accounting, International Public Sector Accounting Standard (IPSAS), Issued by the International Federation of Accountants, January 2003

[35] Source: Report of the Comptroller and Auditor General of India, for the year ended 31 March 2002 (Civil), Government of Orissa.

- **Comparative Figures**: International Public Sector Accounting Standards require that final accounts disclose comparative information in respect of the previous period for all numerical information contained therein. Except for the summary statement of the Finance Accounts, such comparative information, which facilitates an understanding of changes in government activity from year to year, is not being provided. We recommend that comparative information for the previous year be provided in all government annual financial statements.

- **Computerization**: About half of the 38 treasuries have been partially computerized[36]. These are not inter-connected. Monthly accounts to the AG are submitted manually, and not through computer software. Full computerization would speed up the preparation of both monthly and annual financial statements. We recommend that full computerization of the accounting system, including networking with the AG's office, be speeded up and information requirements agreed upon.

Box 4

Good Practice Example: South Africa

Annual Financial Statements

1. The Annual Financial Statements will consist of:

   - A Balance Sheet;
   - An income statement;
   - A cash flow statement;
   - Notes and such other statements as may be prescribed;
   - Based on Generally Recognized Accounting Practice issued by the Accounting Standards Board

2. Submission within 2 months of the financial year end to the Auditor-General for auditing and to the treasury for inclusion in consolidated statements

3. Audited financial statements must be submitted to the treasury and the minister within 5 months after the end of the financial year (audit opinion now part of annual report)

Source: Presentation at the International Seminar on "Accounting for Results" June 2003

10. A detailed comparison of the above mentioned International Public Sector Accounting Standards (IPSAS) with standards practices by the GoO, reveals significant deviations from IPSAS, which need to be addressed at the national level, where the standards are determined. The GoO accounts do not include a comprehensive statement of accounting policies; they are published (generally) within 12 months following the

[36] It is our understanding that 20 Treasuries out of 36 have initiated the computerization process, albeit in a limited manner at this stage of development.

year-end (IPSA's prescribe 6 months); they do not identify extraordinary items (e.g., disaster relief), they do not disclose fixed assets; and they do not disclose the proportion of GoO ownership of companies or corporations it controls; in all cases and accounts are maintained on a single entry cash basis instead of double entry system assumed by IPSAS.

11. In November 2002 the CAG set up a Government Accounting Standards Advisory Board to formulate and propose accounting standards to improve the usefulness of Government financial reports. The Board is headed by the Deputy Comptroller and Auditor General, and includes representatives of the GoI, State governments, Reserve Bank of India and Private Sector Auditors. An exposure draft on the need for improved disclosure of guarantees has been issued. The question whether the Government in India should switch from cash based to accrual based accounting system has been referred to this Board, which still has to submit its recommendations. Any change in this matter in Orissa State has to await the decision of the GoI, based on the advice of the CAG.

D. STAFFING ISSUES

12. The minimum qualification for staff entering the CAG's office is a university degree. Candidates must also satisfy a Staff Selection Commission. The staff receives adequate training at various times of their career progression. Written examinations are prescribed for promotion to certain supervisory levels. At higher managerial level, the selection is made by the Union Public Service Commission through a highly competitive examination. There are several training institutes maintained by the CAG to cater to all cadres.

E. STATE REFORM PLANS

13. The GoO White paper on Public Expenditure Management and Administrative Reforms does not contain any specific comment or action plan with regard to accounting standards or financial reporting.

F. CONCLUSIONS AND RECOMMENDATIONS

14. Good financial reporting is crucial for expenditure and revenue tracking. The accounting standards of the GoO fall short of standards (IPSAS) recommended by the IFAC for cash based financial accounting and reporting, but this is a national, not a State issue, since government accounting and reporting standards in India are largely controlled from the center, notably by the CAG. The form of the finance accounts needs to be simplified and made more user friendly in line with best practice. Within the confines of existing standards, we recommend the following improvements:

a) monthly accounts should be provided on each department of the Government, and a consolidated statement on the Government as a whole showing both actual and budget information within 6 weeks of the close of the month;

b) define within six months how to reconcile or write off unreconciled differences between departments, treasuries, and others agencies or offices;

c) discontinue unnecessary transfers from the Consolidated Account to “Deposits” in the Public Account;

d) issue Annual Financial Statements of the State within six months following the end of the fiscal year and place monthly Financial Statements on the net;

e) disclose in the Annual Appropriation Accounts Explanations for Savings and Excess (Grants);

f) include comparative information for the preceding year in all annual financial statements;

g) computerize the State’s accounting system and network it with the AG’s office; and.

h) provide training for existing staff.

CHAPTER VI
RURAL LOCAL BODIES (PANCHAYAT RAJ INSTITUTIONS)

A. INSTITUTIONAL FRAMEWORK

1. Panchayat Raj Institutions (PRI) are the local governments in the rural areas and have been an integral part of the Indian rural society, albeit in different forms from time immemorial. The Constitution of India[37] recognized their presence as far back as 1948: *'The State shall take steps to organize village Panchayats and endow them with such powers and authority as may be necessary to enable them to function as units of self government'*.

2. The 73rd Constitutional Amendment was a formal instrument introduced by the Central Government in 1992 and was blessed by the State Assemblies, to introduce a minimum level of rural decentralization uniformly across the States.

3. The Constitution Amendment mandates political empowerment of the PRIs leaving issues of design and implementation on sectoral, administrative and fiscal aspects of decentralization to the States. In Orissa, the State Assembly passed the required conformity Acts in 1994, 1995 and 1997 to set in place the present form of the 3-tier system of Panchayati Raj consisting of *Zilla Parishad* at the district level (ZP), *Panchayat Samiti* at the block level (PS) and *Grama Panchayat* at the village level (GP).

4. PRIs are directly under the general supervision and control of the State. The first State Finance Commission was set up in 1996 to make recommendations as regards the financial powers of the panchayats.

The present three-tier structure in Orissa is as follows:

	Location	**Nos**
Zilla Parishad	At Districts	30
Panchayat Samiti	At Blocks	314
Gram Panchayat	At Villages	6,234

B. FINANCIAL RELATIONSHIPS AND FLOWS

5. In FY 2002, the State Government provided Rs. 9.1 billion[38] (6% of the State budget[39]) to PRIs and the Center provided Rs. 3.3 billion. Of the total (State and Center) allocation of Rs. 12.4 billion allocated to the PRIs, 38% (Rs. 4.7 billion) of the funds were provided through District Rural Development Agency (DRDA), the nodal agency set up as

[37] Article 40 Part IV Organisation of village Panchayats.
[38] Data based on own calculation based on official data provided by PR Department and from State Budget documents.
[39] The State budget indicates that 40% of the expenditures relate to `district sector'.

societies (registered under the Societies Registration Act, 1948) at the district level. The remaining 62% (Rs.7.8 billion) was mainly for salaries of staff[40].

6. The Panchayat Raj Department (PRD) of the State Government is accountable for ensuring that an adequate financial management and accountability framework for the PRIs is in place and that funds provided by the State and Center are used for purposes intended. The PRIs are expected to provide utilization certificates to support their use of grant-in-aid funds. The Finance Department of the State Government conducts full audits of the PRIs. The results of these audits are acted upon by the PR Department.

7. The PR Department is also expected to monitor the implementation of the schemes funded by the State and Center to ensure that the purposes intended are being achieved. Monthly physical and financial progress reports are provided to the PR Department by the implementing agencies through DRDAs. The audits of DRDAs are carried out by firms of chartered accountants, in addition to CAG's audits and the reports reviewed by the PR Department.

C. FINANCIAL ACCOUNTABILITY ARRANGEMENTS[41]

8. STRENGTHS OF THE SYSTEM:

- A framework for financial accounting, reporting and auditing is in place for all funds provided to the PRIs.
- The key accounting functions have been staffed.
- Constitution of Palli Sabhas[42] (as ward level constituents of Gram Sabha[43], the general body of the Grama Panchayat) and introduction of social audit[44] arrangements at the Grama Panchayat level.

9. WEAKNESSES OF THE SYSTEM

- PRIs remain almost exclusively dependent on funds from the State and Center. This limits the extent to which the local governments can be self-governing bodies. This is exacerbated by fiscal stresses at the State level making budgeting processes ineffective.

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[40] One of the major issues facing Orissa is establishing an appropriate proportion between development/ welfare expenditure and salaries.

[41] A detailed review of the PRIs was undertaken by the World Bank, and a working paper on Public Financial Accountability in PRIs will be available shortly.

[42] Every 'Grama' constituted is divided into wards and for every such ward, a 'Palli Sabha' is constituted.

[43] `Grama Sabha' is a village assembly and comprises all persons registered as voters to the Assembly in a village or group of contiguous villages notified as a 'Grama'.

[44] 'Social Audit' is a mechanism for the 'Palli Sabha' to publicly review the development works undertaken within their ward. The special meeting convened for the social audit is attended by all Government officials and allows the members to discuss their objections and resolve by consensus or show of hands if the work is satisfactory and free from irregularities.

- Major decisions, such as what kinds of programs will be undertaken and who will be the implementing agency, remain with the State and the Center. PRIs play minimal role in the planning and implementation of schemes – for every function that has been devolved to the PRI, there are specific Line Departments of the State or agencies like DRDAs.

- Excessive levels of State controls over the PRIs, such as the power of the Collector[45] in ordering enquiries against the elected representatives, authority to suspend resolutions passed in the meetings of the elected representatives of PRIs, have resulted in the PRIs being perceived as extensions of the State.

- The accountability of the executive of the PRI remains essentially to the Collector at the District level and the State, and not to the elected representatives of the PRIs.

- The accountability of the elected representatives to their constituents is compromised by their limited role in the management of resources spent at each of the levels of PRIs. The secrecy that surrounds the executive action is most apparent in the selection of beneficiaries for subsidy and poverty alleviation programs – records of meetings do not show how the choices were arrived at or the options or criteria for selection, often concealing the high levels of arbitrary decision making.

- The Management Information System at the PR Department does not provide information on the financial position of PRIs. This limits the ability of the State to take informed decisions on the allocation of resources between PRIs and to the PRIs as a whole, based on the needs of the rural population.

- There are far too many cases of weak accounting, inadequate internal controls (pending utilization certificates for Rs. 910 million[46] for grant-in-aid from the State, unadjusted advances of Rs. 320 million[47] for 95 Panchayat Samitis as on 31 March 2002, unspent balances of grants on 31 March 2002 amounting to Rs. 1.2 billion[48]) and related irregularities, such as diversion of funds reported by the external auditors repeatedly over the years. There appears to be no concrete action plan to address the given fiduciary risk associated with the funds spent in respect of PRIs.

- The effectiveness of the audit function is questionable, given (i) the large number of pending audits (12,990 GPs from 1995-96 to 2001-02); (ii) no audits of ZPs conducted since 1996-97; and (iii) the large number of surcharge cases pending disposal - 50,939 cases amounting to Rs. 123 million as on 31 December 2002 for GPs alone, besides 43,000 odd cases amounting to approximately Rs. 94 million for PSs.

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[45] Collector is the administrative head of the District and also the Chief Executive Officer of the ZP and Executive Director of the DRDAs.
[46] As per data provided by the PR Department
[47] As per CAG report (Civil), 2001-02
[48] As per CAG report (Civil), 2001-02

D. CONCLUSIONS AND RECOMMENDATIONS

10. It is clear from the above that the State's hand in the management of the PRIs has not allowed the devolution process to proceed as may have been intended by legislation. The reasons for this are complex and worthy of analysis at the national level.

11. The motivation to comply with the accountability framework in place is undermined by the diffusion of roles and responsibilities between the various levels of government with limited checks and balances provided by the State Legislature, as is evident from the CAG audit reports of recent years.

12. Steps are being taken to reduce the fiduciary risk. Preliminary discussions have commenced with the CAG on streamlining the accounting and financial reporting systems including the consolidation of the internal audit function. Initiatives are being taken to train the auditors on PRI auditing.

13. In the White paper on 'Public Expenditure Management and Administrative Reforms' published in 2002, the GoO committed to a 12 point program for empowering the village panchayats and set up a high powered Committee under the Chief Secretary to recommend measures for greater devolution of powers and resources to the elected local bodies. The Government also committed to take steps to strengthen the capacity of field administration down to the districts and blocks. However, the recommendations made by the high powered Committee in March 2003 to hand over accountability of functionaries of 26 departments to the PRIs was reduced to 11 departments by the Cabinet of Ministers. The Cabinet also limited the authority of the PRIs to the approval of casual leave of the functionaries.

