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The Institute of Public Auditors of India (IPAI)

The Institute of Public Auditors of India (IPAI) was established in 1996 with the main objective of assisting the authorities in establishing sound accounting, auditing and financial management practices. The Institute has established itself as a leading Institute in the country in the areas of management consultancy, audit and investigative examination, evaluation of programmes, system appraisals and setting up systems for efficient functioning of the organisations/ departments of the central and state governments and local bodies. IPAI has a presence across the country through its eighteen Regional Chapters located at Ahmedabad, Allahabad, Bangluru, Bhopal, Bhubaneswar, Chandigarh, Chennai, Guwahati, Hyderabad, Jaipur, Kolkata, Lucknow, Mumbai, Patna, Ranchi, Shimla, Srinagar and Thiruvanthapuram. Each Chapter is equipped to undertake consultancy assignments and organize training programmes.

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From the Presidents' Desk

This is the 26th issue in the chain of publications of the Journal of Public Audit and Accountability since its inception in 2005. We have been covering in the Journal wide range of issues relating to Audit, Accounts, Accountability, Governance, Management etc. IPAI has already brought out theme based issues on Goods and Service Tax in March 2018 and Panchyati Raj Institutions in August 2016. We approached officers in service in audit and executive, retired officers of Audit and from academics so that we get different perceptions on the issues of audit, finance and accountability.

The present issue has well researched articles on issues of current relevance. We have articles in this issue on the need for a new Audit Act, on fraud oversight by Audit, the deficiencies of public account, public financial management through PEFA, need for engagement with stakeholders, high infant mortality rate, and audit as a catalyst of governance.

We have introduced a new feature of articles on latest Audit reports and we propose to have it in all future issues of the Journal.

Two reviews of the book viz. "Government Audit and Governance" which was published by the Institute of Public Auditors of India in November 2020 have been included.

I hope the articles will elicit readers' interest for further studies on the issues and also induce the creative urge to contribute to the Journal by way of articles. We will be happy to have the valuable reactions of the readers so that we continue our efforts to make the Journal better each time

AJIT PATNAIK

EDITORIAL

Government Audit has been given the pride of place for enforcing rectitude and probity in the functioning of the government and allied agencies in public sector. The expectations by the stake holders have been immense and Audit carries a huge burden to discharge its duties as assigned by the Constitution and DPC Act 1971 to meet the expectations and challenges.

Over the years Audit has evolved acquiring new dimensions of Revenue Audit, audit of Public Sector Undertakings and developing new approach of holistic review on the traditional approach of rule enforcement audit. It has chosen to work behind the veil of anonymity doing the assigned job of reporting to Parliament on the development schemes implementation and on transgressions of limits set by legislature and government. It has produced voluminous reports over the years .While it has silently achieved its objective of ensuring executive works in the assigned sphere, some of the reports have shaken the sense of rectitude of the nation and some have triggered further investigation by Judiciary, Parliament, media and public.

The question to be asked on review of working of Audit - is the Audit discharging its constitutional function as a potent force of enforcement of probity and a vehicle for improvement of governance as the constitution makers wanted it to be? What are the hindrances which have stood in its way to be the agency which will pass the litmus test of expectations of stakeholders removal of which can lead to an efflorescence of Audit?

Reporting is the essence of all audit activity. Reporting to be recognized has to be inherently of high technical perfection which must be prepared in a time frame and it must be presented to the Parliament by the executive without delay after receipt of the same from Audit. Some studies by academicians have pointed out reduction in number of reports

prepared annually and also instances of delayed presentation of reports by the executive. The most important problem with the Audit is delayed presentation of its reports by the executive. It is not enough that audit prepares the reports; what is required is its timely preparation and timely presentation.

Another issue which needs attention - is it the correct approach to deprecate the compliance audit for so called higher value for money audit. TA bill objections to exemplify have been ridiculed by outsiders and even by responsible insiders in public discussions. While it is nobody's case that all our resources and focus should be on compliance audit, it is not irrelevant to say that audit by the basic definition includes compliance audit which is the foundation of audit on which rest of the audit superstructure is built and public disowning and ridicule does not help the cause of audit by lowering the morale of the ground staff.

The idea that it should act as an aid to management to be relevant has not helped the cause of audit. As the Bhagavad Gita says...

Sreyan svadharmo vigunah paradharmat svanusthitat svadharme nidhanam sreyah paradharmo bhayavahah.
Better is one's own law though imperfectly carried out than the law of another carried out perfectly? Better is death in one's own law for to follow another's law is perilous (Radhakrishnan).

The introduction of three phase audit in commercial audit is an instance of this 'paradharmo' approach, which has resulted in audit objections getting dropped even before they reach the stakeholders, leaving the plate of audit being emptied even of important objections on the way to the table of Parliament It is like scoring own goals in soccer.

The reorganization of the department on regional lines for improving efficiency needs a relook. Regionalisation has resulted in multi- audit units instead of having the units on the principle of functional specialisation. Audit lives and dies by functional specialisation and making generalists of auditors is like axing the feet of audit. Reorganisation plans for the sake of it or importing from other organisations have never brought any good to any organisation and unsettles the established systems. This may require full scale review by all concerned after further study.

Audit to be a vehicle of enforcement of rectitude and probity needs underpinning of an appropriate National Audit Act for getting records in time, for presentation of its reports timely to Legislature and appropriate time-bound action by the executive on the audit reports on which CAG DPC Act of 1971 has been found silent. It is another instance of the gap between constitutional expectations and constitutional reality engendered by absence of adequate legal support. It is high time it gets the attention of all concerned by enactment of a new Audit Act.

While a new Audit Act requires action by Parliament and executive, perhaps Audit has to look within and plug loopholes in its inner working *e.g.* improving timeliness, number and quality of reports, reaching stakeholders through publications (in which IPAI can play a role), research activity and innovative auditing like fraud angle etc. It may not be exaggeration to say research activity is not of high value and volume in Audit as not many publications come out in regular intervals and it is time retired officers with scholarly abilities are put in charge as they have to think originally as distinct from the routine approach. While the new Audit Act seems a distant view, perhaps inner working can be revamped to make it a highly technically skilled organization as is expected of it. An organization's public value is directly proportional to its technical and professional strength.

Suggestions for making Audit an efficient vehicle of accountability and promoting good governance have been

discussed ad nauseum by all concerned; but a few have been mentioned above to trigger discussion in all related circles. An organisation howsoever endowed with laudable history and achievements has to have a mechanism of self review to rise to higher heights or the alternative is intellectual stagnation. An organisation whose essence is rational and intellectual activity, must rediscover itself reigniting its rich intellectual tradition. As Will Durant writes-'A bit of wisdom is a joy for ever."

Ajit Patnaik,
Editor in Chief

TIME FOR A NEW NATIONAL AUDIT ACT

THAYYIL SETHUMADHAVAN*

On the last day of the monsoon session of 2020, some 22 audit reports of the Comptroller & Auditor General of India (CAG), 16 of them on Union Government and 6 on Jammu & Kashmir, were tabled in the Parliament more like a ritual to comply with a constitutional requirement. At least two of the Central reports contained findings which were of considerable interest to legislators and the public: one that looked like a routine comment on the accounts of the Union Government for 2018-19 and the other on the abysmal performance of Defence offsets. In the former report, CAG pointed out that there was "short crediting" of GST compensation cess of Rs. 47,272 crore to the GST Compensation Fund during financial years 2017-18 and 2018-19. The irregular retention of the amount in the Consolidated Fund of India (CFI) led to inflated revenue receipts and under-statement of fiscal deficits. But the technically couched audit comment also implied that the States and the Union Territories were deprived of their due share of the GST compensation during that period.

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Offset Contracts

In the case of offset contracts, CAG reported that out of offset claims worth Rs.66,427 crore due in respect of 46 foreign contracts signed during the period 2005 to March, 2018, only Rs.11,396 crore (17 percent) had been claimed; and only 48 percent of it worth Rs.5457 crore was actually accepted. These included the contract for 36 Multirole Combat Aircrafts (Rafale Aircrafts). The supplier, Dassault Aviation, had initially proposed in September, 2015 to discharge 30 percent of its obligation by offering high technology to DRDO which, in turn, wanted to procure transfer of technology for indigenous development of engines (Kaveri) for its Light Combat Aircraft. However, the vendor had not confirmed its willingness to transfer the technology till CAG completed the audit. Significantly, the Defence Ministry, after the CAG report, decided to virtually do away with offset clauses for bilateral contracts and single source suppliers.

As per the Constitution, CAG is to submit audit reports to the President for submission to both houses of the Parliament; but it does not specify a time limit for such a presentation. Nor does it specify the date by which CAG should submit audit reports on accounts of the Union, State Governments and Union Territories for tabling them in the Parliament and the respective legislatures. In the absence of any specified dates for tabling audit reports, it is left for the whim of the executive to decide the timing of tabling of the CAG reports. In the case of the reports mentioned above, CAG submitted the reports to the Finance Ministry on 4th August 20 and the reports were tabled in the House on 23rd September 20 the last day of the session. Audit reports on finance and appropriation accounts of the previous financial year should rightly be available to the law makers before or at least during the budget session to enable them to review and analyze the past year's outcome and participate in the budget discussion more effectively. And it is only logical

that the concerned law and regulations should provide for it clearly.

CAG's DPC Act, 1971

Article 149 of the Constitution provided that till provisions were made under a specific law for that purpose by the Parliament, CAG shall perform such duties and exercise such powers in relation to the accounts of the Union, States and other authorities or bodies concerned as were 'conferred on or exercisable by the Auditor General of India immediately before the commencement of the Constitution'. It took more than two decades for the Parliament to enact the envisaged legislation defining the duties, powers and responsibilities of CAG under the "The Comptroller & Auditor General's (Duties, Powers and Conditions of Service) Act, 1971" (DPC ACT).

The DPC Act was formulated at a time when public audit was in an evolving stage. The thrust of public audit was, at that time, financial and compliance audit to verify the accuracy and correctness of accounting under the umbrella of Financial Audit, with limited checks on the propriety of transactions. Over time, significant innovations in public audit have come to the fore, with performance audits of government schemes, programmes and projects with focus on economy, efficiency and effectiveness occupying the prime place. The DPC Act, however, does not refer to such advanced techniques of audit nor does it define in clear terms the scope and coverage of audit and accountability. Not surprisingly, there were occasions when departments and public bodies questioned the authority of the CAG to carry out performance audits of their activities under the DPC Act, and it took a clarification by the Ministry of Finance in 2006[1] to clarify that performance audit is indeed *deemed to be* within the scope of audit by the CAG. Later, the Supreme Court

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[1] Ministry of Finance / Department of Economic Affairs / Budget Division OM No.F.No.6(5)-B(R)/ 99 dated 13th June ,2006

also, fortuitously, in 2013, confirmed in Arvind Gupta's[2] case that the CAG's right to undertake performance audit is inbuilt in the DPC Act. The DPC Act defines "accounts", but does not define 'audit' which is the thrust of the Act.

It is anomalous that the Supreme Audit Institution (SAI), as CAG is known in the international realm of public auditing, has to depend on the Finance Ministry to clarify the scope of audit and to arm itself with audit authority to exercise its legitimate task. As mentioned by Vinod Rai, former CAG, in his book, "Not just an Accountant"[3], DPC Act provides for the audit coverage of only conventional government departments and public enterprises, but not delivery models such as public-private partnerships, non-governmental organizations etc. which are important, but comparatively recent, instruments of public policy.

Audit of PMCARES Fund

The limitations of the DPC Act were in public domain recently when demands were made by civil society activists and a section of the media that CAG should audit the PM CARES Fund to ensure its transparency and accountability. The aforesaid Fund was created and is managed by the Central Government, but was established as a Trust, with audit of its accounts entrusted to private auditors. But the fact remains that the Fund is in every respect a public fund which entails transparency and accountability as for all other public welfare funds. But by clothing it as a Trust Fund, authorities have managed to keep it outside the scope of public audit thanks to the limited scope of the DPC Act.

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[2] Arvind Gupta V. Union of India and Others/ Supreme Court of India, Oct1,2012

[3] Page 54: Not Just An Accountant: Vinod Rai

CAG's Audit of Kerala Infrastructure Investment Fund Board (KIIFB)

As widely reported in the local media, there was yet another unfortunate episode relating to the DPC Act when the Government of Kerala declined a proposal of the CAG during last year to undertake the audit of a State Government Undertaking called Kerala Infrastructure Investment Fund Board (KIIFB) under section 20 (2) of the DPC Act, 1971. This section provides for CAG's audit of bodies and authorities not entrusted to him by law if he is of the opinion that such audit is necessary in public interest. The denial of the State Government reflected how outmoded the Act has become. KIIFB was established to raise funds for the infrastructure projects of Kerala Government mainly from Non-resident Kerala investors in the gulf- region. The Fund Board also received initial grants from the government for its preliminary expenses. Under Section 14 of the DPC Act, 1971, CAG was entitled to audit KIIFB as a grant-in aid body; but this would be a limited audit targeted primarily at the utilization of the grant. But, having regard to the risk potential arising from the fact that the Government was to be the guarantor for the funds raised from private investors by KIIFB, CAG considered that the scope of its audit should be enlarged to provide for a more comprehensive audit under Sn. 20 (2) of the DPC Act which envisaged the prior approval of the Government. However, Kerala Government reportedly obfuscated the request on the tenuous ground that since the Board was already subject to audit by commercial auditors, a parallel scheme of auditing by CAG might send conflicting signals to the prospective investors and might invite the risk of jeopardizing the purpose for which KIIFB was formed.

It may be recalled that questions were also raised about the right of audit of the CAG under the Act when it initiated the audit of telephone revenues shareable by private operators with the Union Government. The matter went to the Supreme Court

which made it clear that the CAG's rights in this regard were unquestionable. The Court declared that CAG is a constitutional authority entitled to review and conduct performance audit on revenue allocations relating to the Centre, the States and the Union Territories and to examine matters relating to the economy and how the government uses its resources.

Proposal for Amendments of the DPC Act, 1971

Public audit by the CAG provides not only a true and fair view of the management of public funds to the legislators and to the public, but also ensures transparency and trust in the governance process. Audit reports are discussed by parliamentary committees who take evidence from responsible officials before making recommendations based on audit findings. In view of the limitations of the DPC Act,1971, a fairly comprehensive proposal for amendments of the Act was made in October,2010 by the former CAG, Vinod Rai to the then Finance Minister, the late Pranab Mukherjee. The thrust of the proposed amendments was that all plan expenditures should be brought within the CAG's audit, a time limit be fixed to provide information sought in audit, and all government schemes including public-private partnerships and public expenditures routed through specified agencies, presently outside the CAG's audit, should be brought within the scope of CAG's audit. It also sought to prescribe a time limit for tabling audit reports in the legislatures after they were submitted by the CAG to the governments concerned. However, soon after submission of the proposal for amendments to the Act, and in the wake of the media attention to the celebrated audit reports on Commonwealth Games - 2010, 2G Spectrum and Coal Mining Blocks Allocation, neither the Finance Minister, nor the subsequent CAGs had the time or opportunity to pursue the matter. The well- merited proposal for amendment to the DPC Act, 1971 continues to gather dust on the shelves of the Finance Ministry.

International Experience

It is relevant to mention that, faced with more or less similar constraints, several countries have had their audit legislations amended to render them more effective and comprehensive, as should be. In the United Kingdom, as mentioned ante, the Chancellor of Exchequer appointed a Commission under Lord Sharman of Redlynch in 2001[4] and based on his recommendations, amended the National Audit Act, UK substantially to improve the scope and coverage of public audit. The report of the Commission identified what they called 'Non-Departmental Public Bodies', namely, bodies which have a role in the process of national government, but which are not Government Departments or part of one, and which, accordingly 'operate to a greater extent at arm's length from Ministers'. The Commission recommended their inclusion within the audit coverage of the national auditor. (PM CARES Fund, one would presume, will qualify eminently for categorization under this definition). Interestingly, Lord Sharman defined public money, for accountability purposes, as 'all money that comes into the possession of, or is distributed by, a public body, and money raised by a private body where it is doing so under statutory authority', in order to enhance the transparency of governance. New Zealand is another SAI which benefited from a similar exercise.

Need for a new National Audit Act

It will be clear from the discussion above that the current DPC Act, 1971 is outmoded and is constricted in terms of its scope and coverage of public audit. Fortunately, the Regulations of Audit and Accounts issued by the CAG, 2007 (As amended in 2020) clarifies some of the issues and act as a supplement to the Act. However, the need for a comprehensive new National

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[4] Report of Lord Sharman of Redlynch: Holding to Account (February, 2001)

Audit Act cannot be gainsaid. As pointed out by the Constitution Review Committee (CRC), public audit is a powerful instrument of good governance and renders public authorities accountable. The CRC felt that public accountability and transparency in administration depended to a large extent on how well public audit is carried out. In order to strengthen the hands of the CAG and to bring the role and responsibilities of the CAG in clear terms within the ambit of law, it is essential that the DPC Act, 1971 should be replaced by a comprehensive and well enunciated new enactment. The new Act should establish the role, responsibilities and the mandate of the CAG as also the role of the government authorities in clear terms to facilitate public audit, in unambiguous terms.

The CAG of India has been recognized internationally for its professional competence as reflected in its elections, many times, as the auditor of the United Nations and several of its Funds and Programmes. It should not be that such an SAI does not even have a proper base, in the form of a legally and functionally competent enactment, to stand on. There is no doubt that a new and comprehensive national audit act would go further to strengthen the domain of public auditing in India and will lend more transparency in public governance. This can however be best achieved if the new National Audit Act is devised after wide consultations, rather than by incorporating marginal amendments to the existing legislation. There are several basic issues to be addressed in the process: Should Compliance audit give space to performance audit? Should CAG be part of the Parliament? What should be the scope of public audit? Can Audit question policy, etc.[5]

The time is perhaps propitious for the CAG and the Government of India to accomplish the task initiated more than ten years ago.

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[5] Audit-A Catalyst of Governance: Ajit Patnaik, Government Audit and Governance; IPAI (2020)

RISING STAKEHOLDER EXPECTATIONS ON FRAUD OVERSIGHT

Dr. SUBHASH CHANDRA PANDEY*

Chairman, National Financial Reporting Authority (NFRA) recently raised heckles in auditors' community when he advocated shedding of the old belief of auditor "being only a watchdog and not a bloodhound[1]" needs to be "exorcised from our minds". He was articulating growing stakeholder concern on mis-governance. Every time an economic entity fails to meet its obligations, questions are raised whether concerned regulators and auditors were sleeping.

Corporate frauds in World Com, Enron, Volkswagen, Olympus, Hydro One, Satyam etc. are now case studies in corporate governance. ILFS, PMC Bank and failed corporates in real estate and telecom would become case studies once full facts come in public domain. Revamped company law looks up to the auditors and independent directors as the antidote to corporate mis-governance with increased disclosure requirements on listed companies. Most of the corporate failures had exposed direct involvement of top executives. Typically, the frauds involved overstatement of profitability by wrongful capitalisation of expenses, hiding losses in the chain of

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[1] Justice Lopes had observed (Kingston Cotton Mill Co case 1896): "An auditor is not bound to be a detective, or, as was said, to approach his work with suspicion or with a foregone conclusion that there is something wrong. He is a watchdog, but not a bloodhound. He is justified in believing tried servants of the company in whom confidence is placed by the company".

subsidiaries and associates. All large organizations also face significant risks of employee frauds, fake payments against fake/inflated supplies/construction or to fake beneficiaries.

Increasing oversight against fake transactions and assets, both physical and financial, is increasingly being asked for from auditors by concerned stakeholders. The owners and other stakeholders (regulators/bankers/taxmen/consumers) expect auditors to assure them about the existence, proper care, accounting and valuation of assets. They want auditors to vouch for the stuff constructed on ground or claimed to have been bought does not exist merely on paper. Likewise, expectation for vouching for the accounts showing a ‘true and fair view’ of how the entity is being managed include expectation to assure that the accounts are free from material errors and frauds.

An auditor cannot fill the lack of integrity among employees and executives in the audited entity. Auditors visit for a limited time and carry out their examination based on records and information provided to them. However, such defence has not cut much ice with stakeholders. The auditors are trained that detection of fraud is merely in incident not the object of auditing exercise. While conducting an audit may be a way of preventing fraud and error, the auditor is not and cannot be held responsible for their prevention. An auditor cannot obtain absolute certification that significant misstatements in the financial statements will be detected but is only able to obtain reasonable assurance about that fact. The risk of not detecting significant misstatement due to fraud is greater than the risk of not detecting significant misstatement due to errors, as fraud involves active concealment. The auditor's risk of not detecting significant misstatement in managerial fraud is greater than that of employee fraud. The auditor's opinion is based on reasonable assurance and therefore does not guarantee that all misstatements of fraud or error have been detected.

Auditor gives his opinion on the accounts ‘based on

information, replies, clarifications and documents provided to them and it would be impossible for auditors to look at everything presented to them with suspicion. The quality of an audit inevitably reflects the quality of the data supplied by a client. Even the most scrupulous audit is no guarantee that all is well in a business.

The CAG is an examining agency and not an investigating one. We don't have the sweeping powers like some other functional democracies. It does not have coercive powers to demand production of information/records or to summon witnesses and to examine them on oath. There are no codified penalties for non-cooperation with audit unless we go for prosecution under Indian Penal Code criminalizing obstructing a public servant in carrying out his statutory duty. There has been no occasion to invoke these penal provisions.