14. It is evident that the core issue is the need to strengthen the capacity of the PRIs to undertake the functions assigned to them. The recommendations are as follows:

i) transfer all State Government functionaries working on PRIs to the PRIs; and in the interim make State Officials answerable to local elected representatives; and

ii) provide PRIs with the funds commensurate with the functions and augment the capacity of the PRIs to[49]:

- raise their own levels of revenues;
- learn from the experiences of other States, where the accountability of PRIs is increasingly defined in terms of sector outcomes and increased delegation of planning, implementation, monitoring and evaluation to the local governments;

[49] Funds available are not adequate to carry out the functions assigned to the PRIs. Either more funds would need to be allocated, which looks difficult in the present context, or, the functions assigned need to be reviewed.

iii) computerize data base on Aggregate Financial Position and Operational Outputs of PRIs and provide on-line public access to this data base;

iv) expedite audits, clear arrears and take Follow up action; and

v) review the need for and simplify the accounting, controls, reporting, auditing arrangements and training requirements of the accounting staff with a view to improving the effectiveness of the financial management system. Further, evaluate the viability and cost effectiveness of introducing computerization at each level.

CHAPTER VII
URBAN LOCAL BODIES (ULBs)

A. INSTITUTIONAL FRAMEWORK

1. The legal and institutional framework is provided by the provisions of the Constitution through the 74th Amendment, the Orissa Municipal Act, 1950 and the Orissa Municipal Rules, 1953. The two Municipal Corporations have been formed by a recent enactment called the Orissa Municipal Corporations Act, 2003, which came into effect from 18-04-2003. The State Government has not passed any specific law in pursuance of the 74th Amendment to the Constitution

2. There are 103 urban local bodies (ULBs) in Orissa, categorized as Municipal corporations (2), Municipalities (34) and Notified Area Councils (67) with reference to the size of the population.

3. The elected body comprises the public representatives (called councilors) who hold office for a period of five years. Members of the State Legislative Assembly for their respective constituencies are also members of the council. Additionally GoO nominates a few councilors. The Council is the policy making body. Various standing committees are formed as per the statute for rendering specialized functions; there are standing committees on finance, public health, hospitals and dispensaries, public works, etc.

4. The ULBs function under the overall administrative control of the State Housing and Urban Development Department. The Director of Municipal Administration is the head of the department. Each ULB is headed by an executive officer who is ordinarily an officer of the Orissa Administrative Service. The executive officers of the two Municipal Corporations are known as Chief Executives.

5. The State Government has the powers to call for information, conduct inspections, give directions, and dissolve a ULB, cancel orders and even rescind resolutions of the Council under specified circumstances.

6. The functions of the ULBs fall under two categories, namely, obligatory functions such as maintenance of roads, street lights, sanitation, water supply, registration of births and deaths, public immunization and regulation of buildings; and discretionary functions such as formation and maintenance of layouts, parks, schools, hospitals, libraries etc., There are separate departments for the performance of these functions besides an administrative and a finance and accounts department.

7. The own resources of the ULBs are very limited. These comprise rates and taxes, including property tax, license and other fees, income from property, receipts under special laws like fees, ferry rent, etc. The major source of income of the ULBs is the grant received from GoO in lieu of Octroi receipts. Additionally, ULBs receive specific purpose grants from GoO like road maintenance grant, for payment of salaries for teaching and non-

teaching staff. The ULBs also receive central funds as mandated by the Finance Commission, besides funds for the execution of centrally sponsored schemes.

8. During the year 2002-03, an aggregate amount of Rs. 1330 million was budgeted by the State for the ULBs.

9. A few construction activities of the ULBs may be funded from the MP's/ MLA's[50] Local Area Development Funds.

10. GoO has advanced loans to the ULBs. An amount of Rs. 314 million was overdue as on 31st March 2002, besides the overdue interest of Rs. 69 million. The amount of guarantees outstanding as on 31st March 2002 aggregated Rs. 230 million. These guarantees had been given for repayment of principal and payment of interest on loans raised by the ULBs for basic sanitation and water supply schemes.

B. BUDGETARY PROCESS

11. The ULBs prepare an annual budget in the format prescribed by law. After approval by the Council, the budget is sent to GoO for review and finalization. The amendments made by the GoO are incorporated and the final budget is drawn. The budget estimates of revenue and expenditure are mainly based on ad hoc increases over the previous year's budget, considering the amount of funds expected to be provided by the GoO.

12. The government releases the budgeted funds to the ULBs through the controlling department. The funds are released at appropriate intervals. No re-appropriations are allowed except with the approval of the Council on the basis of the recommendations of the executive committee. There are no off budget items as such unless some specific contribution is made by the community for execution of a particular public utility.

C. MONITORING

13. The Housing and Urban Development Department monitors the activities and functioning of the ULBs. The receipt of the utilization certificates is reviewed every month. The implementation of some of the major schemes like National Slum Development Project, Swararna Jayanti Sahari Rojgar Yojna and Valmiki Ambedkar Awas Yojana for alleviation of urban poverty is monitored. In the context of raising resources for upgrading civic services, according to a study conducted by the Participatory Research in Asia (expected to be published shortly) "the collection efficiency is estimated to be less than 50%"[51].

[50] Members of Parliament and of the Legislative Assembly have allocations of funds authorized by law to spend at their discretion on local projects in their constituencies

[51] Business Standard, June 17, 2003: page 4, "States sapping local bodies financially".

D. ACCOUNTS

14. The ULBs maintain accounts in the formats prescribed in the Orissa Municipal Rules. The accounts are kept on cash basis and in single entry form. There are no specified standards or policies for the maintenance of accounts. The books of accounts, records, registers etc., are maintained in prescribed forms under various heads of accounts in respect of all transactions. The main accounting record is the cashbook from which accounts are built up in the form of classified registers in which revenue and expenditure transactions are entered under different account heads. The classified registers are used for compiling the monthly receipts and payment summary. The annual accounts are prepared from the monthly accounts.

15. In terms of the 74th Amendment to the Constitution, the State government may make laws for the maintenance of accounts and their audit. In pursuance of the recommendations of the Eleventh Finance Commission, the Government of India issued guidelines for utilization of local bodies grants in June 2001. As per these guidelines the CAG has prescribed the format of the budget and accounts for the Panchayati Raj institutions and Urban Local Bodies. Orissa has not so far implemented the format. These formats encourage financial accounting on an accrual basis and more effective asset management along with better cost accounting procedures relating to services provided by ULBs.

E. AUDIT

16. The audit of the ULBs is conducted annually by the Local Fund Auditors of the State Finance Department. The government procedures are followed; no auditing standards as such have been prescribed. Audit covers hundred percent transactions of ULBs. When embezzlements are detected, the auditor has the power to allow the errant employee to deposit the amount to make good the loss. Surcharge is levied for minor omissions and commissions after due process of issue of notice to the errant employee. The amount of surcharge can be recovered as arrears of land revenue. Serious irregularities are reported to the appropriate authorities for necessary action. Whether action actually takes place is not adequately documented.

F. STRENGTHS

17. The main strengths of the financial system as prescribed are;

- Well defined rules and regulations for the functioning of the ULBs; basic accounting records and formats are well established;
- Appointment of the suitable officials in key positions;
- Budgets are also required to be prepared annually; and also approved by GoO;
- System of review of financial performance by GoO is prescribed; and
- Hundred percent audit is done by the Examiner Local Fund Audit.

G. WEAKNESSES

There is a gap between precept and practice. A study of a selected number of audit reports reveals that:

- Budgets are not being sent to the GoO for approval in every case;
- Demand and tax collection records are not properly maintained;
- Embezzlement of tax receipts (money collected from tax payers not credited to ULBs accounts);
- Utilization certificates of grants are not being furnished to the State Government;
- Amounts remain unspent for the purposes intended;
- ULB revenues are overestimated by the bodies. Unrealistic estimates are generally not achieved and the reasons for shortfall are not analyzed;
- The audit of ULBs is in arrears. While this has been attributed to shortage of staff, the need is obvious for adoption of scientific systems of statistical sampling. The audit reports need to be placed before the Council; and
- Further, the transparency of their financial position is hampered by the lack of audited financial statements showing their assets and liabilities; and there are arrears in independent auditing of their cash transactions. Auditors' reports indicate significant fiduciary risk.

H. CONCLUSIONS AND RECOMMENDATIONS

18. The financial position of the ULBs is not very healthy. Only 38 out of 103 ULBs, including the two Municipal Corporations are reported to be operationally sound. There is need for greater generation of internal revenues and narrowing the tax gap. The option of periodical revision of rates of the property tax needs to be exercised. User charges are another way to augment revenues.

19. The accounts of the ULBs are maintained on cash basis and do not reflect the accrued liabilities, nor the very substantial assets of these public bodies. The GoO needs to implement the format recommended by the CAG.

20. The Housing and Urban Development department needs to present a consolidated picture of the financial and physical performance of the ULBs. This report should be tabled in the legislature on an annual basis.

In view of the above, in consultation with the GoO the following recommendations are being made:

i) generate greater internal revenues to narrow the tax gap. In addition, the option of periodical revision of rates of the property tax should be exercised;

ii) enhance own revenue base;

iii) implement the format recommended by the CAG, as the accounts of the ULBs are maintained on cash basis and do not reflect the accrued liabilities. In this regard, improve completeness and timeliness of Cash Accounts and account for the assets of these bodies in a manner consistent with the requirements for sound asset management;

iv) introduce accrual based accounting;

v) computerize the accounting system and records of the ULBs;

vi) place the audit reports before the Council on a timely basis and avoid future delay in audit of the ULBs;

vii) the Housing and Urban Development department should present a consolidated picture of the financial and physical performance of the ULBs. This report should be tabled in the legislature on an annual basis; and

viii) train employees of ULBs in more modern financial management techniques associated with the need for more cost effective service delivery.

CHAPTER VIII
STATE OWNED ENTERPRISES (SOEs)

A. INSTITUTIONAL FRAMEWORK

1. The legal and institutional framework for the Government companies and the statutory corporations under the control of the Government of Orissa (GoO) is provided by the Companies Act 1956 and the specific statutes under which the statutory corporations have been established. These are Central Government laws.

2. As of 31st March 2002, there were 68 Government companies under the control of the GoO registered under the Companies Act, 1956. Of these there were 35 non-working companies in the process of liquidation/ closure/ merger etc. In addition there are three statutory corporations.

3. The accounts of the Government Companies are audited by statutory auditors appointed on the advice of the Comptroller and Auditor-General of India (CAG). Under the law the CAG has the right to give directions to the statutory auditors, review their work, and also to conduct supplementary audit. The audited accounts are presented at the Annual General Meeting of the company/corporation and are public documents. The annual accounts of the companies and statutory corporations and the CAG's reports thereon are submitted to the Government, which lays them before the State Legislative Assembly (SLA).

4. Under Article 208 (I) of the Constitution of India the SLA has framed Rules of Procedure and Conduct of Business which among other things, prescribe the constitution of a committee for legislative oversight called the Committee on Public Undertakings (COPU). The COPU follows up on the Audit Reports of the CAG and may also take up matters/ companies not covered by the Audit Reports. Additionally, the Legislature's Committee on Papers laid on the Table monitors the timely submission of the annual reports of the statutory corporations and companies.

5. The Government companies and statutory corporations function under the respective line departments. In addition, the Department of Public Enterprises is the nodal agency responsible for laying down general policies and guidelines for the effective management of public enterprises, regulating industrial project proposals through the Project Approval Committee, laying down norms for financial discipline, and prescribing model Memorandum of Understanding

B. FINANCIAL RELATIONSHIP AND FLOWS

6. Government funds have been provided by way of investments in equity and loans to Government companies and statutory corporations as follows:

As on 31.3.2002

	Equity	Loans
	(rupees in millions)	
Government Companies	14760	16174
Statutory Corporations	1853	371

Source: Report of the Comptroller and Auditor General of India, for the year ended 31 March 2002 (Commercial), Government of Orissa

In addition, Government guarantees in respect of Government companies and corporations outstanding at the end of March 2002 are reported to be Rs. 38471 million.

7. The budgetary payments in the form of equity and loans and grants and subsidies from the State Government to 10 working Government companies and the three statutory corporations during 2001-02 totaled about Rs. 759 million.

	(rupees *in millions*)
Equity	100
Loans	81
Subsidy	578
Total	**759**

Source: Report of the Comptroller and Auditor General of India, for the year ended 31 March 2002 (Commercial), Government of Orissa

8. Government funds involved in the 35 non-working companies amounted to Rs. 869.4 million (equity Rs. 584.2 million and loans Rs. 285.2 million).

C. ACCOUNTS

9. Only three out of the 33 working companies had finalized their accounts for the year 2001-2002. None of the statutory corporations had finalized its accounts. The extent of arrears in finalization of accounts ranged up to eight years. The accounts of non-working companies were in arrears ranging up to 36 years.