Since we are not an investigative agency and our scrutiny is largely confined to records of audited entities, the scope of investigation is necessarily limited and often can only points to strong possibility of fraud or corruption. We don't go around looking for ghosts. We visit our audited entities as per a schedule of periodicity to carry out systematic test-checks, which may or may not throw up issues of fraud and corruption. It is this credo that guides the routine work of an auditor where he goes about test-checking selected transactions and selected controls from the viewpoint of their authority, regularity, and appropriateness.

The responsibility for the prevention and detection of fraud and error rests primarily with the management of the audited entity through the implementation and continued operation of accounting and control systems designed to check fraud. Auditors are required, however, to evaluate and report on the adequacy of the systems in place and competence with which the management has discharged its responsibility in relation to prevention, detection, response and follow-up/ remedial measures in relation to fraud and corruption.

Fraud examination calls for auditors being alert for situations, control weaknesses, inadequacies in record keeping, errors and unusual transactions or results, which could be indicative of fraud, corruption, improper expenditure or lack of probity.

Typical frauds involve manipulation, falsification or alteration of records or documents; misappropriation / misapplication of assets, suppression or omission of the effects of transactions from records; recording of transaction without substances; and misapplication of accounting policies.

There are several typical indicators of possible fraud. (i) When there is no segregation of duties, checks and balances are diluted and fraud risk increases. (ii) When there is a sole source or unusual terms in contracts, bid is always given to the last bid received, same vendor wins by a small margin, or when the purchase price is abnormally higher than ascertainable fair market value, which is not always possible to ascertain, there is a prima facie suspicion of fraud. (iii) When purchases and other financial transactions are split merely to avoid approaching higher authorities or when there are unnecessary purchases, idle inventory, little feedback from user/beneficiary, a prima facie case to look for possibility of fraud can be made out.

Frauds are often detected as a result of routine reconciliation and comparison of information from different sources. For example, if one unit claims to have despatched certain goods to another unit and the despatch invoice is compared, as part of test check, with details of goods received by the other unit, a fake despatch may be detected. There may be some delays and mistakes in recording of transactions at both end and so we proceed with caution instead of declaring each and every discrepancy, non-reconciled transaction, a case of fraud, misappropriation, embezzlement.

A typical fraud occurs when payments are made against

non-existent supplies. The documents may be faked to show that such and such goods have been received without actually receiving it. On government audit side, we have seen the most well-known case of 'fodder scam' in Bihar where fictitious purchase of fodder was unearthed.

Auditors normally rely on certificates given by responsible personnel of the auditee organisation. In case of fodder scam, the 'vouchers' in support of purchase of fodder would have carried usual stamp of the 'stock receipt', i.e., someone certifying with a signature and stamp that fodder supplies having been 'received' and 'taken on charge' or entered in stock register on such and such date.

Stakeholders (regulators/bankers/taxmen/consumers) expect auditors to assure them about the existence, proper care, accounting and valuation of assets; to vouch for the stuff constructed on ground or claimed to have been bought does not exist merely on paper. There may be cases of fake works, fake roads, fake wells/ponds all constructed/dug on paper. Physical inspection is not part of usual audit drill. In any case, without authentic documentation, auditor can never be sure whether the stock or physical asset shown to him is indeed linked to the financial transaction being verified; that it did not pre-exist the transaction or that it has not been temporarily brought to site just before inspection. Random snapshots can be deceptive proof like dummy teachers/students arranged before inspection or dummy stocks placed there to make up for shortfall.

Auditors do not normally go for physical verification of stocks and fixed assets but the conspirators may leave some discrepancies in the documents that can expose the fraud. For example, certain registration numbers of vehicles purportedly used for transport of large consignments of fodder turned out to be of two wheelers rather than of trucks. Little more attention to the discrepancy could have blocked fraud detection. A prima facie case of fraud is established which may be defended as mere

clerical mistake in recording correct particulars. Of course, there are smarter fraudsters.

Traditional view of fraud detection being merely an incidence of auditing activity is now giving way to more structured and focused approaches to detection of systemic symptoms of possible frauds by analyzing trends and profile of transactional data.

One of the main issues of detecting fraud the sheer volume of transactions that take place and it is simply not practical to review every single one manually for suspicious activity. Forensic data analysis can help us analyse vast volume of data to identify underlying trends relating to transactions that have taken place. With Big Data Analytics tools, it is now increasingly possible to move away from mere sample-base scrutiny for arriving at audit assurance to examine the whole range of data and look for questionable trends and profile indicating possibility of fraud or sub-optimal management decisions.

In one instance, the comprehensive data on voucher level computerization system was scanned for the temporal and district wise trend and profile of certain specific types of payments to establish whether any unusual pattern emerged indicating the possibility of suspected fraud.

Some areas of fraud are discussed below.

Frauds in storage and transportation of goods

When stores move by rail or road, there is inevitable ‘transit loss’ through theft/pilferage. The quantity despatched does not match with quantity received and the receiving storekeeper records ‘deficient receipt’. Nothing prevents from showing exaggerated or fictitious ‘short receipt’! If the higher up prescribe a norm on short receipt, say at most 2% as acceptable transit loss, one can be sure that 2% of stores

expected to be received will not be shown as 'received' even if short receipt is less than 2%!

In a 2014 performance audit of weighbridges in Indian Railways, Audit noticed that Railway Board failed to ensure weighment of all freight traffic. Out of 1176 loading points, 759 did not have their own weighbridges. The performance of weighbridges was not being checked regularly and nor being maintained properly. CBI and Railway Vigilance conducted country-wide surprise raids on weighbridges and found tampering with them to facilitate over-loading of railway wagons going undetected, causing revenue loss to railways and also leading to faster wear and tear of the tracks and rolling stocks.

Export bound containerised cargo and even trucks carrying PDS foodgrain now use GPS enabled tracking with or without tamperproof locks, RFID tags. Petroleum and Explosives Safety Organisation is using a barcoded system of tracking explosive consignments. Plan is to go upto tracking of each individual cartridge, not just the carton. These new technologies have reduced transit losses to a great extent.

Storage and transportation losses of foodgrain are well known. In 1997, Government had requested the CAG to carry out special audit of inventories of foodgrain held by the Food Corporation of India (FCI) after auditors refused to vouch for the authenticity of figures of stocks and shortages shown in the annual accounts. The CAG entrusted the task of "complete physical verification of ground balances of wheat, rice and paddy held by FCI as well as by the State Agencies for the Central Pool" to M/s SGS India Ltd., a reputed firm of certified surveyors/valuers, and 4 firms of Chartered Accountants. The contract required 100% counting of bags and physically weighing of these bags. Later, 100% counting of bags with proper weighing was substituted by bulk density method (weight-volume ratio method). This involves drawing out

sample bags from stacks on random basis, measuring its volume in a separate sample stack and weighment. The sample's weight volume ratio would then be extrapolated to the bigger stack. Finally, the exercise was abandoned after some limited test check as the firm found it too daunting a task.

The common perception of audits – tedious, time-consuming, expensive, unproductive, necessary evil – applies to warehouse inventory too and internal audits continue to be used to help track inventory accuracy, minimize stockouts, avoid spoilage, improve utilization, prevent fraud, stop pilferage, etc.

Inventory auditors must confirm not only the existence of goods but also the rights to ownership – and the value – of such inventory. Audits can be in the form of daily cycle counts of specified locations to quarterly, wall-to-wall counts done by large (often external) teams that verify and record every single item in the warehouse. Various analytical procedures have been developed by auditors to randomly/statistically sample inventory data – instead of counting each item – and yet gain a reasonably accurate view of the entire warehouse inventory.

Recent report of the Commission on Agricultural Costs and Prices for Rabi 20-21 noted that wheat stocks in Central Pool reached a new record level of 55.8 million tonnes on May 31, 2020. The FCI reports that at end of May 2020, it held 28.5 MMT rice and 35.8 MMT wheat (total 64.3 MMT). Discrepant as these figures are, can the management and auditors vouch for existence of this stockpile? On what basis? Foodgrain are bulk commodities with more weight than intrinsic economic value. Hence, every movement even for stock verification purposes costs money and the cost of actual stock verification may far exceed the cost of shortages detected!! For valuable inventories, inventory auditors are using advanced technologies including RFID tags and drones. Whether it is feasible and cost effective for foodgrain inventory remains an unexplored question. The CAG being the sole auditor of the FCI may consider reviving this aborted project.

Frauds involving fake/ineligible beneficiaries

Technology is necessary to provide public services to large populations in an efficient manner. Technology has its own risks and rewards.

White collar crime and financial frauds are the fastest growing menace, which have serious consequences and implications for reputation and profitability. The best and only way to combat frauds is through proactive and preventive strategy, through strengthened internal audit.

Data theft detection and prevention is particularly important issue. With near universal AADHAR enrolment, opening of PMJDY accounts and their AADHAR seeding and growing spread of Direct Benefit Transfer to cover most subsidies through banking channel, there is a discernible risk of fraud on public finances handled through this system. We would like to have the IT systems have strong audit checks and trails built into the system.

Many government schemes suffer from the problem of fake/ineligible beneficiaries. Many government schemes collect Aadhaar number and mobile number of beneficiaries without biometric authentication hence beneficiary databases would contain undetected duplicate Aadhaar / mobile numbers.

AADHAAR linking of ration cards had helped in weeding out 2.95 crore ration cards resulting in a saving of Rs.17,000 crore annually (Ministerial statement on Feb 26, 2018). These invalid cards were susceptible to misuse by ration card dealers to show fake sales and then sell the stocks in open market. Out of 21 crore ration cards, about 90 per cent have been linked with Aadhaar of at least one of the family member listed on the card. Once every adult member's Aadhaar is linked, more ineligible ration card beneficiaries may come to light. Aadhaar linking of every adult member would be necessary to make every individual's ration entitlement portable to any part of the

country He can draw ration from any PDS shop. This will help migrants and also help weed out invalid entries in ration cards. (The ongoing 'One Nation, One Ration Card Scheme' by 17 States. All are expected to be covered by March 2021.)

Recent reports have emerged of payments remitted to accounts of fake beneficiaries under PM-KISAN scheme. Scamsters used Aadhaar numbers available in public domain to create fake Aadhaar cards which were then used to create a bank account matching the name in the Aadhaar card. Over 10 crore beneficiaries are registered with the scheme. Apparently, registration of beneficiaries by local officials does not require biometric authentication and online transfers are made directly to the bank accounts without biometric authentication of beneficiary at each transaction. Tamil Nadu reported Rs.110 crore payments to 5.5 lakh ineligible persons across 13 districts. Similar reports have come from Assam and Himachal Pradesh.

There have been reports that some examinees were arrested for using fake fingerprints to beat biometric authentication. A fingerprint cloning gang was busted in Hyderabad, three arrested, in Nov 2018.