10. SOEs have been informed that the Government will not sanction additional cost of living allowances nor provide additional guarantees unless serious effort is demonstrated towards finalization of annual audited accounts.

11. The audited reports on all three completed accounts were qualified. Given that similar irregularities are being pointed out year after year, the qualifications in the reports of the auditors do not appear to have any effect.

D. WORKING RESULTS

12. According to the latest finalized accounts of 33 Government companies and three statutory corporations, 20 companies and one corporation had incurred aggregate losses of Rs. 7320 million and Rs. 143 million respectively. Only seven companies had earned aggregate profits of Rs. 1154 million; the aggregate profit earned by two corporations amounted to Rs. 41 million. The remaining companies had not commenced commercial activities or finalized their first accounts.

13. The accumulated losses of six companies aggregating to Rs. 12280 million exceeded their equity of Rs. 4748 million. The accumulated losses of the 35 non-working companies, amounting to Rs. 23861 million according to the latest finalized accounts had completely wiped out their equity of Rs. 22113 million. The main reasons for the losses were understood to be a combination of ineffective management, overstaffing, time and cost over run in project implementation, lack of professionalism in decision making, lack of accountability and poor productivity. These enterprises are not always headed by professionals either with a proven track record or with adequately long tenure to allow for the achievement of the high levels of performance.

14. Of all the State SOEs likely to remain in the Government ambit, the performance of the power sector, more particularly the energy distributors need to be keenly investigated, to assess: (i) the impact of power thefts; (ii) inability of the distributors to reduce such losses, and (iii) visibility of relating the cost of efficient operations with Tariffs.

Box 5

GRID CORPORATION OF ORISSA LIMITED

– the Government owned Power Transmission Company

Last Audited Financial Statement:	FY 1999-2000
Opinion:	Qualified
Subject to:	15 Items covered in Annexure-II to the Audit Report
Concerns:	1. Net impact on GRIDCO's financial position not quantified, 2. Unclear whether opinion is "qualified" or "denial"

E. REFORM PROCESS

15. The GoO has initiated a reform process in order to ensure higher growth, provide competition, promote efficiency, provide good governance and eliminate budgetary support. Some of the enterprises have been divested and various bold divestiture options are being considered for some others. As part of the reform process, the erstwhile State Electricity Board, a statutory corporation, has been unbundled and power distribution has been privatized. Government needs to hasten its decision regarding the future of

companies which have become defunct. Completing their accounts and have them audited would be a good first step.

16. A study has been undertaken on what to do about the loss-making companies while the reform process is implemented. The concern is that the condition of these companies, both physical and financial, will rapidly deteriorate during the period when reforms are being discussed, debated and implemented. Such deterioration will cause greater stress on the State Budget and will also make the companies more unattractive to any intending buyer, thus reducing the potential realizable value.

17. GoO in consultation with the Ministry of Finance GoI undertook (April 15, 1999) to act upon a time bound reform program for investment and restructuring of certain State Owned Enterprises. The CAG Report for year ended March 31, 2002 points out that a review of action taken (as at September 2002) indicates that none of the milestones have been achieved[52].

F. ACCOUNTABILITY

18. The core issue remains one of accountability. Government companies and statutory corporations are primarily accountable to the shareholder which in this case is the GoO. The involvement of government funds also implies accountability to the SLA, and, through it, to the people of Orissa State. The legal and institutional framework which lays down the requirements of presentation of accounts, audit by external auditors and follow up by the legislative committees is intrinsically sound.

19. The facts and figures presented above indicate, not only a dismal profitability record, but also a dysfunctional accountability mechanism for most of the Government companies and statutory corporations. There can be no accountability without accounts. Prolonged arrears in accounting and auditing therefore imply a breakdown of accountability. There are also indications that internal accountability mechanisms such as internal control and internal audit are in poor shape.

20. In addition to the weaknesses noted above:

- Historically, the Government companies and the statutory corporations have been established with a multiplicity of objectives, which are not always mutually compatible. The duty has been imposed on them to meet certain social obligations which may be inconsistent with the achievements of purely commercial objectives, yet the cost of meeting the social objectives is not separately disclosed.

- The issue of autonomy of the Government companies and statutory corporations has not been satisfactorily resolved. Political interference also adversely affects performance.

[52] CAG Report for year ended on March 31, 2002, 'Restructuring Programme of GoO', para 1.5.1, page 13.

- At the same time the monitoring role of Government, which is the shareholder, has not been effective.

- Business plans are not drawn up for state government review on a timely basis.

- There are audit committees in high risk areas such as the power sector, but they do not adequately pursue issues relating to serious audit qualifications and their impact on the financial statements, nor do they focus the State's attention on the extensive weaknesses in internal control and internal audit at SOEs.

- Response to external audit and the recommendations of the legislative oversight committee has been poor.

21. This SFAA report does not list all the individual weaknesses in control and accountability identified in the C&AG's Reports[53]. A careful reading of the Audit Report for year ended March 31, 2002 suggests a range of important issues of corporate governance that need attention including the need for monitoring Memorandum of Understandings (MoUs) such as between the State Government and the Ministry of Power, GoI on the implementation of the reforms program in the power sector[54]. Further, the Audit Report among a range of observations pertaining to a number of SoEs points out for example that despite a hike in tariff GRID Corporation of Orissa Ltd and private distribution companies incurred a loss of Rs. 21 billion mainly due to increase in transmission and distribution losses. In the case of the Review on Orissa Agro Industries Corporation Ltd the Report points out that this company need to formulate suitable procurement policies and procedures with a view to make available agricultural tools and implements at competitive rates to the small farmers. It also points out that improper financial planning and failure to deposit statutory employees provident fund deductions resulted in a payment of penal damages of Rs. 12.2 million. In the case of the Orissa State Warehousing Corporation head office administrative overheads ranged between 19 and 22% of warehouse receipts during 5 years ended March 31, 2002 as against the norm of 8%. The excess expenditure on this account works out to Rs. 80 million.

G. CONCLUSION AND RECOMMENDATIONS

22. The functioning of the SOEs, at present, falls short of the legal/regulatory framework laid down for their financial management. To overcome the shortfalls, a reform process has been commenced[55]. The GoO reform process of public sector enterprises envisions the ultimate continuance of only a few selected companies. The opportunities for improvement are accordingly discussed in the context of this ultimate goal.

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[53] All CAG reports are available on the web.

[54] CAG report for year ended on March 31, 2002, 'Reforms in Power Sector', para 1.11.1, page 17.

[55] The GoO undertook a detailed review of the SOEs and a White Paper has been issued which provides analysis on their financial position.

23. Good Corporate governance requires that there be a succession plan in place in each enterprise and senior appointments be made based on proven track record.

We therefore recommend that GoO:

i) define clearly the specific objectives of the companies and corporations. When these include the achievement of certain social goals, there should be a clear recognition and statement of the related costs for the proper appreciation of the financial and operating performance of the enterprise;

ii) make business plans visible and available on a timely basis for state government review;

iii) establish an arms length relationship between the Government and the companies and corporations. The latter should have complete operational freedom in return for full public financial accountability operating on a timely basis;

iv) monitor the SOEs more effectively. Key performance indicators should be identified and periodical reports obtained and reviewed. The number of such performance indicators should be kept small. Review meetings should be chaired by the Secretary of the line department, at which the representative of the Department of Public Enterprises should be a regular invitee;

v) launch a crash programme to bring the accounts of the entities up to date. The accounts that are produced and presented should be transparent, any tendency towards proliferation of notes should be discouraged. The notes should generally state the accounting policies adopted, deviation therefrom and such other matters as need explaining;

vi) insist that the effect of any qualifications, observations and comments of external auditors on the working results and financial position should be clearly stated. When such qualifications, observations and notes render the external auditors opinion ineffective, there should be no hesitation in denying an opinion on the accounts;

vii) establish effective audit committees as mandated by the recently proposed amendment to the Companies Act;

viii) discourage and curb the practice of appointing Members of the Legislative Assembly (MLAs) to the office of Chairperson; this has the potential to erode the autonomy of the Government companies and blurs the lines of accountability;

ix) respond better to external audit as well as the recommendations of the legislative committee. Individuals should be held accountable for their action. Senior Government functionaries should be held accountable for failure to enforce accountability;

x) allow the managements sufficiently long tenures to perform effectively and to be held to account. The role of Government nominee directors should be clearly spelt out for determining the accountability of such directors;

xi) cause the managements to introduce modern management practices, strengthen internal controls including internal audit and bring them on par with the best national practices;

xii) cause managements to introduce greater transparency in the Annual Reports to the shareholders which should be a candid assessment of the achievements and failures, strengths and weaknesses of the enterprise, and its systems along with measures that are being taken to improve the organization's financial and operating performance;

xiii) publish an annual public enterprise survey. This should inter alia give the extent of Government financial involvement in the Government companies and corporations, their state of accounts and working results, achievement of objectives, results of external audit, recommendations of the legislative committee and follow up action taken. The survey should be a public document freely available and also put on the State Government website; and

xiv) appoint Chief Executives and directors through transparent selection process with a 3-5 years tenure in order to induct professionals with proven track record.

CHAPTER IX
EXTERNAL AUDIT

A. INSTITUTIONAL FRAMEWORK

1. India has a unitary public audit function in a federal set up. The CAG is the country's Supreme Audit institution, and also the auditor of the State of Orissa. He is an authority prescribed in the Constitution- an officer neither of the executive nor of the legislature- on par with the apex judiciary. The Constitution prescribes exhaustive safeguards for the independent functioning of the CAG like guaranteed fixed non-renewable tenure, full access to information, and the right to table his reports at the Legislature without hindrance. In Orissa, the CAG functions through the Accountant General (Audit) located at the State capital Bhubaneshwar.

2. Globally the expectations of the Parliament and the Public from Supreme Audit Institutions (SAIs) have undergone a change. In addition to discharging the traditional functions of highlighting irregularities and pointing out weaknesses, SAIs are expected to play a more proactive role and act as an aid to management in improving system efficiency and effectiveness. While this could be partly achieved through the periodic audit reports, SAIs have been exploring other means of disseminating their findings/ideas to the Public, including research in State Finances[56].

3. The framework in India and Orissa is reasonably sound and compares favorably with other developing democracies. However compared to the more advanced Westminster democracies there is room for improvement in the areas of timeliness of audit, emphasis given to the system rather than the transaction audited, building of a stronger working relationship with the auditee and the nature and extent of public interface between the auditors and civil society.

B. SCOPE OF COVERAGE OF PUBLIC AUDIT

4. The duties, powers and conditions of service of the CAG are prescribed in the Constitution and the laws framed thereunder more especially, the CAGs (Duties, Powers and Conditions of Service) Act, 1971. In addition to the audit of accounts of the GoO, he also audits the accounts of statutory corporations, Government companies, other authorities and bodies as prescribed by law. The scope of coverage is comprehensive with two exceptions. First, he is not the auditor of companies where the State has less than 51% of the equity. The power distribution companies fall in this category. Second, in the rare case of State owned statutory Corporation where the audit was not assigned to the CAG as was in the case of IDCO.

[56] Research Paper published by International Centre for Information Systems and Audit (iCISA) Office of the Comptroller & Auditor General of India

C. REPORTING LEVEL, AUDIT REPORTS AND TRANSPARENCY

5. The CAG submits his Audit Reports to the President or the Governor who shall mandatorily cause them to be laid before the appropriate Legislature. What is to be included in the Audit Reports is to be decided entirely and exclusively by the CAG. The Reports become public documents after being presented in the Legislature and are placed on the CAG web site. The CAG also writes on an annual basis to the State Chief Minister about the salient points made in the State Audit Reports. An epitome of the Audit Reports is also published.

D. VISION AND MISSION OF STATE PUBLIC AUDIT

6. The public audit function is in the process of renewal. The purpose of public audit is to safeguard the financial interests of the State and to promote accountability and sound and economical management practices. In practice, the CAG's audits are mainly to verify *compliance* with rules and regulations of the Government and the extent to which program objectives have been met, in the effort to assist the Legislature in the exercise of financial control over the executive. Unlike the more developed nations such as UK, Canada or Australia that have a similar constitutional framework of accountability, the focus of audit in India has not been to act as an agent of change and renewal of the public sector, nor to provide independent audit assurance on the *fair presentation* of summary level financial statements of the government in accordance with stated accounting principles and policies. This may however change rapidly given the growing interest of the CAG of India in conforming to evolving international standards of public sector audit, and steps underway to modernize of the public audit system.

7. The absence of any definition of the Expression 'Audit' in the Constitution or in the CAG's (DPCS) Act, 1971 has enabled audit to respond to the continuous changes in the pattern of Government activities, receipts and expenditure, keep pace with the international developments in the profession, and match the rising expectations of the stake holders regarding public accountability.