A 'teacher recruitment scam' was recently unearthed in UP when it was found that using the ID and certificates of one hapless Anamika Shukla, many 'fake' Anamika Shuklas were working as teachers in Kasturba Gandhi Ballika Vidyalayas (KGBV). The alleged fraud was unravelled when a digital framework, called Prerna, alerted officials about some teachers with identical documents in March. At least six fake teachers posing as Anamika Shukla had withdrawn salaries worth Rs.12,24,700. So they had also opened bank accounts using bogus KYC documents and apparently without biometric authentication. 3 have been arrested. Real Shukla said she had applied for the government job at KGBVs in four districts but did not attend the counselling process due to personal reasons. Real Anamika Shukla finally got a job. Documents of all school

teachers have been ordered to be checked. UP government has been increasing deploying technology to check employee malfeasance. Biometric attendance and requirement for teachers to upload class pictures have been implemented to check chronic problem of absentee teachers.

Bogus employee problem is not new. In areas of pure manual work, this has been a long outstanding concerns. There are fake muster rolls for workers whose wages would be drawn, who will verify thumb impressions on clumsily organized, sullied scrolls. Then there are cases where somebody is coming to collect wages, but someone else (a family member or accomplice) is working in field, usually with connivance.

Instances of duplicate and outright fake beneficiaries have also been reported. Instances are known where already married girls participating in fresh marriage ceremonies to get government benefits and withdrawal of multiple widow pension or other pensions. Enrollment linked incentives under school mid-day meal scheme and aanganwadi schemes also invite fake enrollment. How far can one go to check if the children actually get the intended education and nutrition?

Film Munna Bhai MBBS highlights the problem of ghost examinees. I once heard account of a scam in a foreign country where people had preserved cut thumbs of dead people to be used for drawing old age pension disbursed by cash vans sent by government. Smart people find ways to evade CCTV coverage. There is no limit to people's ingenuity in cheating.

With salaries, pensions, scholarships and other benefits being directly credited into bank accounts without any biometric authentication of beneficiary, the manual system of 'acquittance roll' has been dispensed with. If there is no proper bank reconciliation between disbursing office and bank or if there is collusion, payments can go into fake accounts (proxy accounts of scamsters). Without proper bank reconciliation, it would not

be known whether the payment supposed to have been made to A, B and C has actually been conveyed to the bank as advice to credit the accounts of A, B and D!! I came across one such case of fraud where a cheque drawing DDO withdrew salaries of even non-existent/transferred out employees and these excess drawls were directed to the bank accounts of corrupt officials complicit in this fraud.

So what next in authentication technology? Iris scan? Facial Recognition software? Implanted chips? Yes, all these technologies are increasingly being used to safeguard against financial frauds. The self-service kiosks of banks having no human attendant around are big users besides access controls in particular rooms in offices and factories. Access controls on entry of only bonafide customers into unmanned smart branches/kiosks after biometrics recognition through fingerprints and Iris scan, behavioral biometrics like the way customers type in the key board, click the mouse, facial expression (smile on the face, blink of eyes), gestures and speech recognition.

Robots interacting with customers using speech recognition and facial expression recognition technology are cost effective solutions to deal with manpower shortage and minimising risks of human failure. The pandemic has seen gradual introduction of robots as frontline warriors. Full-scale robotics and smart interactive devices and interfaces, banking on the drive, bank on your smart watch; all are likely scenarios of future banking with diminishing direct contact with banking staff and representatives. Future of a typical bank is a fintech company.

Authentication technologies are evolving to check online frauds, identity thefts. QR Codes, masked AADHAAR card based e-KYC are increasingly used in mobile banking. The user ID and password for online login has been found insufficient. Online financial transactions now have additional safeguards of

two-factor authentication in place. Mobile OTP and complex Captcha Codes – numeric, alphanumeric, visual, word clues, and even simple arithmetical calculations and click to prove you are not a robot, virtual keyboards, disable copy paste etc. are now in place. Even then scamsters often are able to steal the ID and fool gullible people to part with mobile OTP.

When Aldous Huxley wrote 'Brave New World' in 1932, he visualised a system of mass-scale control of human being by scientific establishment. When he came out with 'Brave New World Revisited' in 1958, he found a world far ahead of his Sci Fi imagination and today it is even more so. The technology of malfeasance and malfeasance control both have evolved. Protest and protest control; disease and disease control; all are going high tech beyond his imagination. As the population has exploded, imperatives of technology enabled governance have also grown, bring in its wake fresh concerns about misuse of technology.

We would like to have all IT systems including AADHAR-based DBT systems to have strong audit checks and trails built into the system.

Fake claims: A major class of frauds and their impact on plans of administrative simplification

False and exaggerated insurance claims is a major problem for the insurance industry worldwide. All segments of insurance - motor vehicle, crops, medicare etc – have reported cases of systemic siphoning off of funds through such claims.

Cases of fake medical reimbursement, travel and LTC claims have occasionally been reported in government departments and public sector undertakings and many are under CBI investigations.

Apart from the loss such fraudulent transactions cause to the paying organization, a bigger damage is done through

harassment caused to sincere claimants because authorities strengthen checks and balances, procedures.

When procedures are tightened, say asking people to provide boarding passes and pictures of places visited as a proof of actual travel of asking for empty vials and pouches of medicines to prove actual consumption, it understandably causes all-round harassment and indignation and even loss to the honest claimants. In one extreme case, an officer was only reimbursed onward journey for LTC because he had lost the ticket for return journey. Also, such additional checks are also not fool proof.

This type of intrusive scrutiny makes citizens crib about increasing bureaucratization of administration and calls for simplification procedures, institution of trust-based procedures. This is a constant dilemma for policy makers and auditors alike.

The best government is that which governs least: Minimum government maximum governance. That is not possible if a large segment of population looks up to government for support and sustenance. Herein lies the dilemma. Urge or necessity to have State intervention comes with the risks and restraints on freedoms and privacy, even dignity!

We don't want auditors, managers and public administrators to be guided by constant suspicion, intrusive scrutiny and invasion of privacy and assault on dignity. It slows down the system. However, there must be exemplary and deterrent action to deal with those who betray the trust in a trust-based simplified administrative system.

PUBLIC ACCOUNT – AN ABIDING DISTORTION IN OUR FINANCIAL SYSTEM

Dr. GOVINDA BHATTACHARJEE*

As a principle, government accounts closely follow the budget which determines the level of government activities during the year in terms of allocation of resources among different sectors and developmental programmes. At the federal level, the Union budget requires parliamentary approval for raising revenues and incurring expenditure, while at the provincial level, the respective provincial Legislatures accord approval to the revenue and expenditure proposals of the provincial governments. However, the budgeting system in India lack transparency due to a typical feature of the government accounting system called the Public Account, which distorts the public financial management system and renders the system of public accountability vulnerable to misuse. Very few countries in the world today has such a system of government accounting.

Structure of Government Accounts

Part XII of Indian Constitution deals with government finance which is organized under three funds. Under article 266 (1), all revenues received by the Government of India or any state, all loans raised by the issue of treasury bills, loans or ways and means advances and all moneys received by the Government in repayment of loans shall form one consolidated fund, to be entitled the Consolidated Fund of India or of the State, as the case may be. Article 266 (2) says that all other

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public moneys received by or on behalf of the Government of India or of a State, shall be credited to the Public Account of India or of the State. Finally, a Contingency Fund will be created under article 267 with a fixed corpus to enable the Government to make unforeseen expenditure without prior legislative approval (e.g. expenditure on relief after a natural calamity), later to be recouped from the Consolidated Fund under the usual legislative approval procedures. Government accounts record all transactions pertaining to the above three funds.

Further, article 266 (3) states that no moneys out of any Consolidated Fund shall be appropriated except in accordance with law - for the purposes and in the manner provided in the Constitution. The manner of such appropriation falls under the respective "Procedure in Financial Matters" under Chapter II for the Parliament (articles 112 to 117) and Chapter III for the State Legislatures (articles 202 to 206) of the Constitution. No such legislative approval, however, has been prescribed for withdrawing any money from the Public Account, which does not involve revenues or debt of the Governments but other public moneys that do not belong to the Government as such. Thus there is no legislative control over the use of funds from the Public Account, and it is this lack of legislative control that makes the article 266(2) somewhat intriguing, and this is what also makes it vulnerable to misuse and subject to many aberrations in our financial system. Only three countries in the Indian subcontinent – India, Pakistan and Bangladesh - that share the common burden of partition, population and poverty and still nurture a dated Government financial system bequeathed by the British two thirds of a century ago, have a public account - no other country in the world has such distortion in their financial system.

It is interesting to trace how this article came to be included in the Constitution. Many articles in our Constitution can be traced to the earlier Government of India acts, but article

266(2) did not have any corresponding presence in those Acts - it came into existence only after independence when the Constitution of the new republic was adopted. Proposing this article on the creation of Public Account, the Constituent Assembly had noted:

"in drawing the definition of the Consolidated Fund we lumped along with it certain other moneys which were received by the state, but which were not the proceeds of taxes or loans, etc., with the result that public money received by the state otherwise than as part of the revenues or loans also became subject to an Appropriation Act. Obviously the withdrawal of money which should strictly not form part of the Consolidated Fund of the State cannot be made subject to any Appropriation Act. They will be left open to be drawn upon in such manner, for such purposes and at such times subject to such conditions as may be laid down by Parliament in that behalf specifically. It is, therefore, to enlarge the definition expressly of the Consolidated Fund and to separate the Consolidated Fund from other funds which go necessarily into the public account that these changes are made. There is no other purpose in these changes."[1]

Thus the Public Account came into existence more as an administrative convenience rather than an economic necessity: *"The Finance Ministry drew attention to the fact that our provision in regard to the Appropriation Act was also made applicable to other moneys which generally went into the public account and that was likely to create trouble. It is in order to remove these difficulties that these provisions are now introduced in the original article.*"[2]

It is to be noted that no procedure as promised in the debate above has since been laid down by the Parliament, in the

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[1] Constituent Assembly Debates, Book No 4, Vol IX, Lok Sabha Secretariat, 2009 Reprint, Pp 1191.
[2] Ibid.

absence of which the Governments have complete liberty to use these funds the way they like - a liberty that overrides all accountability and legislative control. But before proceeding further, let us understand the nature of transactions that go into the Public Account.

Structure of Public Account

There are five major heads of accounts under the Public Account: (i) Small Savings, Provident Fund and Other Accounts; (ii) Reserve Funds; (iii) Deposits and Advances; (iv) Suspense and Miscellaneous; and (v) Remittances. A full length discussion on these is beyond the scope of this paper. Briefly, these accounts comprise funds that do not belong to the Government, but which the government holds in trust and manages on behalf of their owners who can be ordinary people or government contractors or anyone, and sometimes even the Government itself when it holds taxpayers' money outside of Consolidated Fund. Once some money gets parked in the public accounts, the legislative process of voting the appropriations and exercising controls over the use of those appropriations through examination of audit reports by the Public Accounts Committee cease to operate in respect of these funds. Some of these funds are interest bearing on whose balances the Government has to pay interest from the Consolidated Fund using taxpayers' money - others may not carry any interest liability.