E. CAG'S AUDITING STANDARDS

8. The CAG has promulgated his own Auditing Standards which prescribe principles and practices to be followed in the conduct of Audit, and constitute the criteria against which the performance of Audit can be benchmarked. The Auditing Standards have drawn heavily upon the Auditing Standards elsewhere e.g. the INTOSAI, albeit tailored to the national environment. These standards and related policies are national, and cannot be changed by the GoO.

F. STRATEGIC AUDIT PLAN AND CUSTOMIZED AUDIT PLANS

9. The AG (Audit) prepares a two year rolling strategic audit plan designed to optimally utilize audit resources, meet the constitutional and statutory obligations of State Public Audit, maintain an element of surprise, and ensure that no auditable unit escapes audit over a prescribed time cycle. Deviations from audit plans are required to be analyzed and explained.

10. Detailed customized Audit Plans are centrally prepared for conducting value for money audit of all India programmes, projects and schemes that feature simultaneously in the CAG's Audit Reports on the Union and the State Governments. Audit plans for conducting Value for money audits of the State Government programmes, are prepared by the AG (Audit).

G. AUDIT TYPES AND APPROACH

11. The AG (Audit) carries out three broad categories of Audit: Financial Statements Audit (essentially for compliance), Financial or Regularity Audit, and Value for Money Audit. Despite this three-fold classification, the audit function is indivisible. The AG (Audit) follows a two track approach: Off-site Audit of vouchers and accounts which is conducted in the office of the Accountant General, and On-site Audit which is carried out by deputing peripatetic audit teams to the offices of the auditees. The latter is the principal instrument of audit. Audit teams prepare the inspection reports on the conclusion of audit after duly considering the replies of the auditees to the preliminary audit memos issued in the course of inspection. A typical inspection report comments upon serious financial irregularities that may need the attention of the Legislature and other irregularities.

H. AUDIT REPORTS

12. The Audit Reports are shown to the executive at the highest level of bureaucracy at the draft stage. Reports are very informative regarding cases of non-compliance with government rules and regulations. Recent Audit Reports have indicated weak budget control, insufficient revenue collection, inadequate accounting reconciliation, large wastage of public resources, inappropriate accounting, poor return on investment, diversion of funds, failure to achieve programme objectives and numerous instances of poor management of public resources including those provided by donors such as the World Bank. The Audit Report for FY02 quotes the specific example of a Rural Development Program in which the auditor tested 42% of the total expenditure and found that only 38% of the test sample was actually spent on the program within the fiscal year. The remaining 62% was either lying unused somewhere, diverted to other uses, or affected by other irregularities.

I. QUALITY REVIEWS

13. Although there exists no formal peer review mechanism at Orissa, CAG's own stringent procedures ensure high quality output. The facts and figures in CAG's audit reports have rarely, if ever, been challenged or disputed, and the Reports enjoy tremendous respect and carry high degree of conviction and credibility. The CAG has his own mechanism for internal control including internal audit. The expenditures and accounts of the offices are audited by different specified offices of the CAG. There is no provision for external audit of the CAG.

J. STRENGTHS

14. The public audit function is characterized by high degree of integrity and competence. Inherent strengths of the State Public Audit in Orissa include: high status of the CAG enshrined in the Constitution; independence from the executive as well as the legislature; freedom of the CAG to define audit scope, determine the nature and extent of audit as well as the scope of his Reports; the requirement that the Audit Reports should be tabled before the Legislative Assembly, and thereafter become public documents; Auditing Standards promulgated by CAG; well-documented Audit Manuals and instructions; strategic audit plans to ensure optimization of audit resources; customized audit plans for conducting specific audit tasks; highly informative audit reports; audit comments based on documentary evidence that ensures their veracity; opportunity given to the executive at each stage to explain and clarify its position; range of pubic sector activities examined and covered; highly professional manner in which the Audit Reports are written; in-built quality control measures for high quality output; and elaborate instructions issued by the state government for settlement of audit objections, response to audit and action on recommendations of Legislative Committees.

K. IMPACT AND FOLLOW UP

15. After being tabled in the Assembly, the CAG's Reports are examined by the appropriate legislative oversight Committee which recommends follow up action. There is no prescribed role for civil society, and public demand or follow up action is conspicuous by its absence.

16. The GoO has pointed to the need for improving executive response to audit observations in the White Paper issued in 2002. The GoO has also instructed that the reply to the inspection report should be sent to the Accountant General (Audit) within one month. The reply to the draft para for the Audit Report should be sent within six weeks; Explanatory Notes on audit paras should be sent to the Legislative Assembly Secretariat within three (now four) months. Action Taken Notes on the recommendations of the Legislative Committees should be sent within six months. Despite the above measures, however, the impact of public audit on Orissa's development agenda appears to be minimal.

L. OPPORTUNITIES FOR IMPROVEMENT

17. The public audit system is not having the desired impact. Perceptions of the auditees in Orissa include that: the CAG's Audit Reports are not timely and speak of matters of the distant past; the reports are too negative and not always presented in a sufficiently constructive manner, and they often do not delve into the cause of the problems detected, and consequently, do not make specific recommendations for operational improvements to governments systems and programs. The auditee points out that there is a call for change in mind-set, making the audit an agency for promoting positive change rather than merely an instrument for the detection of irregularities.

18. In our view the core issue, however, is inadequate response to public audit at all levels, bordering sometimes on indifference on the part of government officials, which has seriously dented the accountability architecture. Inspection reports have been outstanding since 1964-65, the departments do not send replies even to draft paragraphs intended for inclusion in CAG's Audit Reports, explanatory Notes on paragraphs finally included in the CAG's Audit Reports have not been furnished from 1989-90 onwards, and a very large number of recommendations of the Legislative Committees are awaiting implementation. The elaborate system prescribed by Government for the speedy settlement of audit objections, scrutiny of CAG's reports and action taken on reports of the Legislative Committees seems to have become dysfunctional. More than 60% of Draft Paragraphs proposed by the Accountant General (Audit) for inclusion in CAG's Audit Reports for the year ended 31st March 2002 which were sent to the highest level of State bureaucracy at the draft stage were not responded to by the Executive.

19. Neither the senior bureaucracy nor the political masters appear to have demonstrated the will to take concrete action against past irregularities pointed out by audit. There appears to be very little incentive to take action on such transgressions (no matter how severe) given the complexity of procedures for disciplinary action, lack of public demand for financial accountability, and the slowness with which the enforcement machinery works at Orissa in line with other parts of the country.

20. The bureaucracy has expressed a view that very often the decisions are the consequence of the orders of the political executive. In these cases it would be unfair to expect the bureaucrat to be held answerable. It is the Minister who should be held answerable. The dilemma that is faced by the civil servants in similar situations has led to the evolution of a system in the Westminster set up whereby a civil servant in the UK is authorized to point out to the Minster that he has a duty to report to the CAG any decision which the former believes is improper, unlawful or irregular in some material respect. No responsibility attaches to the civil servant where the civil servant is overruled and he has informed the CAG in accordance with the procedure stated above. At Orissa, the civil servant facing such a dilemma has access to the Chief Secretary.

M. CONCLUSIONS AND RECOMMENDATIONS

21. The key problem of external audit as an instrument for reducing fiduciary risk in Orissa State is not the quality of the audit work or its reporting, but its lack of impact as a result mainly of the timeliness of reporting and the very poor response to audit findings by the Executive, and lack of public clamor for better response. Selection of topics for audit, based on more rigorous risk assessment may provide an answer to this problem. Another suggestion from the GoO is to engage auditors to provide an overall assessment with a clear opinion, on the quality of management assessed by audit along with the irregularities encountered.

22. In Andhra Pradesh, the State Government has made further releases of funds to the executing officers contingent upon their rendering replies to the audit inspection reports, audit paragraphs and PAC recommendations[57].

23. The GoO has taken some initial steps to remedy the poor response to audit described above. Among other measures it has set up a committee for each department to follow up on the departmental responses to AG's queries and the actions taken, and also an 'apex' committee headed by the Chief secretary has been established to review the main issues. Implementation of these procedures however has been difficult. There is no ongoing dialogue with CAG on the core issue of indifference towards follow up, or on the related constraints to satisfactory implementation of audit recommendations.

24. A set of indicators has also been prescribed to assess and review the performance and responsiveness of Government departments. One of the indicators prescribed is the disposal of pending audit paragraphs and inspection reports. The rating of the officers could be reflected in their Annual Confidential Reports. The senior officers need to be held accountable for failure to enforce accountability.

To further improve the audit impact in Orissa, we recommend the following measures:

i) senior officers should review the progress of settlement of outstanding inspection reports and paragraphs during their inspection of subordinate offices;
ii) empower Financial Advisors to comment on responsiveness of departmental officers to audit in the Annual Confidential Reports of the latter;
iii) the officers of the Accountant General (Audit) and the Government departments should jointly review the pre-2000 inspection reports and consider whether these still need to be pursued;
iv) Addition of a clause in the CAG's (DPCS) Act, 1971 to make it obligatory for departmental officers to reply to draft audit paragraphs within the stipulated time frame;

[57] In this regard, see box on Government of AP's "Norms of Public Financial Accountability before release and drawl of funds" on page 49.

v) individuals should be held accountable for their acts of omission and commission; and action should be taken which is prompt, visible, and acts as a deterrent against similar lapses and wrong doings;

vi) the AG (Audit) should write management letters to the Secretaries of the Government departments every quarter pointing out the cases of serious financial irregularities and system failures noticed during inspections. The management letter(s) should include the adequacy of follow up action taken on previous audit observations. Additionally, quarterly meetings should be held based on a structured agenda, between the AG (Audit) and each of the involved departmental Secretaries;

vii) strengthen relationship with AGs in order to:

- improve constructiveness and timeliness of external audit report;
- ensure emphasis on systems rather than individual transactions; and
- initiate preventive rather than detective measures; and

viii) clarify the financial accountability of Ministers as distinct from the Controlling Officers of departments and agencies of the GoO.

At question is what additional incentives could be provided for the state's bureaucracy to encourage more timely and substantive response to audit observations.

Box 6

Government of Andhra Pradesh

Norms of Public Financial Accountability (PFA) before release and drawal of funds

The CAG has been conducting periodical inspections to verify transactions and maintenance of important accounts and other records and accordingly, Inspection Reports are issued to the Heads of the Department. All the Secretariat heads and the Heads of the Department are requested to take immediate action on the Inspection Reports/ Audit Paragraphs/ PAC Paragraphs etc. and ensure that necessary action is taken to send replies to at least 50 % of the pending Inspection Reports/ Audit Paragraphs/ PAC Paragraphs for the year 2000-01, latest by September, 2002 failing which further Budget Release Orders will be withheld by the Finance Department pertaining to the relevant schemes.

At the field level, all the Drawing and Disbursing Officers are hereby made responsible to ensure that suitable replies are sent to the Inspection Reports/ Audit Paragraphs/ PAC Paragraphs relating to the Schemes up to 2000-01 and furnish a certificate to the extent that replies to the Audit Paragraphs 2000-01 have been sent pertaining to that particular scheme for which bills are being submitted to the Treasury/ PAOs for the drawal of funds. It is instructed that no amounts would be permitted to be drawn for that particular scheme by the particular Treasury Officer until and unless the DDO submits a certificate that at least 50% of the pending audit paragraphs etc. for years up to and inclusive of 2000-01 have been replied to.

Source: Government of Andhra Pradesh GO No 507 of April 2002

CHAPTER X
LEGISLATIVE SCRUTINY AND OVERSIGHT

A. INSTITUTIONAL FRAMEWORK

1. Legislative oversight over public finance is the keystone of the architecture of responsible government and parliamentary democracy. This involves oversight over the raising of revenues, spending of public moneys and holding the executive accountable for the achievement of the designated goals, objectives and purposes. The legal framework is provided by the relevant provisions of the Constitution of India, the laws framed thereunder and the Rules of Procedure and Conduct of Business in the Orissa Legislative Assembly promulgated under the Article 208(1) of the Constitution. The institutional framework is on par with the framework at the Union Government level and other state Governments. It also compares favorably with other developing countries and is largely at par with more developed Westminster democracies.

2. Legislative oversight over public finance is exercised both before and after the raising of revenues and spending of public moneys. This chapter is concerned mainly with "ex post facto" legislative oversight.

B. MANDATE AND PROCESS

3. The Rules of Procedure and Conduct of Business in the Orissa Legislative Assembly prescribe the constitution of the Committee on Public Accounts (PAC) and the Committee on the Public Undertakings (COPU) for follow up action on CAG's Audit Reports.

4. PAC deals with the CAG's Audit Reports (Civil) and the Audit Reports (Revenue Receipts) which relate to Government departments; COPU deals with the CAG's Audit Reports
(Commercial) on Government companies and corporations. CAG's Audit Reports stand remitted to the appropriate committee after their presentation to the Legislative Assembly.

C. THE COMPOSITION OF THE LEGISLATIVE COMMITTEES

5. Both the Committees are elected by the Assembly from amongst its members (other than a Minister) according to the principle of proportionate representation. The Chairmen are appointed by the Speaker. By convention, the Chairman of the PAC is not from the ruling party. The term of office of members of the Committees is one year. The Committees are provided secretarial support by the Assembly Secretariat. One Section Officer and a prescribed number of assistants are exclusively sanctioned for each of the Committees.

6. GoO instructions require that the Government departments should furnish detailed explanatory notes to the Assembly Secretariat on matters commented on in the CAG's

Audit Reports within a period of three months (recently revised to four months) of their presentation to the Legislature. The Committees are empowered to summon witnesses at the highest level of bureaucracy, send for records and persons, and take evidence. A verbatim record of the proceedings is required to be kept when a witness appears for evidence. The meetings of the committee are not open to the public.

D. REPORTS OF THE COMMITTEES AND FOLLOW UP

7. The Committees generally function in a non-partisan manner and their reports embody the decisions of the majority of the members present and there shall be no minute of dissent. The Committees present their reports to the Assembly as soon as these are ready. Government departments are required to furnish statements of action taken on the Committees reports within six months of their presentation.

E. THE ROLE OF THE ACCOUNTANT GENERAL (AUDIT)

8. The Accountant General (Audit) assists the Committees in their work by scrutinizing the Explanatory Notes as well as the Action Taken Notes of the departments mainly for their accuracy, preparing questionnaires for the examination of departmental officers and supporting the Committees during evidence taking.

F. STRENGTHS OF THE SYSTEM

9. Legislative scrutiny and oversight of public financial accountability has certain inherent strengths, represented mainly by the attributes described above; including both the PAC and COPU have been established under rules framed in terms of a Constitutional provision; all-party representation; Chairman of the PAC from a non-ruling party; prohibition of Ministerial membership; non-partisan nature; majority vote of members present, with no minute of dissent; powers to summon any official; and the support and assistance of the CAG's organization. In addition, conferences of Chairman of the PACs of Union and State Governments are held periodically for a mutually beneficial exchange of views.

G. WEAKNESSES OF THE SYSTEM

10. Notwithstanding their inherent strengths, the Committees have not been sufficiently effective in their main duty of ensuring proper legislative oversight of public finance. The Committee system works largely *in camera* – civil society interface remains minimal. The Committees do not table annual reports on their own performance for the Speaker's attention at the Legislature.

11. The main concerns include the following:

- Both the committees are heavily in arrears; PAC from 1990-91 (Audit Report-Civil); and from 1988-89 (Audit Report-Revenue Receipts) and COPU from1987-88 (Audit Report Commercial).

- Government departments have not furnished "suo moto" Explanatory Notes on Audit paragraphs from1991-92 Audit Report (Civil), 1989-90 Audit Report (Revenue Receipts)

Note: The COPU in their meeting held on 13.08.2002 unanimously resolved to waive audit paras till 1992-93.

Year of Audit Report	**Total paragraphs /reviews in Audit Reports (Civil)**	**Number of paragraphs/ reviews for which explanatory notes were not received**
1991-92	70	10
1993-94	60	18
1994-95	57	14
1995-96	61	15
1996-97	77	56
1997-98	64	37
1998-99	64	60
1999-2000	54	50
2000-2001	54	54
Total	561	314

On average 56% of Audit Observations have not been responded to by Line Departments. Similarly, Explanatory Notes have not been furnished to 221 paragraphs/ reviews out of a total number of 578 paragraphs/ reviews which were included in the audit reports (revenue receipts) from 1989-90 onwards.

- Government departments have also not furnished Action Taken Notes on Committees' recommendations. As many as 3193 recommendations of the Committees are outstanding for implementation.

- Due to non-receipt of explanation for overspending by the departments, excess of expenditure over the budgetary provisions (Rs. 68 billion) had not been regularized from 1996-97 onwards; an important requirement of the Constitution of the financial supremacy of the legislature could not be realized.

- The secretarial support available to the Committees is not commensurate with the nature, variety and complexity of issues dealt with in the CAG's Audit Reports, and followed up by the Committees.

- The currently prescribed tenure of one year for the members of the Committees is considered much too inadequate for the effective discharge of the functions of the Committees.

Box 7
Inadequate follow up action on the recommendations of the Committees

Mention was made in paras 3.15.6.2.1, 3.15.6.3., and 3.15.6.4. (i) of Audit Report (Civil) for the year 1984-85 about the system deficiency under Public Distribution System leading to (1) shortfall in providing fair price shops in hilly and tribal areas, (2) circulation of excess ration cards, and (3) issue of sub-standard quality of food grains to consumers.
PAC in their 75th Report (Ninth Assembly) 1988-89 had asked the department to furnish a comprehensive note indicating the reasons for less coverage in respect of (1) above and to take adequate steps to avoid such situation in future in respect of (3). Action taken notes on the recommendations of the PAC have not been furnished by the Department as of August 2001.
It was, however, observed in audit during subsequent scrutiny that the position has not improved even after 14 years.

CAG's Audit Report (Civil) for the year ended 31st March 2001.

H. CONCLUSIONS AND RECOMMENDATIONS

12. The Legislative oversight and scrutiny system is *not* having its desired impact on the State's development process. The core issues are the lack of *timely* hearings on transgressions pointed out by audit, as well as the inadequate executive response to both audit and subsequent recommendations of the oversight Committees of the Legislature. There are several factors involved. The main reasons for this, however, are a mindset at both the bureaucracy and the political culture that is symptomatic of working *in camera*, along with general apathy to public financial accountability, and the absence of any effective punitive action for failure to respond in a timely manner to audit observations and recommendations of the Committees. The need is also evident for better research and organizational support to the Committees, and more civil society participation in their deliberations.

13. Adequate and timely, corrective and remedial action is the essence of effective financial accountability, the absence of which can breed unhealthy cynicism in the entire accountability architecture. At issue is the use of public money for development and fighting poverty.

14. Suitable strategies need to be considered for overtaking the backlog of arrears and strengthening the oversight function of the Legislature.

15. Both the PAC and the State Government have shown heightened consciousness of the need for giving timely response to Audit paragraphs and PAC recommendations with time bound targets. The measures suggested in this paper are expected to fast forward the work of the Committees and enhance their impact on the state's development process. The role the Speaker of the Assembly and civil society decide to play could be crucial for the way reforms can be affected. Accountability delayed is, like justice delayed, accountability denied to the citizens of Orissa and India – rich and poor.

16. Public pressure is an important element in the governance process that determines the efficiency of public services, which in turn ultimately depends on sound management of public funds. In Orissa, as in many other States, the civil society needs to be energized and assisted to generate such pressure. The State Government could take the initiative to evolve suitable arrangement by which informed citizens may act as pressure groups to assist in securing better compliance of principles of public accountability. For example, the Action Taken Report on Audit observations presented to the Legislature could be discussed and commented upon by group(s) of concerned citizens so that public interest and pressure could be generated on vital issues of audit of public funds.

We recommend the following improvements:

i) encourage enlargement of the role of AG (Audit) in following up cases of previous Audit Reports which the Committees may not like to pursue for detailed examination. In such cases the Committees may obtain specific recommendations of the AG (Audit) whether the departmental replies are acceptable and thereafter decide the further course of action. A stringent time schedule needs to be laid down and followed for this exercise;

ii) suggest to the Speaker that Committees may consider adoption of a similar procedure of examination of selected paragraphs even of current Reports. The Committee should discuss the most recent reports of the CAG as a matter of priority. The principle of “last in first out ” is one way to address the issue;

iii) include in the annual confidential reports of the departmental officers, an assessment of the quality of response to the audit reports and recommendations of the Committees;

iv) provide the Committees with secretarial assistance at sufficiently superior levels commensurate with the nature, variety, and complexity of issues dealt with by them; appointment of experts on short term contracts may be considered;

v) suggest to the Speaker that members of the Committees should have longer tenure; continuity and change can be ensured by stipulating that one third of the members retire every year; and

vi) civil society should be sensitized and involved in the accountability process. Transparency has its undoubted advantages. In more developed democracies the hearings of the Committees are open to the public. A beginning may be made by issuing a detailed press release at the end of each sitting of the Committee. An annual report of the work done by the Committees could also be presented to the House listing the accomplishments of Committee members and any constraints faced by them. Both these measures will ultimately promote greater involvement of the civil society in ensuring public accountability.

CHAPTER XI
FIDUCIARY RISK

A. THE OBJECTIVE

1. One of the objectives of this report, as stated in the opening chapter, is to assess the extent to which public funds in Orissa are exposed to the risk of being used for purposes other than those for which they are intended; or without due regard to economy and efficiency; in other words, to assess the fiduciary risk[58] to which such public funds are exposed. In trying to form a judgment on this matter, the Orissa SFAA team considered the following:

- the fiduciary risk assessment methodology of OECD/ DFID;
- evidence from projects financed by the World Bank in Orissa State;
- independent assessments of perceived levels of corruption; and
- evidence presented in Chapters I through X of this report.

B. FIDUCIARY RISK METHODOLOGY OF OECD AND DFID

2. This methodology basically poses nineteen questions under seven main headings in an effort to determine levels of fiduciary risk. When we asked these questions about Orissa State, we found that the State complies with fifteen out of nineteen criteria in the methodology. We also found, however, that the methodology apparently fails to assign different weights to the different questions. We believe, for example, that the question of whether rules and regulations are actually *implemented* should carry more weight than questions about the existence of those regulations on paper. *A library full of the best laws in the world can provide no assurance on fiduciary risk if the laws are not implemented effectively*. This methodology provides a limited basis for assessing the fiduciary risk as articulated in the Banks Articles of Agreement.

C. EVIDENCE FROM WORLD BANK-FINANCED PROJECTS

3. A recent special review of project audit reports in Orissa State (and Uttar Pradesh State) concluded that there is limited assurance on the fiduciary risk attaching to Bank provided funds because:

[58] The Bank's Charter (Article 111 Section V (b) of IDA's Articles of Agreement) specifies that : " The bank shall make arrangements to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other non-economic influences or considerations".

- it is difficult to judge from project audit reports whether or not there is independent assurance that the funds are actually being *used* (as distinct from spent) for the purposes for which they were intended[59]; and

- project audit reports do not address the economy and efficiency aspects of project implementation.

- The financial management arrangements at the 'project level' are subject to similar constraints and shortcomings seen at the state level. While 'ring fenced' systems are in place at the project level to provide timely information on the project expenditures and physical progress, the issues of reliability of the information remain. This is largely on account of the inability to reconcile the expenditures with the Government accounts and results in CAG annual reports certifying only part of the expenditures reported.

- Additionally, annual CAG audit reports provide only a limited level of assurance on the use of the funds - focused essentially on certifying the SOEs and not the total project expenditures. Delays in providing funds for project implementation have been a standard feature of the Orissa portfolio. Though the State provides quite adequately for the project requirements in the budget, cash liquidity problems often result in less than adequate funds being put in the hands of the Departments/Project Units for implementation purposes. This leads to inefficiencies in project management. Follow up on audit observations is weak, resulting in substantial disallowances being adjusted by the Bank[60].

D. INDEPENDENT ASSESSMENTS OF PERCEIVED LEVELS OF CORRUPTION

4. One of several parameters which assist in determining the level of fiduciary risk is the level of reported corruption. In Orissa State there has not been a Country Procurement Assessment Report (CPAR). Authoritative international organizations, such as Transparency International (TI), do not normally publish indices of perceptions of corruption within states in a country. There is, therefore, no really authoritative assessment of the level of corruption in Orissa State, nor is there any reliable way of comparing corruption levels in Orissa State with that in other States in India or in other countries. The latest TI index placed India as a whole in 79th position out of 90 countries, denoting a relatively high level of perception of corruption at the " Country " level.

5. A DFID-financed study of anti-corruption efforts in Orissa State was undertaken in FY 2002. This study did not attempt to determine the level of corruption, either in

[59] Based on a letter of the Country Director, The World Bank, dated January 15, 2003 addressed to the Department of Economic Affairs, Ministry of Finance, GOI, it is understood that a review of the independent audit reports submitted for the India portfolio of investment projects indicates that in the State of Orissa, Bank funds totaling Rs. 284 million (out of India total of Rs 1536 million) have been used for **ineligible** expenses.