The first three of these accounts deal with receipts and payments in respect of which the Government is liable to repay the moneys received or has a claim to recover the amounts paid. In respect of these transactions, the Government acts as a banker, receiving amounts which it later repays and paying out advances which it subsequently recovers. Provident Funds of Government Employees, Deposits of Local Funds, Reserve Funds Deposits made by outside agencies, Departmental Advances, etc. fall under this category. Balances in these accounts constitute a part of the overall financial liabilities of

the Government, a proposition whose logic is not beyond doubt.[3] The other two accounts – Suspense and Remittances - are used only for adjustment purposes; all initial debits or credits to these accounts are made pending final adjustments and cleared eventually by mutual adjustments once their final destinations are traced. Suspense temporarily accommodates all governmental/ inter-governmental/ departmental transactions pending availability of the requisite details in corresponding vouchers/ challans that would identify their final destinations. It also includes temporary investments of cash balances in short term loans or Government securities at nominal rates of interest. Remittances concern intra- and inter-Governmental cash remittances between its various departments / ministries and also between the central bank of the country, the Reserve Bank of India (RBI) and various Governments and Government Departments.

The most important of these accounts is of course the "Small Savings, Provident Funds and Other Accounts" that includes a number of interest bearing obligations in respect of provident fund contributions of all Government and non-Government employees and some other contributions. Small Savings include National Savings Deposit, Post Office Savings and Recurring, Post Office Time Deposits, Post Office Monthly Income Account, Senior Citizen Savings Scheme, Sukanya Samriddhi Account, National Savings Certificates, Defence Savings Certificates, National Development Bonds, Post Office Certificates, etc. All these are put together into the National Small Savings Fund (NSSF) from which investments are made by way of issuing securities to the central and state governments. Provident Funds include the Public Provident Fund (PPF) and State Provident Funds which include GPF, CPF, Defence,

[3] The other financial liabilities of the Government being its public debt liabilities and contingent liabilities on account of outstanding guarantees given to public sector entities and public bodies/ authorities.

Railways and Other Provident Funds. Other Accounts include Special deposits by retirement funds with the Central Government and Insurance and Pension Funds like Family Pension, CGEGIS, State Government Employees' Group Insurance Scheme, Post Office Insurance Funds, etc. Besides, there are securities issued in lieu of subsidies to the Oil Marketing Companies, FCI and fertiliser companies, as well as some other special deposits and accounts.

Government has to pay interest on moneys deposited in these funds at the prescribed rates, and in return can use these funds for investment in specified Government securities; such investments can eventually be channelled for development purposes for which the funds provide a ready source of capital at the disposal of the Government. Because of this reason, the logic of including these balances in the Government's total financial liabilities along with outstanding public debt is perhaps understandable, but the logic behind including the balances of other heads of Public Account in the Government's total liability is often baffling. For example, the Reserve Funds are created by debit to the Consolidated Fund to create reserves which are assets, e.g. for the renewal/ replacement of assets of Governments / parastatals (Depreciation Reserve Funds of Government Commercial Concerns), for amortization of loans raised by the Government (Sinking Funds) and for other specific and sometimes esoteric purposes, such as Hindu Religious and Charitable Endowment Fund or various Development and Welfare Funds, etc.[4] But these are shown as Government's funds liabilities to the respective funds. The Consolidated Sinking Fund (CSF) and Guarantee Redemption Funds (GRF) are maintained by the States with the Reserve Bank as buffer for repayment of their liabilities. As of March 2019, 24 states are

[4] Some of these funds - like the Sinking Fund, Calamity Relief Fund or State Disaster Response Fund etc. have been created as per recommendations of the successive Finance Commissions.

members of the CSF while 18 are members of GRF. Outstanding investment by states in the CSF and GRF as at end-March 2019 stood at Rs 1.1 lakh crore and Rs 65000 crore respectively.

Some of these are interest bearing and some are not, and all these funds are managed by the Government usually through the Secretaries / Principal Secretaries of the concerned Departments/ Ministries. The Government creates these funds out of taxpayers' money and then pays interest to these funds again by using taxpayers' money; it also controls the use of these funds through its administrators who are its own bureaucrats, but without any accountability to the Legislature, as these funds are maintained outside the Consolidated Fund. Interest bearing funds include Depreciation Reserve Funds of PSUs, Sinking Funds for amortization of loans raised by the Government and for other purposes, Hindu Religious and Charitable Endowment Fund, Various Development and Welfare Funds, State Roads and Bridges Fund, etc., while the non-interest bearing funds include Famine Relief Fund, National/ State Disaster Response Fund (SDRF), Guarantee Redemption Fund, Railway Safety Fund, Rural Employment Guarantee Fund, etc. Many of these funds also remain inoperative for a number of years; CAG had pointed out earlier that Rs 1,674.75 crore was lying in 48 dormant reserve funds of the Government of India by the end of 2014-15. The number of such funds lying with the States run into hundreds.

The Deposit head under 'Deposits and Advances' includes sums deposited with Government in the daily course of business by members of the public, e.g. deposits made in connection with revenue administration, deposits made in civil and criminal courts, security deposits taken from government servants/ contractors when required, public works and earnest money deposits, deposits made by electoral candidates, deposits of local funds of municipalities and panchayats, electricity

boards, housing boards, universities, etc.[5] Like the reserve funds, some of these again carry interest liability while others do not; but all these are included in the Government's total financial liabilities. The non-interest bearing deposits include Defence Deposits, Postal Deposits, Telecom Deposits, National Investment Fund, etc. Civil Advances relate to interest free temporary advances including advances of a permanent nature held by Government officers to enable them to incur contingent expenditure in the day-to-day administration like the Permanent Cash Imprest. They also include the Departmental Advances given to the Departments of Forest, Telecom, Railways, Defence, etc.

Tables 1 through 7 show the Public Account Liabilities of the Central Government, and the liabilities pertaining to the individual components. It is noted that these liabilities amounting to Rs. 9.14 lakh crore constitute 11.7 percent of the total outstanding liabilities of the Government, spread unevenly across its constituent parts.

There is another problem also in the way the government accounts are presented. In the government accounts, Part III - Public Account has the following 6 sectors (indicated by letters of alphabet as per Government accounting procedures):

Public Account

I. Small Savings, Provident Fund and Other Accounts

J. Reserve Funds

K. Deposits and Advances

L. Suspense and Miscellaneous and

M. Remittances

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[5] All these are interest bearing funds.

N. Cash Balance

Thus from the above, it would appear that all individual components of Public Account stand merged with the cash balance of the Government. But the cash balance is actually a balancing item, and is affected by all the three accounts: Consolidated Fund, Contingency Fund and Public Account. Public Account balances, being shown to be merged with the cash balances of the Government, thus inflate them and also make the cash management of the Government fraught with risks. It may be mentioned that balances in Suspense and Remittances are transitional in nature pending their final identification and clearance and do not actually constitute a liability of the Government; the FRBMA 2003 also recognises this and does not consider these as part of the "Other Liabilities" of the Government of India. It would thus stand to reason to club the Suspense and Remittances balances along with Cash Balance and treat this as a separate balancing item, instead of treating these as part of the Public Account.

The way these accounts are maintained, especially the interest bearing ones, again defies all logic. For example, there is one fund created in April 1999 under the Small Savings called the National Small Savings Fund (NSSF) to which all public deposits under the Central Government's small savings schemes (PPF, NSC, KVP, etc.) are credited. States were obliged to borrow 80 percent from this fund initially (and hence pay interest to the Centre), with the option to go up to 100 percent. This borrowing, strangely, is based on availability rather than requirement. Since 2002-03, the net collections were being invested only in States Govt. Securities and thus States are forced to borrow the entire proceeds. But the responsibility to repay to the investors lies with the Centre and these schemes are linked to tax deductions under sec 80 C of the Income Tax Act 1961. They carry interest higher than the market rates and these rates are administered by the Centre.

Securities issued to NSSF used to be a major source of financing the GFD of the States till 2006-07 when the interest rates became more favourable to the market loans and the NSSF share had dwindled; excess NSSF flows before that were also responsible for the subsequent build-up of surplus cash with the State governments.[6] Following the recommendations of 14th Finance Commission, since 2016-17, save Madhya Pradesh, Kerala, Arunachal Pradesh and the Union Territory of Delhi, all other States and Union Territories have opted out of the scope of borrowings through NSSF investments and hence, NSSF no longer finances their GFD. For the Central Government, however, borrowing from NSSF continues to be a source of financing its fiscal deficit and such borrowing was shown under public debt as these were part of the Consolidated Fund; these borrowings comprised the investments in Central Government Special Securities against collections net of withdrawals and reinvestment of proceeds of such investments therein.[7] The remaining liabilities, (i.e. total liabilities of NSSF – such investments) are treated as Public Account' Liabilities of the Centre in the Union Budget.[8]

Similarly, provident funds, the most important constituent of the Public Accounts of the states, are unfunded debt of the State Governments carrying higher than market rates of interest. The net proceeds are entirely available to the states and though the Centre has the ultimate responsibility to repay

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[6] Report of the committee on comprehensive review of the NSSF- MoF, GOI, June 2011, http://finmin.nic.in/ reports/ report_committee_comprehensive_review_nssf.pdf.

[7] Also includes securities which were issued after inception of the NSSF in April 1999 against the outstanding balances under various small savings schemes at the close of March 31, 1999.

[8] This also include the borrowings by States from the NSSF against special securities and loans given to public agencies from the NSSF which should be netted out to reflect solely the Central Government liabilities to NSSF.

the amounts to the depositors, it has no control over the loans taken by the states or their ability to repay the same.

Also, prior to 2009-10, the balances under Small Savings, Provident Fund and Other Accounts used to be in the total outstanding liability of the state governments and other public account balances were excluded as they had the effect of distorting the actual liability carried by the States. These balances often did not represent any real liability; further, their effect would show up in higher cash balances of the state governments leading to a position where most states have surplus cash balances and yet resort to heavy borrowings, the surplus cash being invested under Cash Balance Investment Accounts.

Many of these Public Account funds are again created by transferring taxpayers' money from the Consolidated Fund, and kept at the disposal of the Government. The license to do so freely often allows the Government to devise ingenious ways to defeat the normal accountability controls. One such control is the "Rule of Lapse" of funds at the end of every financial year under any budget grant for which the legislature had voted; such unspent funds, or 'savings', cannot be carried over to the next year and must be surrendered back at the close of the financial year, to be included in the fresh budgetary appropriations next year if needed. One mechanism the Governments often use to defeat such statutory control is to withdraw these savings from the Consolidated Fund and park them in the so-called Personal Ledger Accounts (also sometimes called Personal Deposit Accounts) maintained under the Public Account so that the funds can remain there indefinitely at the disposal of the Government without any legislative scrutiny - an aberrations made possible by the nature of Public Account. Table 8 shows the number of such accounts lying with the states.