[60] The GoO has established in each department Audit committees to monitor progress on audit findings as well as an Apex Committee headed by the Chief Secretary to review the process and monitor the follow up at each department.

absolute terms, or in relation to other Indian States or other countries. Its justification for the study is that: "The problem of corruption is said to have become deep rooted and to be getting more serious and widespread." The Bank was informed that GoO plans to formulate and adopt a broader anti-corruption strategy based on wide-ranging consultations and public debate[61].

6. The study identified both the strengths and the weaknesses in the way in which corruption is being tackled by GoO and goes on to recommend that GoO should develop a simple, clear, coherent and complete strategy to deal with enforcement of the laws against corruption; education of the whole community on the dangers of corruption; and development of public support. The report has a total of twenty-four recommendations for reducing corruption in Orissa State[62].

7. None of the report's analyses, however, helps us in judging the absolute or relative level of corruption in Orissa State, or its impact on the level of fiduciary risk.

E. THE ANALYSIS IN THIS REPORT

8. The facts and analyses in Chapters I through X of this report probably represent our most reliable source of information for assessment of the level of fiduciary risk in Orissa State. The clearest message emerging from those analyses is that although central laws, standards and norms predominate in such key areas as budgeting, accounting and auditing, the State nevertheless, has scope to manage its resources, and thereby determine the level of fiduciary risk to which they are exposed. It is precisely in this area of the implementation of existing laws and standards that wide gaps between theory and practice have been observed, as we illustrate below with a few examples flowing from this report.

③ **Impact of unrealistic revenue forecasting which ignores the norms of proper budgeting** is illustrated in the table below;

Risk: Budget is not realistic. This has adverse consequences on expenditure management and integrity of the approved plans (also refer "Budget implementation" and "Cash Management" on Pages 15 – 17 of this report).

FY 02 BUDGET Vs. ACTUAL

(Amount: rupees in billion)

	Budget Estimate	Actuals	Difference	% of difference over budget
Revenue Deficit	18	28	10	56
Fiscal Deficit	33	40	7	21

[61] Orissa MOP March 28, 2003 prepared by PREM

[62] The GoO has acknowledged the need to address issues of fraud, waste and abuse of public funds. The GoO has put in place an internal vigilance unit in each of the three major non wage spending departments.

③ **The regulation requiring monthly reconciliation of accounts is not being complied with in a significant number of cases.**

Risk: Untimely/non detection of Fraud and Misclassifications and uncertainty regarding proper utilization.

Reconciliation's between AG & Concerned Controlling Officers FY 2001-02	
No. of accounts for Reconciliation	290
Reconciliation's not done	46
	16% accounts un-reconciled

③ **Rural Local Bodies (PRIs) do not present Utilization Certificates in time, as required by regulations. Amounts pending appear to be larger than necessary.**

Risk: Delays in project implementation

Pending Utilization Certificates	
	(rupees in million)
1998/99 to 2002/03	910

③ **Rural Local Bodies (PRIs) are not being audited on a timely basis.**

Risk: Untimely/non detection of fraud, waste and abuse of funds and delay in appropriate remedial and corrective action.

Pending Audits up to 2001/02	
	(rupees in billion)
Gram Panchayat	130-on average 25% in default
Panchayati Samiti	Information not Available
Zilla Parishad	No Audit Started

③ **State-owned enterprises are heavily in arrears in presenting their audited accounts.**

Risk: The investment in State-owned companies is under managed

Status of Annual Accounts	
No. of Companies	Extent of Arrears
33 Working Companies	85 % in default (up to 8 years)
35 Non Working Companies	100 % in default (up to 36 years)
♣ Accounts are heavily in arrears ♣ All audit reports are qualified ♣ Qualifications in audit reports could be interpreted as virtual denials of an auditor's opinion	

③ **The Executive does not respond adequately to external audit.**

Risks: 1. Improvement in systems and procedures get delayed; and
2. Enforcement is weakened

Audit Report F/Y 02				
1.	Response to inspection reports (1964/ 65) and onwards (cumulative)	18,150 (11% higher than in FY01 report)		
		Civil	**Commercial**	**Revenue**
2.	No. of paragraphs forwarded	36	17	56
	No. of paragraphs for which reply to AG was not given	24	13	30
		Civil		**Revenue**
3.	No. of paragraphs included in audit reports	561		578
	No. of paragraphs for which explanatory notes were not given to legislature	314 (from 1991/92)		221 (from 1989/90)
4.	Action taken reports (ATRs) not provided since 1991 onwards			

Source: Data Published by the Comptroller & Auditor General of India

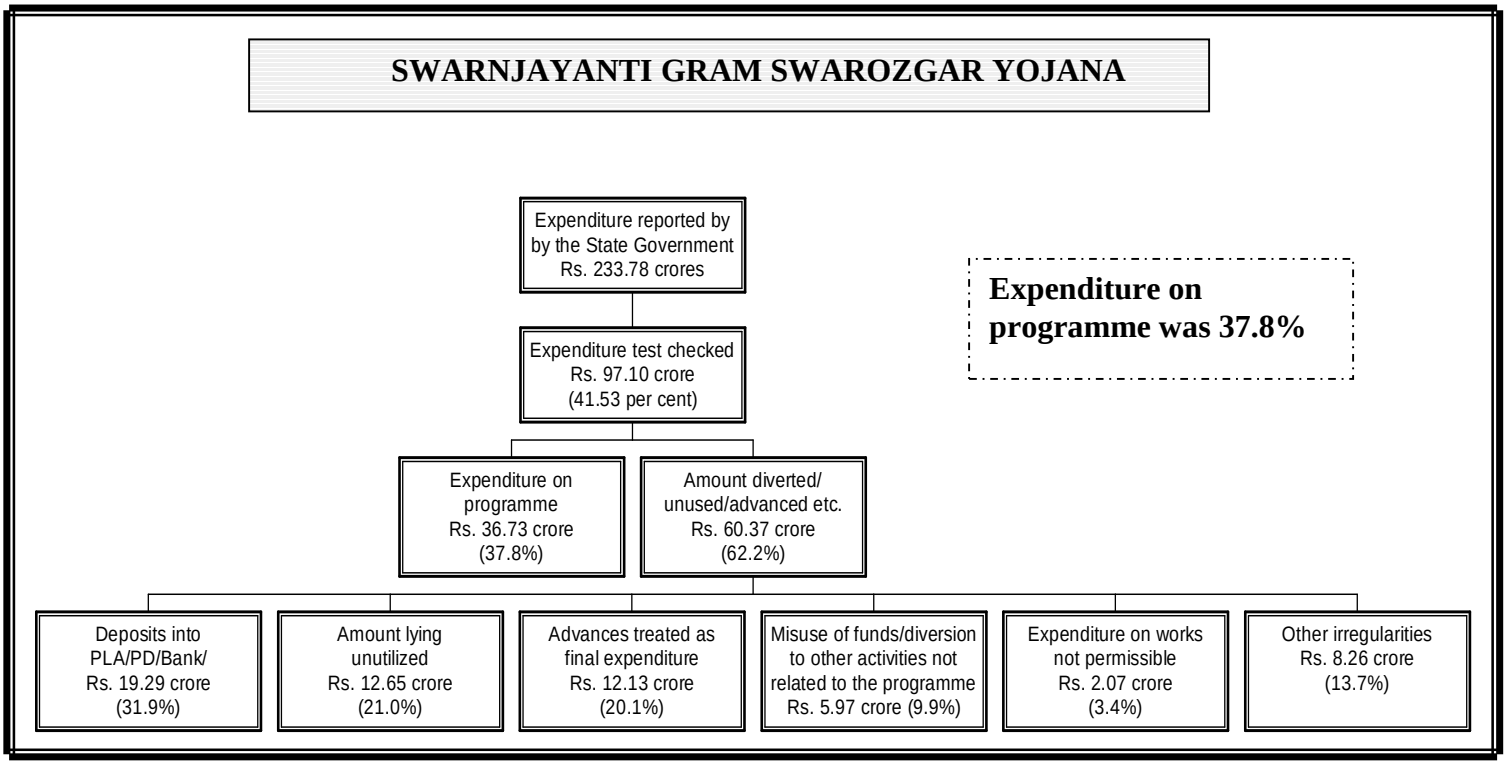
- **Excess expenditure is not being regularized by the legislature as required under the Constitution. Cumulative unauthorized expenditure is rising.**

Risk: Legislature Control of the State budget is weakened

Excesses over grants not regularized				
FY/ 98	FY/ 99	FY/ 00	FY/ 01	FY/ 02
Rs. 11 billion	Rs. 12 billion	Rs. 39 billion	Rs. 64 billion	Rs. 68 billion

③ **In, perhaps, the clearest illustration of lack of assurance that funds are being applied to their intended purpose, 62% of the tested expenditure in a rural development program was irregular in one respect or another. Only 38% of the tested sample was actually used on the program.**

Risk: Funds are not being fully used for purposes intended



Source: Pg. 129, Report of the Comptroller and Auditor General of India, for the year ended 31 March 2002 (Civil), Government of Orissa

Note: Rs. 1 crore = Rs. 10 million

9. We compared the audit reports of Orissa with the situation at Karnataka, Andhra Pradesh, Uttar Pradesh, and Tamil Nadu, and found on the whole a remarkable similarity in the messages being conveyed by the State's external auditor's reports. These reports point to significant fiduciary risk at SOEs, state and local governments.[63]

10. In the light of the above analysis and examples, the risk that public funds in Orissa may not be used for the purposes intended with due regard for economy and efficiency is quite significant. The GoO is aware of the problem, aspects of which it has, frankly and creditably, acknowledged in its 2002 'White Paper on Public Expenditure and Administrative Reforms': for instance the need to reform the entire budgetary process and the need to respond to external audit findings to mitigate the risk of delayed remedial measures.

11. We would commend the GoO for developing and implementing a Development Action Plan on the lines recommended in this Assessment.

[63] The GoO has decided to launch an expenditure tracking of selected major programs to identify leakages and improve targeting and efficiency.

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List of Persons Met

1. Dr. Bannerji, Joint Secretary, Ministry of Finance (State Plans), Government. of India
2. Dr. P.K. Choudhry, Deputy Director, Dept. of Public Enterprises.
3. Dr. R.V. Singh, Director, Planning and Coordination Department.
4. Executive Engineer, Prachi Irrigation Division, Government of Orissa
5. Mr. A K Naik, Block Development Officer, Panchayat Samiti, Ghatagaon.
6. Mr. A.K. Sabat, FCA, Partner of A.K.Sabat & Co, Chartered Accountants.
7. Mr. A.K. Samantaray, IAS, Principal Secretary, Dept. of Housing & Urban Development.
8. Mr. Ashok Patnaik, Deputy Direct, Dept of Public Enterprises.
9. Mr. Aurobinda Mishra, Deputy Secretary, Finance Department, Government of Orissa.
10. Mr. B. Baral, (Audit Superintendent)
11. Mr. B. K. Patnaik, Secretary, Water Resources.
12. Mr. B.B. Singh Samanta, Engineer-in-Chief, Irrigation Department, Government of Orissa
13. Mr. B.K. Nanda, Director of Treasuries, Government of Orissa
14. Mr. B.K. Tripathy, Dy.Director (Accounts), Finance Department, Government of Orissa
15. Mr. B.P. Misra, Director, Municipal Administration, Dept. of Housing & Urban Development.
16. Mr. Bimbadhar Patro, Audit Officer, (Head Quarter)
17. Mr. C S Mishra, Project Director, DRDA & Executive Officer, ZP, Keonjhar.
18. Mr. C. Venkatramana, Chairman-cum-Managing Director, National Aluminium Company Ltd.
19. Mr. C.J. Venugopal, IAS, Managing Director, Orissa Mining Corporation Ltd.
20. Mr. D Naik, Additional Block Development Officer, Panchayat Samiti, Ghatagaon.
21. Mr. D.C. Sethi, Executive Officer, Gopalpur NAC
22. Mr. D.K. Das, Resident Manager, Adam Smith Institute & Formerly Executive Director (Finance), Industrial Development Corporation of Orissa Limited.
23. Mr. D.K. Samantray Executive Director (Finance), Orissa Mining Corporation Ltd.
24. Mr. D.N. Padhi, IAS, Chairman-cum-Managing Director, Orissa Hydro Power Corporation Ltd. & Principal Secretary, Dept. of Energy.
25. Mr. D.V. Kurien, Adviser, Planning Commission, Government Of India.
26. Mr. Dhirendra Swarup, Additional Secretary (Budget), Government. of India
27. Mr. G.B. Mukherjee, Principal Secretary, Forest Department, Government of Orissa
28. Mr. Gunanidhi Jena, OAS, Chief Executive, Cuttack Municipal Corporation.
29. Mr. J. Panda, Secretary, Primary Education.
30. Mr. J. Sethi, Deputy Secretary & Project Director, Urban Poverty Alleviation Cell
31. Mr. J.K. Mohapatra, IAS, Commissioner-Cum-Secretary Department of Public Enterprises
32. Mr. Jena, Financial Adviser, Agriculture.