The interest liability of the Government of India during 2017-18 on its public account balances was Rs 39485 crore, or

7.8 percent of its total interest liability. In all other countries, similar funds are managed by professional bodies that determine their investment in appropriate assets so as to earn commercial interests to make these funds self-sustainable, without forcing the taxpayers to foot their interest bills.

Paradox of Surplus Cash and Heavy Borrowing

The Gross Fiscal Deficit (GFD) of the Government- the total resource gap in the economy- can be computed as the sum total of its revenue deficit, capital outlay and net lending which is equal to the total expenditure (revenue plus capital) minus revenue and non-debt capital receipts. It is financed partly by raising public debt through borrowing under the Consolidated Fund, partly by using the Public Account resources and the rest by drawing down the cash balances. The entire resources under the Public Account is available to the Government and often the Government is forced to resort to over-borrowing – such over-borrowing leads to building up of idle cash balances that earn very little from their investments in low-earning Treasury Bills, while the Government continues to pay much higher rate of interest on the borrowed funds. Most state governments resort to over-borrowing despite having substantial surplus cash balances that could otherwise be economically utilised to finance their fiscal deficits.

RBI is the banker to any Government and besides the State's deposits with RBI, the cash balance of the State also comprises the investments held in the Cash Balance Investments Account, cash and permanent advances for contingent expenditure with Departmental officers plus the investments of Earmarked Funds under the Reserve Funds. Under agreements with the RBI, every State Government has to maintain a minimum cash balance with it *(about Rs 2-3 crore)*. If the actual cash balance falls below the agreed minimum on any day, the deficiency is made good by taking normal and special ways and means advances/overdrafts and if there is any surplus above the

specified minimum, it is automatically invested in 14-day Intermediate Treasury Bills (ITBs) of the Government of India. This interest rate is significantly lower than that paid on the market borrowings by the governments and hence the interest paid constitutes a negative carry for them. RBI also conducts weekly / fortnightly auctions of treasury bills for maturity periods of 91 days, 182 days or 364 days (Auction Treasury Bills or ATBs) that carry slightly higher rates of interest. Since surplus can be invested cash only in ITBs or ATBs, particularly for the states, they earn lower returns on these investments compared to the interest they pay on their market borrowings; ideally, they should then use their surplus cash balances to meet their GFD financing requirement and thereby curtail their market borrowings.

The surplus cash balance is the difference between the total financing raised by the government (net of all repayments and disbursements) through borrowing under the Consolidated Fund plus the surplus in the Public Account less their GFD requirements. While the borrowing under Consolidated Fund can be adjusted according to the needs, the surplus in Public Account is totally beyond Government's control, and this is what leads to over-borrowing. From Tables 9 and 10, it can be seen that there surplus borrowings were made by both the Centre and the States in some years. In 2016-17, the over-borrowing by the Central Government touched almost Rs 90000 crore, on which the annual average interest liability was Rs 6200 crore calculated at the weighted rate of 6.9 percent. During 2016-17, the Government earned interest amounting to Rs 4851 crore on investments of its cash balance. Even assuming that the entire cash balance investment came from this surplus, the different of additional interest of around Rs 1350 crore was avoidable. Over-borrowing by the States amounted to Rs 31000 crore in 2015-16, Rs 14000 crore in 2016-17 and Rs 17000 crore in 2017-18. Given that states are perennially short of funds, the excess

interest paid on such amounts would have dented their capacity to spend on social or economic services for development.

Government Accounting Standards Board

Thus too many distortions in the government accounting system have been created by the structure of Public Accounts. The Comptroller and Auditor General of India who under Article 150 of the Constitution has the responsibility of prescribing the form of accounts constituted Government Accounting Standards Board (GASAB) in August 2002 for establishing and improving governmental accounting standards for Union and the State Government accounts. The mission of the Government Accounting Standards Advisory Board (GASAB) is to formulate and recommend Indian Government Accounting Standards (IGASs) for cash system of accounting and Indian Government Financial Reporting Standards (IGFRS) for accrual system of accounting, with a view to improving standards of Governmental accounting and financial reporting for enhancing the quality of decision-making and public accountability.

The Government of India, Ministry of Finance, has so far notified only three standards under the IGAS series so far:

1. Guarantees given by Governments: Disclosure Requirements (IGAS 1)
2. Accounting and Classification of Grants-in-aid (IGAS 2)
3. Loans and Advances made by Governments (IGAS 3)

Three more standards already approved by the Board and sent to the Government years ago are yet to be approved or notified by the Government of India:

1. Foreign Currency Transactions and Loss/Gain by Exchange Rate Variations (IGAS 7)
2. Government Investments In Equity (IGAS 9)

3. Public Debt and Other Liabilities of Governments: Disclosure Requirement (IGAS 10)

As far as accrual based Accounting Standards IGFRS series is concerned, the following five standards have been approved by the Board years ago, but again are yet to be notified by Government of India:

1. IGFRS 1: Presentation of Financial Statements
2. IGFRS 2: Property, Plant & Equipment
3. IGFRS 3: Revenue from Government Exchange Transactions
4. IGFRS 4: Inventories
5. IGFRS 5: Contingent Liabilities (other than guarantees) and Contingent Assets: Disclosure Requirements

If the Government treats its recommendations with such scant regard, then perhaps there is a case for the CAG either to revisit these standards or rethink the purpose of creation of the GASAB itself.

Inconsistency in IGAS 10

As stated above, IGAS 10, the Accounting Standard relating to Public Debt and Other Liabilities of Governments: Disclosure Requirement, is still under consideration of the Government. However, the Government Accounts, both at the Union as well as at the State levels, have already incorporated these proposed standards and liabilities are shown accordingly. However, this standard has its own limitations.

Under Article 292 of the Constitution, the executive power of the Union extends to borrowing upon the security of the Consolidated Fund of India within such limits as may be prescribed by Parliament by Law. Article 293(1) of the Constitution provides a similar provision in respect of State Governments. The Fiscal Responsibility Legislations (FRBM

Acts) enacted by the Union and each state place the limits upon their borrowing powers, defined in terms of an upper limit of the ratio of their Gross Fiscal Deficits (GFD) to their Gross State Domestic Products (GSDP). States were given various fiscal incentives under recommendations of the 12th and 13th Finance Commissions for keeping their fiscal deficits within the limits defined in their FRBM Acts.

The objective of the proposed IGAS 10 is to lay down the principles for identification, measurement and disclosure of public debt and other obligation of Union and the State Governments including Union Territories with legislatures in their respective financial statements. It ensures consistency with international practices for accounting of public debt in order to ensure transparency and adequate disclosure. The proposed IGAS 10 now apply to the financial statements prepared by the Union and State Governments and Union Territories with legislature. The IGAS also covers "other obligations", but does not include in its ambit, guarantees and other contingent liabilities and non-binding assurances on behalf of the Government. The disclosure requirement under this IGAS requires that the financial statements of the Union Government, State Governments and the Union Territories with legislature shall disclose the opening balance, additions and discharges during the year, closing balance and net change in rupee terms with respect to internal and external debt as well as other obligations, and also the interest paid by the governments on public debt, small saving, provident funds, reserve funds and on other obligations, and also the interest received on loans and advances given by the governments besides the interest received on investments of cash balances and other items.

The public account by its very structure creates a large number of distortions and anomalies in the Government accounts as explained in the succeeding paragraphs.

1. Fictitious Liability:

As explained earlier, many of these do not represent any real liability, and including them in liabilities has the effect of introducing distortions in the accounts. While some accounts (e.g. provident fund) may represent a real liability, the liability is actually that of the Central Government, while the balances are available to the States for borrowing. The debt is thus guided by availability rather than need for funds. This creates its own distortions in turn, as states often borrow unnecessarily, and as a result build up reserves of surplus cash. If they could use the available cash judiciously, they would be in a position to limit their borrowings to that extent.

2. Interest to be paid public account balances from the Consolidated Fund

Merging of the public accounts into the cash balance creates further distortions; these balances get invested in Treasury Bills with the RBI, earning nominal interest while the actual interest liability of the State Government on these accounts is much more, hence the Government loses money on that account. It is to be noted that interest liability is paid from the Consolidated Funds, even on public account balances in respect of all interest bearing accounts. Hence public account creates a liability for the exchequer even though the legislature has no control over it, neither in respect of the balances nor in respect of the interest. It exercises very limited oversight in respect of utilisation of some of these funds.

3. Funds under Public Account created by transfer from Consolidated Fund

Often funds are transferred out of the Consolidated Funds and kept in the Public Account, outside the constant watch of the auditor and the legislature. Thus funds transferred from the Consolidated Fund to the Personal Deposit accounts in the Public Account to avoid lapse, funds transferred to various

reserve funds – many of whom bear interest, balances in numerous deposit accounts, many of which become inoperative over a period of time, continue to distort not only the accounts but also the public finances. No country outside the subcontinent has such a convoluted system of public accounting. These reserve funds are administered by Secretaries of concerned departments and are vulnerable to misuse also.

4. Over-borrowing by States and Surplus Cash Balance

As already discussed, structure of the public account and their merger with the cash balance leads to the problem of over-borrowing by the States. The surplus cash balance is the difference between the total financing raised by the states (net of all repayments and disbursements) through borrowing under the Consolidated Fund plus the surplus in the Public Account less their GFD requirements. While the borrowing under Consolidated Fund can be adjusted according to the needs, the surplus in Public Account is totally beyond Government's control, and this is what leads to over-borrowing.

But the most perilous and unpredictable consequence of this cash surplus would be its impact on the Union finances, because all cash surpluses from the States invested in treasury bills are automatically available to the Central Government and constitute part of its total financial liability. This is a huge reservoir of resources and temptation to indulge in populism at the cost of these funds is often irresistible, even if we have to ignore their inflationary potential. If these surpluses could be utilized pragmatically to finance the fiscal deficits of the States, the public finances in our country then would be a different story altogether.

5. Anomaly arising out of suspense and miscellaneous and remittances balances being kept outside the scope of IGAS-10

It is to be noted that two components of Public Account, (1) Suspense and Miscellaneous and (2) Remittances we have discussed earlier are not included in the Other Liabilities, for reasons not very well understood. Though both these accounts are of interim, adjustment nature, they holds transactions pending their final identification and consequent credit/ debit to a particular head of account, or to cash. Hence these transactions are as much a part of the accounts as any other; their exclusion thus is not supported by a sound logic.

The logic gets further twisted when we take into account the fact that the entire balance of public account, including the suspense and remittance balances, are taken into account while financing the fiscal deficits of the states. Fiscal deficit is financed by the net borrowing on the Consolidated Fund, together with the net balance available under all public account heads taken together plus the net changes in cash balance of the State. This would create an unresolved anomaly if these two heads of public account are not taken into account while determining the other liabilities of the Government.