33. Mr. K.C. Badu, Addl. Secretary, Department of Finance, Government of Orissa
34. Mr. K.N. Ravindra, Company Secretary, National Aluminium Company Ltd.
35. Mr. M R Debrata, Block Development Officer, Panchayat Samiti, Khurda.
36. Mr. M. Naveen Kumar, IA & AS, A.G. (Audit-II), Orissa
37. Mr. Mahalik, Under Secretary, Dept. of Local Fund Audit.
38. Mr. Misra, Financial Adviser, Panchayat Raj Institutions.
39. Mr. N. Roy, Financial Advisor, Forest Department, Government of Orissa
40. Mr. N.C. Das Ex. Managing Director, Orissa Mining Corporation Ltd.
41. Mr. Narottam Das, Ex-Director, Finance, Industrial Development Corporation of Orissa Ltd.
42. Mr. P.C. Mishra, Financial Advisor, Panchayat Raj Department, Government of Orissa.
43. Mr. P.K. Mishra, Financial Advisor, Panchayat Raj Department, Government of Orissa.
44. Mr. P.B. Misra, Financial Adviser & Joint Secretary, Dept. of Housing & Urban Development.
45. Mr. P.K. Mishra (Audit Superintendent)
46. Mr. P.K. Mishra, Special Secretary, Finance Department, Government of Orissa
47. Mr. Pattanaik, Secretary, Public Works Department.
48. Mr. Poti, Scretary, Rural Development
49. Mr. Pradhan, Additional Secretary and Financial Adviser Water Resources
50. Mr. Pradhani, Financial Adviser, Rural Development.
51. Mr. R N Dash, Director (Special Projects), Panchayat Raj Department, Government of Orissa.
52. Mr. R V Singh, Special Secretary, Planning and Co-ordination Department, Government of Orissa.
53. Mr. R. Misra, Director, Finance, Grid Corporation of Orissa Ltd.
54. Mr. R.N. Das, IAS (Retd) Ex. Chairman, Orissa Mining Corporation Ltd., Ex-Chief Secretary, Government. of Orissa.
55. Mr. R.R. Misra, IRS, Director Finance, Orissa Hydro Power Corporation Ltd.
56. Mr. S S Sethi, Additional Project Director, DRDA, Khurda.
57. Mr. S.B. Parida, OAS, Executive Officer, Puri Municipality
58. Mr. S.C. Bhadra, FCA, Partner of SRB & Associates, Chartered Accountants.
59. Mr. S.K. Panda, OAS, Executive Officer, Berhampur Municipality
60. Mr. S.N. Pradhan, (Audit Superintendent)
61. Mr. S.S. Patnaik, Addl. Secretary, Department of Finance, Government of Orissa
62. Mr. S.W. Oak, Principal Chief Controller of Accounts, Central Board of Direct Taxes, New Delhi.
63. Mr. Samal, Secretary, Orissa Legislative Assembly
64. Mr. Sapneswar Baya, Director (Grama Panchayats), Panchayat Raj Department, Government of Orissa.
65. Mr. Sarangi, Secretary, SC, ST and Tribal Welfare.
66. Mr. Senapati, Joint Secretary, Orissa Legislative Assembly
67. Mr. Sidhartha Pradhan, IRS, Commissioner of Income Tax (Admn. Bhubaneswar) and formerly Secretary, Special Secretary & Addl. Secretary, Dept. of Public Enterprises.

68. Mr. Srinivas Rath, Development Commissioner and Secretary, Planning and Coordination.
69. Mr. T.K. Misra, Secretary, Food and Civil Supplies.
70. Mr. T.K. Misra, Special Secretary, Transport
71. Mr. Tripathy, Finance Secretary
72. Mr. Utpal Bhattacharya, Principal Accountant General, Orissa.
73. Mrs. Anita Pattnaik, IA & AS, A.G. Audit-I, Orissa
74. Mrs. Anusuiya Basa, DG of Audit, CAG, India
75. Mrs. Aruna Makhan, Controller General of Accounts, New Delhi.
76. Smt. Alka Panda, Secretary, Agriculture.
77. ----------, Grama Panchayat Extension Officer, Panchayat Samiti, Khurda.
78. ----------, Grama Secretary, Uparadiha Grama Panchayat.
79. ----------, Sarpanch, Narangarh Grama Panchayat.

Dr. U. Sarat Chandran,
Principal Secretary to Govt.,
Finance Department,
Orissa.

☎ 0674 –2536950 (O)
2535532 (R)
0674 – 2405755 (Fax)

D.O. No. 20376 /F.,
Bt-V-12/2004
Bhubaneswar – 751 001

Dated: 10.5.04.

Dear Mr Carter,

Sub. : Development Action Plan (DAP) under State Financial Accountability Assessment (SFAA)

I am enclosing the Development Action Plan (DAP) prepared under State Financial Accountability Assessment Study for the State of Orissa and approved by Government. This is in continuation of this Department letter No. 49756/F., dated 24th November, 2003 and D.O. letter No. 54915/F., dated 29th December, 2003.

With regards.

Yours sincerely,

Sarat Chandran.

(U. Sarat Chandran)

Mr. Michael F. Carter,
Country Director, India
The World Bank, 70, Lodi Estate,
New Delhi - 110003

Development Action Plan Matrix for Orissa
STATE FINANCIAL ACCOUNTABILITY

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
Category – A							
1	Improve the enforcement of existing laws and regulations, including, response to inspection reports and audit paragraphs, PAC and COPU requests, recommendations and enforcement of penalties for non compliance	**a)** Apex Committee has been established under the Chairperson of the Chief Secretary at the State Level **b)** Monitoring Committee at department level constituted. **c)** Monitoring the monthly progess has been institutionalized by Secretary, Finance Department. **d)** Departmental Secretaries and FAs are specifically made responsible for compliance vide Chief Secretaries letter No. 2099 dated 13/1/2003.	Compliance of the reported pendency	July 2004		FD	Compliance to all all audit paras appearing in audit reports for 31/3/2001 of action report on the recommendation of PAC during 10th and 11th Assembly.
2	Prepare and implement a program for the step-by-step computerization (details given separately) and networking of the accounting system of the State Government, the PRIs, ULBs and SOEs and linking GoO with CAG systems	**a)** Computerization in the Treasuries is at the VLC level. **b)** Decision is being taken to entrust a Consultant for computerization of the entire process linking transactions from Treasuries to Finance	i) Networking accounting system from treasury to FD as per the **Concept Paper** annexed.	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	DFID / WB for provision of fund FD for implementation	On-line accounts
			ii) System to be put in place in the disposal of the Audit	ii) 31-10-2004		ii) FD	ii) Access to PRI data from PR Department

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
		Department as suggested by SFAA (**A Concept Paper is prepared**). c) Computerisation process has already started and the data is available in PR Department website **d)** The system of Commercial Tax Dept. has been studied, tasks identified and entrusted to the Consultant to establish linkage between vehicles passing through the check posts with the Head Office and other check posts	Officers for accessing data from PR Department				
			iii) Pilot running, Test and Acceptance and implementation	iii) May 2004		**iii)** CCT & FD	iii) Establishment of connectivity between Check gates and Headquarters
3	Implement greater transparency, disclosure, result and performance orientation, and openness in both reporting and dissemination of financial and output information in budgeting accounting, financial reporting, internal control and audit, external audit.	**a)** GP audit has been brought under the control of Finance Department **b)** Format for maintaining GP account has been improved as instructed by the CAG **c)** Government have agreed to maintain accounts and audit them as per the technical guidance and supervision of the CAG	i) Accounting Network from Treasury to Finance Department	i) November 2004 or 32 weeks from the date of entrustment	i) Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	i) DFID / WB for provision of fund FD for implementation	i) On-line accounts
			ii) Improvement in the accounting of the PRIs including training of the gram panchayat personnel and clearing the audit backlog	ii) 31st March 2005		ii) FD	ii) The accounting system improved and arrear audit backlog cleared and training of Sarpanchs and Secretaries of GP

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
		d) The Amendment Bill of GP Act is placed in the State Legislature e) Various Executive instructions have been issued to improve the operational and reporting standard f) One training programme on ToT to improve the audit standard has been completed g) Funds arranged for improvement of the accounting system in PRIs and ULBs h) Compliance of the Audit objection by CAG and PSE is institutionalized	iii) Publication of Accounts on the Government website regularly	iii) 1st December 2004	iii) Computerization of Treasuries and FD is completed by 31st August 2004	iii) DFID / WB for provision of fund FD for implementation	are completed iii) Data available on website
4	Hold "Controlling Officers" answerable for the operating performance of their departments, including action taken in response to public audit and legislative scrutiny, in line with the stated responsibilities of secretaries to the Government	This has been reiterated by the Chief Secretary in a D.O. letter addressed to the Chairman PAC vide letter No.21857 dt.19.5.2003.					
5	Implement a capacity building programme	Training ToR has been agreed and signed with	i) Finalisation of training design and	i) 31-4-2004	i) Approval by DFID/WB	i) DFID / FD	iii) Finalisation of Training plan &

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	including staff training, support with consultants and other resources to implement the DAP prepared by the GoO as a result of this SFAA.	DFID	plan for the officers / personnel involved in expenditure control and budgeting and implement the suggestion of the SFAA				design
			ii) Engagement of training consultant	ii) 31-5-2004	ii) DFID finalises the contract	ii) DFID	ii) Entrustment decision
			iii) Completion of training of some key officers / personnel involved in expenditure control and budgeting and implement the suggestion of the SFAA	iii) 31-5-2004	iii) Fund is provided	iii) DFID / FD	iii) Training completed
			iv) Training of officers / personnel involved in expenditure control and budgeting and implement the suggestion of the SFAA	iv) December 2005	iv) Financial & consultancy support are provided	iv) DFID / FD	iv) Training Completion data
			v) Training design at the induction level of the OFS officers	v) 31st May 2004	v) Consultant Support is to be provided	v) DFID / FD	v) Training design
			vi) Training of Audit Personnel /	vi) 31st March 2005	vi) Approval of training plan and	vi) FD	vi) Completion of training

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
			Secretaries and Sarpanchs of gram Panchayats		engagement of Consultancy		
Category – B							
Budget Preparation & Approval							
1	a) Present annual expenditure projections for the medium term to the Legislature	GoO have drawn up a medium term fiscal plan projecting resources and expenditure in accordance with the recommendation of the EFC and has entered into an agreement in form of an MoU with GoI.	Budget to be formulated basing on such agreement	31st July 2004		FD	Annual Budget
	b) Ensure that enhanced revenue forecasting procedures are instituted	The revenue forecast is being made by the FD in consultation with TRS branch of CCT (O). For other departments like MV, Excise, Revenue etc. forecast is made during the budget exercise in consultation with the concerned department.	Tax Research Cell to be constituted in FD and other revenue collecting Departments.	31st July 2004		FD and other related departments	Constitution of the Research Cell
	c) Train State Government officers in budget formulation, tax administration and budget monitoring	Training ToR has been agreed and signed with DFID	i) Finalisation of training design and plan for the officers / personnel involved in expenditure control and budgeting and implement the	i) 30-4-2004	i) Approval by DFID/WB	i) DFID / FD	iii) Finalisation of Training plan & design

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
			suggestion of the SFAA				
			ii) Engagement of training consultant	ii) 31-5-2004	ii) DFID finalises the contract	ii) DFID	ii) Entrustment decision
			iii) Completion of training of some key officers / personnel involved in expenditure control and budgeting and implement the suggestion of the SFAA	iii) 31-5- 2004	iii) Fund is provided	iii) DFID / FD	iii) Training completed
			iv) Training of officers / personnel involved in expenditure control and budgeting and implement the suggestion of the SFAA	iv) December 2005	iv) Financial & consultancy support are provided	iv) DFID / FD	iv) Training Completion data
			v) Training design at the induction level of the OFS officers	v) 30th April 2004		v) DFID / FD	v) Training design
			vi) Training of Audit Personnel / Secretaries and Sarpanchs of gram Panchayats	vi) 31st March 2005		vi) FD	vi) Completion of training
2	Initiate procedure	The line departments	On line monitoring	November 2004	Funds are to be	DFID / WB for	On line computer