As discussed earlier, pragmatic solution to this situation would be to separate the suspense and remittance balances and club these two items with the cash balance. These together then can constitute a new balancing item – instead of only the Cash Balance as is the case now.

6. Application of new definition of Other Liabilities in Government accounts

It is to be noted that with effect from 2009-10, the new definition of the outstanding liabilities of the Government as per IGAS-10 has already been applied in preparation of Government Accounts, even though this standard is yet to be notified by the

Ministry of Finance, Government of India. Earlier the total liabilities of the Government used to comprise the public debt of the Government, that is, internal debt of the Government plus loans from the Centre, besides the public account liability in the form of loans from small savings and provident fund and other accounts only. As per the new proposed accounting standard, Other Liabilities of the Government are now being shown as inclusive of all public account balances, minus the Suspense and Miscellaneous and Remittances balances. This has the effect of depicting the liabilities that may not represent the actual liability of the Government.

Summing Up

The above anomalies will continue to distort the Government account and public finances of the State as well as Union Governments until the public account is completely separated from the Government account. It is high time the Public Account funds are separated from the cash balances and their management entrusted to professional managers relatively free from Government control. That would need appropriate institutional and administrative mechanisms to be set up for the purpose, without perhaps any Constitutional amendment to be made for the purpose. For this, the CAG, CGA, RBI must arrive at a convergence, in consultation with the Union and State Governments to consider separation of public accounts and taking it outside of Government control in a phased manner. This will make these funds self-sustaining and would not create any additional burden for the taxpayers.

It is important to appreciate that efficient debt management requires equally effective cash management which will not be possible till the time the cash balances are separated from public account. At the same time, since on many public account heads, the Government carries an interest liability, it is imperative that these funds be deployed in such manner so as earn the maximum return without compromising the safety of

money that belongs to the public. Since these funds are not taxpayers funds, it is improper to make the taxpayers shoulder the burden of paying interest on these funds. These funds should be deployed in such a manner so as to make them self-sustaining in discharging their interest and other obligations.

Tables

Table 1: Public Account Liabilities of the Central Government

	2013-14	2014-15	2015-16	2016.17	2017-18
Total Public Account Liability (Rs Lakh Crore)	7.23	7.61	8.16	8.57	9.14
Public Account Liability as % of Total Liability, of which	13.6	13.0	12.5	12.2	11.7
NSSF	2.0	1.7	2.0	2.0	1.7
State Provident Fund	2.7	2.6	2.6	2.6	2.6
Other Accounts	5.9	5.4	4.9	4.6	4.2
Reserve Funds and Deposits, of which	2.9	3.2	3.0	3.0	3.2
Bearing Interest	1.8	1.9	1.9	1.8	1.8
Not Bearing Interest	1.1	1.4	1.1	1.1	1.4

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years.

Table 2: Liabilities and Investments of NSSF (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016.17	2017-18
Total Liabilities of NSSF	8.58	9.08	10.15	11.32	12.90
Investments of NSSF, of which	7.49	8.06	8.85	9.90	11.53
Borrowings by Centre	2.29	2.61	3.13	3.81	4.84
Borrowings by States	5.19	5.43	5.71	5.38	5.07
Loans to IIFCL	0.02	0.02	0	0	0

Loans to Public Agencies	0	0	0	0.7	1.6
Net Liabilities	1.09	1.02	1.3	1.42	1.37
Net Liabilities of NSSF as % of GDP	1.0	0.8	0.9	0.9	0.8

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 3: Liabilities of State Provident Funds (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016.17	2017-18
Total Liabilities	1.43	1.55	1.67	1.85	2.01
As % of GDP	2.7	2.6	2.6	2.6	2.6
As % of Total Liabilities	1.3	1.2	1.2	1.2	1.2

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 4: Liabilities of Other Accounts (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016-17	2017-18
Special Securities Issued in lieu of Subsidies, of which	1.66	1.63	1.63	1.63	1.63
Securities Issued to Oil Marketing Companies	1.34	1.31	1.31	1.31	1.31
Securities Issued FCI	0.16	0.16	0.16	0.16	0.16
Securities Issued to Fertiliser Companies	0.16	0.16	0.16	0.16	0.16
Other Accounts Liabilities as % of Total Liabilities	3.1	2.8	2.5	2.3	2.1

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 5: Liabilities of Reserve Funds (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016-17	2017-18
Total Reserve Fuds	0.30	0.35	0.32	0.26	0.44

As % of Total Liabilities, of which	0.6	0.6	0.5	0.4	0.6
Bearing Interest	0.2	0.2	0.2	0.1	0.1
Not Bearing Interest	0.4	0.4	0.3	0.3	0.5

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 6: Liabilities of Deposits (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016-17	2017-18
Total Deposits	1.26	1.53	1.66	1.82	2.09
As % of Total Liabilities, of which	2.4	2.6	2.5	2.6	2.7
Bearing Interest	1.6	1.7	1.7	1.7	1.7
Not Bearing Interest	0.7	0.9	0.9	0.9	0.9

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 7: Liabilities of Advances (Rs Lakh Crore)

	2013-14	2014-15	2015-16	2016-17	2017-18
Total Advances	-0.02	-0.02	-0.01	0	0
As % of total Liability	-0.03	-0.03	-0.02	0	0

Source: Status Report of Public Debt 2017-18, Govt. of India and Union Finance Accounts for respective years

Table 8: Number of Personal Deposit Accounts in States

State	Total Number of PD Accounts as on March 31, 2017	Balance as on March 31, 2017 (₹Crore)	Nature of Balance (Dr/ Cr).
Andhra Pradesh[9]	58539	357	Cr.

[9] Andhra and Telangana marks every grant relating to devolution or transfer either from the state or the centre to the third tier of government as a PD account (8448-106). Other states mark them under 8443-106. CAG has constitute a Committee to regulate the PD accounts and to see that it is not opened only to avoid the lapse of funds, and also to ensure that PD accounts remain open for not more than a limited period.

State	Total Number of PD Accounts as on March 31, 2017	Balance as on March 31, 2017 (₹Crore)	Nature of Balance (Dr/ Cr).
Arunachal Pradesh	15	0	Cr.
Assam	26	1	Cr.
Bihar	177	4459	Cr.
Chhattisgarh	281	1892	Cr.
Goa	118	67	Cr.
Gujarat	478	395	Cr.
Haryana	124	235	Cr.
Himachal Pradesh	113	2	Cr.
Karnataka	64	2942	Cr.
Kerala	1144	126	Cr.
Madhya Pradesh	799	5350	Cr.
Maharashtra	2528	13335	Cr.
Manipur	2	2	Cr.
Meghalaya	7	6	Cr.
Nagaland	1	0	Cr.
Odisha	827	456	Cr.
Punjab	161	34	Cr.
Rajasthan	1528	5196	Cr.
Tamil Nadu	735	442	Dr.
Telangana[8]	28087	33	Dr.
Uttar Pradesh	1317	13	Dr.
Uttarakhand	19	185	Cr.
West Bengal	153	5141	Cr.

Source: Union Finance Accounts and CAG Audit Reports on State Finance of individual states for 2016-17

Table 9: Financing of GFD of the Centre (Rs Lakh Crore)

	GFD	Cash Drawdown	Over-borrowing
2013-14	5.0	-0.2	0.2
2014-15	5.1	+0.8	
2015-16	5.3	+0.1	
2016-17	5.4	-0.9	0.9
2017-18	5.9	+0.4	

Source: Union Finance Accounts for respective years

Table 10: Financing of GFD of States (Rs Lakh Crore)

Year	Gross Fiscal Deficit (GFD)	Cash Drawdow n	Over-borrowin g
2013-14	2.48	0.18	
2014-15	3.27	0.18	
2015-16	4.21	-0.31	0.31
2016-17	5.34	-0.14	0.14
2017-18	4.10	-0.17	0.17

Source: State Finances: A Study of Budgets of 2019-20, RBI

PUBLIC FINANCIAL MANAGEMENT SEEN THROUGH THE PRISM OF PEFA

Mrs. O GGP CMUJ KI WRVC*

Introduction:

1. Public financial management (PFM) supports accountability and efficiency in the management of public resources and delivery of services, which are critical to the achievement of public policy objectives. It plays a crucial role in achievement of development goals and implementation of national policies. The development goals including poverty reduction, gender equality, inclusive growth, health and education for all etc. require huge financial resources. Given limited capacity to generate tax and non-tax revenues, prioritization of competing demands and effective and efficient use of scarce resources becomes an essential requirement for any Government. Thus the efficacy and effectiveness of the PFM becomes critical for overall fiscal discipline and achievement of stated goals of public policy.

2. In view of the complexities of the processes involved and association of a large number of stakeholders and institutions, it is not possible to assess the effectiveness of PFM through one index. Various agencies over the years, have carried out Expenditure Reviews etc. as an assessment tool. So far, Public Expenditure and Financial Accountability (PEFA) framework

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appears to be the most robust framework to review the PFM. This paper attempts to study how the seven pillars of PEFA assess the various components of PFM and gain an insight into how they facilitate accountability, efficiency and effectiveness in meeting the desired policy objectives. The section I of the paper describes the Public Financial Management and its various components, section II describes the PEFA framework as a measurement tool to assess the effectiveness of PFM and section III discusses the Way Forward.

What is Public Financial Management?

3. Public Financial Management refers to the laws, rules, systems and processes used by the Governments to mobilize resources, allocate public funds, undertake public spending, account for funds and obtain audit results. The basic objectives of the PFM system are aggregate fiscal discipline, allocative efficiency, operational efficiency and ensuring transparency and accountability in the entire process. PFM system is expected to ensure that the policies of governments are implemented as intended with desirable fiscal and budgetary outcomes:

- **i. Aggregate fiscal discipline** refers to effective control of the total budget and management of fiscal risks.
- **ii. Strategic allocation of resources** involves planning and executing the budget with the aim of achieving policy objectives.
- **iii. Efficient service delivery** refers to optimal use of budgeted revenues to achieve the best levels of public services

4. The main stakeholders of the PFM include the Legislature, Government namely the Ministry of Finance and the executing ministries, the implementing agencies and various service providers and of course the Civil society. The concept of PFM has been evolving over time. In its narrowest form, it refers

to how the governments manage the budget through the three phases of formulation, approval, and execution. Over the years, concept has evolved from expenditure to managing public resources, including resource mobilization and debt management, involving medium- to long-term implications and risks to public finances from today's policy decisions.

5. It is generally characterized by six stages beginning with policy formulation and ending with external audit conducting an independent evaluation of the entire exercise. The Stages in PFM are:

Figure1: Stages in PFM

6. Budget preparation is a highly technical and complex function given the political choices, limitations on revenue generation through taxes and committed liabilities of the Government. This being a financial document, the emphasis is on how the resources are raised though taxes, non-tax revenue and debt; and the application of resources to various competing

demands to fulfill the policy objectives. There is no explicit connect with the outputs/outcomes expected to be achieved. In some countries this is addressed by preparing a Performance Program Budget Document.