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	involving Line departments, including FAs in the budgetary process more intensively	are being associated with budgetary process by holding pre-budget scrutiny meetings under the chairmanship of FD's representative with the membership of FAs of the concerned department and the executing authority.	through computerized network	or 32 weeks from the date of entrustment	provided and entrustment order is issued to the Service Provider by 31st December 2003	provision of fund FD for implementation	network
3	Realistic forecast of a) external assistance b) tax and non tax revenue	a) The Budget is prepared by forecasting external assistance as per discussion with the GoI and other funding agencies. b) Being assessed by the Concerned Departments based on past figures	a) Forecasting should be limited to firm commitment and on on-going projects*			a) FD	a) Realistic Budget forecast
			Tax Research Cell to be constituted in FD and other revenue collecting Departments.	b) Annual Budget 05-06		b) FD	b) Assessment of the revenue by Tax research cells
4	Provide sufficient time for more informed debate on budget	Budget exercise now begins in the month of November and is presented in the OLA by end of February and is being discussed for the entire month of March before it is passed.	Periodical Review of the Budget implementation and Forecast.	Annual Budget 05-06	Computer Networking is established and on line information is obtained	DFID / WB for provision of fund FD for implementation	On line accounts

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
Budget Implementation & Monitoring							
1	Train and build awareness to replace budgetary optimism		i) Completion of training on Budget formulation and implementation ii) On line Data retrieval on budgetary expenditure for analysis	i) December 2005 ii) November 2004 or 32 weeks from the date of entrustment	i) Financial & consultancy support are provided ii) Funds are to be provided and entrustment order is issued to the Service Provider by 31st	i) DFID / FD ii) FD	i) Training Completion data ii) On-line accounts
2	Set up a tax research Unit in Finance Department	The revenue forecast is being made by the FD in consultation with TRS branch of CCCT (O). For other departments like MV, Excise, Revenue etc. forecast is made in the budget exercise in consultation with the concerned department.	Tax Research Cell to be constituted in FD and other revenue collecting Departments. *	31st July 2004		FD and other related departments	Constitution of the Research Cell
3	Train staff in specific areas of mid term forecasting of revenue, scientific revenue estimation and preparation of performance budgets and reports	A **Concept Paper** is prepared.	i) Networking accounting system from treasury to FD **A concept Note is provided on this aspect separately.** *	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	DFID / WB for provision of fund FD for implementation	On-line accounts
			ii) System to be put in place in the disposal of the Audit Officers for accessing data from PR Department	ii) 31-5-2004		ii) FD	ii) Access to PRI data from PR Department

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
5	Reduce incidence of excesses and savings		On line monitoring of budgetary allocation and expenditure through computerised network	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	DFID / WB for provision of fund FD for implementation	On-line accounts
6	Disclose major assumptions and high risk areas and also fully disclose contingent liabilities and actuarial evaluation of pension obligations in years to come		i) A separate chapter is to be included in the Budget Document disclosing major assessments and high risk areas.	Annual Budget 05-06		FD	Budget at a Glance
		A Civil Service Employees database is in the process of development, with support from DFID, in the FD	ii) Employee database is made fully operational.	31st December 2005	Extension of support for Employee Database.	DFID / FD	Employees Database
7	Take steps to prevent deficient asset management	Steps have already been taken for proper management of assets in all the line departments and instructions from FD are already issued.					
Internal Control & Internal Audit							
1	Speed up the Review of rules and regulations as proposed in the White	a) Suspension of benefits of Surrender Leave Encashment	Budgeting to be made more realistic & streamlined with	Annual Budget 05-06	Online compuetrisation is complete and	FD / DFID & WB	More effective mecjanism of budgeting and

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	Paper of 2002	and Leave Travel Concession w.e.f. 01.04.2002 b) Organisational Review started to locate surplus staff c) VR Scheme has already been declared by GoO d) Grant-in-Aid regulation has been passed and being implemented e) GP audit establishment has been brought under FD and basic format for maintenance of account are changed as suggested by CAG. f) The GP Act has been placed before the Legislature for amendment.	proper and well structured internal audit deployed with well defined mandate.		operational and training of officials is completed.		control
2	Introduce formal Risk Management through exception reporting for high risk areas	Efficiency Audit is being conducted in High Risk areas	Conducting efficiency audit in high risk areas is to be institutionalized	31-05-2004 *		FD	Efficiency Audit report in high risk areas.
3	Prepare Quarterly analysis and reports on variations between Budget and Actuals (physical and financial)		Computerisation of treasuries defining physical parameters	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	DFID / WB for provision of fund FD for implementation	On-line accounts

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
4	Involve FAs in all significant Financial management decisions		Letter to be issued to all Departments highlighting the significant role being played by the Fas and his duties and responsibilities *	31-4-2004		FD	Instruction to all departments on FA's role
5	Make internal audit report directly to the secretary		Instruction to all administrative departments to submit a report of audit conducted in their department by common cadre auditors directly to the Secretary of the department with a copy to FD *	31-4-2004		FD	Instruction to all departments
6	Provide Proper orientation and regular training on modern internal audit techniques		This will be covered under the detailed training programme	March 2005		FD	Completion of Training
Accounting & Financial Reporting							
1	Monthly accounts should be provided on each department and a consolidated statement of actuals and budget within 6 weeks of close of the month		Computerisation of treasuries and Finance Department for availability of information within specified time limit Availability of detail accounts on the web	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	DFID / WB for provision of fund FD for implementation	On-line accounts
2	Define within 6 months how to reconcile or write off differences between		Computerisation of treasuries and Finance Department	November 2004 or 32 weeks from the date of	Funds are to be provided and entrustment order is	DFID / WB for provision of fund FD for	On-line accounts

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	departments, treasuries and other agencies of offices		for availability of information within specified time limit Reconciliation would be done by the computers automatically. (refer to the concept note) Availability of detail accounts on the web	entrustment	issued to the Service Provider by 31st December 2003	implementation	
3	Discontinue unnecessary transfers from Consolidated Account to "Deposits" in the Public Account		Discontinue depositing in Civil Deposit indiscriminately	Annual Budget 05-06	Improvement in Ways & Means position & Successful implementation of financial management system	FD	75% reduction in Civil Deposit
4	Issue Annual Financial Statements of the State within six months following end of the fiscal year and place monthly statements on Net		Computerisation of treasuries and Finance Department for availability of information within specified time limit Availability of detail accounts on the web	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service Provider by 31st December 2003	FD	On-line accounts on website
5	Disclose Annual Appropriation Accounts Explanations for savings and excesses (Grants)	Already being placed in the Assembly	To be put on web	November 2004 or 32 weeks from the date of entrustment		FD	Website information
6	Include comparative information for preceding year in all annual financial year statements		Computerisation of treasuries and Finance Department for availability of	November 2004 or 32 weeks from the date of entrustment	Funds are to be provided and entrustment order is issued to the Service	FD	Budget at a Glance

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
			information within specified time limit Availability of detail accounts on the web		Provider by 31st December 2003		
Rural Local Bodies (PRIs)							
1	Expedite audits, start clearing arrears and take follow up actions	Decision taken to clear up audit in GP by engaging auditors on contract basis	i) Finalisation of empanelment of retired auditors for clearing the backlog	i) 31-5-2004		i) FD	i) Empanelled list is available in FD
			ii) clearing of backlog of auditing PRIs and ULBs	ii) March 2005		ii) FD	ii) Zero arrear for audit of accounts of GP by the month of March 2005
Urban Local Bodies							
1	Implement the format recommended by CAG. Improve completeness and timeliness of Cash Accounts for assets of these bodies	i) Format for maintaining ULBs account has been improved as instructed by the CAG ii) Government have agreed to maintain accounts and audit them as per the technical guidance and supervision of the CAG	DONE	DONE	DONE	DONE	DONE
2	Place the audit reports before the Council on a timely basis		H&UD department to be requested to ensure placing of audit reports before the Council. *	30-4-2004		FD	
3	H&UD Department should present a		H&UD department to be requested to	30-4-2004		FD	

* Key Actions to be taken

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	consolidated picture of the financial and physical performance of the ULBs, which would be tabled in the Legislature on annual basis		present the consolidated report on financial and physical performance of the ULBs.. *				
State Owned Enterprises							
1	Define clearly the specific objectives of the companies and corporations. When these include the achievement of certain social goals, there should be a clear recognition and statement of the related costs for the proper appreciation of the financial and operating performance of the enterprises		The Public Enterprises Department will be requested to ensure publication of annual report by the public enterprises with a chapter indicating the specific objectives of the Corporation and its achievements. *	30/4/2004		FD	
2	Make business plans visible and available on a timely basis for state government review		P.E. Department will be advised to ensure this. *	30/4/2004		FD	
3	Monitor the SOEs more effectively. Key performance indicators should be identified and periodical reports obtained and reviewed. The number of such performance indicators should be kept small. Review meetings should		The P.E. and administrative Department will be advised accordingly. *	30/4/2004		FD	

* Key Actions to be taken

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	be chaired by the Secretary of the line department, at which the representative of the Department of Public Enterprises should be a regular invitee						
4	Launch a crash programme to bring the accounts of the entities up to date. The accounts that are produced and presented should be transparent, any tendency towards proliferation of notes should be discouraged. The notes should generally state the accounting policies adopted, deviation there from and such other matters as need explaining		The F.D. and Public Undertaking Committee share the same concern. The P.E. Department will be advised to draw up a time bound programme for finalization of accounts and presentation of the same before the Legislature by each public enterprises. *	30/4/2004		FD	
5	Insist that the effect of any qualifications, observations and comments of external auditors on the working results and financial position should be clearly stated. When such qualifications, observations and notes render the external		The Public Enterprises will be advised through P.E. Department. *	30/4/2004		FD	

* Key Actions to be taken

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
	auditors opinion ineffective, there should be no hesitation in denying an opinion on the accounts						
6	Establish effective audit committees as mandated by the recently proposed amendment to the Companies Act		The Public Enterprises will be advised through P.E. Deptt *	30/4/2004		FD	
7	Respond better to external audit as well as the recommendations of the legislative committee. Individuals should be held accountable for their action. Senior Government functionaries should be held accountable for failure to enforce accountability		P.E. Department will be advised on this. *	30/4/2004		FD	
8	Cause managements to introduce greater transparency in the Annual Reports to the shareholders which should be a candid assessment of the achievements and failures, strength and weaknesses of the enterprise, and its systems along with measures that are being		The public enterprises will be advised through P.E. Department. *	30/4/2004		FD	

* Key Actions to be taken

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	taken to improve the organization's financial and operating performance						
9	Publish an annual public enterprise survey. This should inter alia give the extent of Government financial involvement in the Government companies and corporations, their state of accounts and working results, achievement of objectives, results of external audit, recommendations of the legislative committee and following up action taken. The survey should be a public document freely available and also put on the state Government website.		The public enterprises will be advised through P.E. Department. *	30/4/2004		FD	
10	Appoint Chief Executive and directors through transparent selection process with a 3-5 years tenure in order to induct professionals with proven track record.	A Committee constituted by the P.E. Deptt is doing the appointment of Chilef Executive and Directors to the Public Enterprises under the Chairmanship of the Minister, P.E. Department.					

* Key Actions to be taken

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(1)	(2)	(3)	(4)	(5)	(6)	(7)	(9)
External Audit							
1	Empower FAs to comment on responsiveness of departmental officers to audit the Annual Confidential Reports of the latter	FAs are made responsible for audit compliance vide Chief Secretary's letter No. 2099 dated 13/1/2003	A letter to be issued to all departments defining the role of FA and his authority in monitoring audit compliance.	30/4/2004		FD / GA	
2	Officers of CAG (Audit) and Government departments should jointly examine the need of pre-2000 reports		PAC to be requested to allow the officers of AG and Government of Orissa to examine the need of pursuing the pre-200 inspection reports. *	30/4/2004		FD	
3	The AG should write management letters to Secretaries of Government every quarter pointing out serious financial irregularities and system failures.		AG to be requested to write management letters to all Secretaries. *	30/4/2004		FD	
Legislative Scrutiny							
1	Suggest to the Speaker that Committees may consider adoption of a similar procedure of examination of selected paragraphs		Hon'ble Speaker to be requested. *	30/4/2004		FD	
2	i) Civil Society should be sensitized and involved in the accountability process		i) Citizen's access to information through websites	November 2004 or 32 weeks from the date of entrustment	Netwoking of the entire accounting system	FD / IT Department	Website information

* Key Actions to be taken

Sl.	Recommendation of SFAA	Actions Taken	Action to be taken	Date [1]	Pre-requisites / Assumptions	Authority Responsible	Output Indicators
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	ii) An annual report of the work done by the Committees could be presented to the House listing the accomplishments of Committee Members and any constraints faced by them.		ii) Hon'ble Speaker to be requested.*	30-4-2004		FD	

1 The date (Column 5) assumed in some of the key actions are subject to fulfillment of the pre-requisites listed against each of those key indicators in Column No. 6.

* Key Actions to be taken