In India, this was addressed by presenting an Outcome Budget along with Budget. Output Outcome Monitoring Framework has been introduced with effect from 1 April, 2017. It typically includes the financial outlays, outputs/deliverables against the outlays and projected medium term outcomes in respect of all the major schemes.

7. Typically, the Budgets are prepared by the Finance Ministry in consultation with line ministries including the Government Departments. The countries may also have a formal system of engaging with stakeholders at the time of preparation of Budget. The Budget is presented by the Finance Minister to the Parliament annually as per the legal framework.

8. The budget is examined by the Legislature as per the legal framework and passed by the law makers after appropriate scrutiny of the budget proposals.

In India, since 2016, the Budget is presented on First February every year by the Finance Minister in the Parliament as per the Constitutional provisions. Every Demand for Grant is examined by the concerned Parliamentary Standing Committee during the recess period of the Budget Session of the Parliament. Thereafter, the Budget is approved by the Parliament as per the Constitutional provisions.

9. Budget execution is the real crux. It may be interesting to note that during the course of the year through Supplementary Demands passed by the Parliament the initial allocation of funds for the Schemes may get altered. At the Revised Estimates stage also, allocations to Ministries and Departments may undergo a revision and in some cases substantially. The Schemes and

Projects have to be implemented as per the approved design and timelines and this entails incurring of the expenditure and booking of expenditure. From the accounting perspective, significant savings and excesses have to be explained. In fact, the excess expenditure is required to be explained in all the cases and is to be regularized by the Parliament. However, this does not cover the outcomes and quality of expenditure.

10. External Audit is expected to review and examine the entire process independently and give the audit opinion on the overall process, which should be used as feedback mechanism to bring in appropriate changes in the scheme design or delivery mechanisms. Every country has a Supreme Audit Institution that functions as an Independent External Auditor and submits its report to the Parliament.

In India, as per the Constitutional Provisions the External Audit of all Government transactions is carried out by the CAG of India and reports submitted to the Parliament or State Legislature as the case may be. These Audit Reports are in turn subjected to legislative scrutiny through PAC and COPU, who may call the Executive for oral evidence and thereafter submit their Report and Recommendations to the Parliament.

11. The PFM framework appears to be rather comprehensive as it involves the stakeholders and engages with the concerned institutions. It covers various stages of decision making in preparation of budget, legislative scrutiny of the budget and evaluation by the auditors as the last stage of the process. While in this process, the fiscal discipline is certainly assessed the other major objectives of the PFM namely allocative efficiency and operational efficiency are assessed only indirectly. The budget execution in financial terms does not capture the outputs and outcomes. A zero deviation between Budget Estimate and Actual Expenditure does not imply that physical target has been achieved, leave alone the desired outcome.

12. Public Expenditure and Accountability Framework is used as a tool for assessing PFM. It was developed in 2002 and since evolved and is used both by the donor agencies as well as the Governments.

Public Expenditure and Accountability Framework for Assessing PFM

13. The Public Expenditure and Financial Accountability (PEFA) program was introduced in 2005 as a tool to assess the Public Financial Management in any country. It was revised in 2016 and over the years more than 500 assessment stated to have been done. PEFA program provides a framework for assessing and reporting on the strengths and weaknesses of Public Financial Management using evidence based quantitative indicators to measure performance. It measures the extent to which PFM systems, processes and institutions contribute to the achievement of aggregate fiscal discipline, strategic allocation of resources, and efficient service delivery. It provides a framework for assessment of transparency, accountability and timeliness in terms of access to information and reporting in key areas like budgetary exercise and external audit etc.

14. PEFA identifies seven pillars for assessment of a PFM system. The PEFA framework assesses and reports on the strengths and weaknesses of public financial management using 31 performance indicators corresponding to seven pillars that are further disaggregated into 94 dimensions. The performance of each indicator and dimension is measured against a four-point ordinal scale from A (indicator of good performance) to D (performance is below the basic level). The seven pillars of PEFA for assessment of a PFM system are discussed below:

I. Budget reliability

15. Public financial management refers to effective management of the collection of revenues and expenditure of funds by governments. The budget should reflect overall

economic policy of the government encompassing all revenues and expenditures accurately and in a comprehensive manner. Actual revenues and expenditures are compared with the original budget, as a measure to assess that the government budget is realistic and implemented as intended. Specific indicators to measure this pillar include:

i. Aggregate expenditure outturn

ii. Expenditure composition outturn

iii. Revenue outturn

II. Transparency of public finances

16. Information on public financial management should be comprehensive, consistent, and accessible to users. Transparency of public finances is reflected in quality of documentation as well as completeness of information. There should be no off budget transactions. This is achieved through comprehensive budget classification, transparency of all government revenue and expenditure including intergovernmental transfers, published information on service delivery performance and ready access to fiscal and budget documentation. Transparency of public finances is measured through following indicators:

i. Budget classification

ii. Budget documentation

iii. Central government operations outside financial reports

iv. Transfers to subnational governments

v. Performance information for service delivery

vi Public access to fiscal information

III. Management of assets and liabilities

17. Effective management of assets and liabilities is critical for public financial management in any economy. Recording of assets and managing the liabilities including debts and guarantees has to be ensured for inter-generational equity as well. Public investments must provide value for money. The indicators to measure this pillar are listed below:

i. Fiscal risk reporting

ii. Public investment management

iii. Public asset management

iv. Debt management

IV. Policy based fiscal strategy and budgeting

18. The fiscal strategy must be clearly defined and should be compatible with the strategic plans, and macroeconomic and fiscal projections. Engagement with the stakeholders at the time of preparation of budget is necessary to ensure participation of all the institutions. There must be a detailed legislative scrutiny before the budget is passed. This can be measured through following indicators:

i. Macroeconomic and fiscal forecasting

ii. Fiscal strategy

iii. Medium-term perspective in expenditure budgeting

iv. Budget preparation process

v. Legislative scrutiny of budgets

V. Predictability and control in budget execution

20. Budget execution is most critical part of the PFM as it is linked to service delivery and is expected to strike appropriate balance between revenue generation and utilization of the same

for intended purpose. The implementation of budget is guided by prescribed standards, rules, regulations, processes, and internal controls. ensuring that resources are obtained and used as intended. This can be measured through following indicators:

i. Revenue administration

ii. Accounting for revenue

iii. Predictability of in-year resource allocation

iv. Expenditure arrears

v. Payroll controls

vi. Procurement

vii. Internal controls on non-salary expenditure

viii. Internal audit

VI. Accounting and reporting

21. Integrity of financial data and dissemination of accurate and reliable information is corner stone of effective PFM. This also facilitates decision-making by policy makers and management by executive. The indicators for measuring this pillar are listed below:

i. Financial data integrity

ii. In-year budget reports

iii. Annual financial reports

VII. External Scrutiny and audit

22. Independent review and examination of the entire process by the external audit is absolutely essential to get an assurance regarding transparency of the process and accountability mechanism. The relevant indicators in this regard are:

i. External audit

ii. Legislative scrutiny of audit reports

23. PEFA is the most comprehensive tool available today to assess the strengths and weaknesses of PFM in any country. It has been widely used by the donor agencies and countries themselves. While, seven pillars and 31 indicators with 91 dimensions are very comprehensive to assess fiscal discipline in the Government, the issues of allocative efficiency and operational efficiency are not adequately captured. Budget execution does cover the payroll controls and procurement controls but implementation of schemes and projects is far more complex than that. Further, these indicators are very process oriented and there is emphasis on timelines. Quality aspects for example quality of expenditure need to be factored in to address the issues of allocative and operational efficiency.

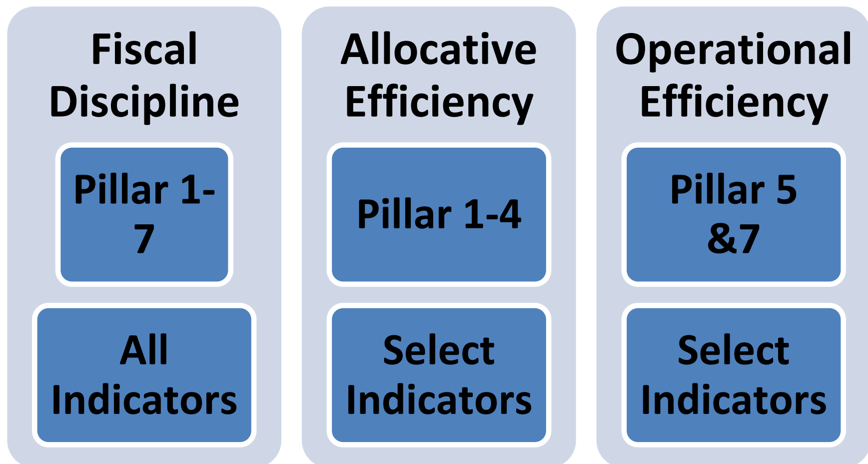
Way Forward

24. An ODI research paper in 2016 observed, "The Public Expenditure and Financial Accountability (PEFA) framework has been hugely successful in harmonising approaches to public financial management (PFM) systems in developing countries, and remains the most comprehensive indicator of PFM to date. However, not all elements of the framework are universally relevant, and indicators do not always capture which systems are not working or why." It further mentioned that, PEFA ratings should be just one input in any reform process. More could be done to interpret which ratings matter in each national context, and why.

25. As has been mentioned earlier that the basic objectives of PFM are Fiscal sustainability, allocative efficiency and operational efficiency. Seven pillars of PEFA are expected to relate to these objectives. If we look at the PFM cycle, it predominantly caters to fiscal discipline and allocative efficiency and operational efficiency though stated to be

objectives of PFM are not explicitly covered by the PFM cycle. External audit may comment upon the operational efficiency through Value for money audits but that may be restricted to specific schemes/ projects. If we analyze the three objectives of PFM in conjunction with seven pillars of PEFA, then again, there is a preponderance of Fiscal Discipline. Indicators like Debt Management, Medium term perspective in Expenditure Budgeting may refer to allocative efficiency, indicators like payroll control, procurement etc. may refer to operational efficiency though only partially.

Figure 2: Correspondence of PFM objectives to PEFA



26. Recent PEFA report on Global PFM for 2020 has observed,

*"*Countries on average perform better in preparing their budgets than executing them. Internal audit, management of fiscal risks, external audit, and scrutiny by Supreme Audit Institutions and the legislature remains the weakest areas of PFM. The budget preparation process, predictability of in-year resource allocation, internal controls on non-salary expenditure, and debt management were the highest scoring areas. Gender considerations in the design, implementation, and evaluation of

budget policies are not yet mainstreamed in most countries, though some countries have made important advances in this area."

27. It may be mentioned that PEFA, itself recognizes that the indicators focus on the operational performance of key elements of the PFM system and thus do not measure every factor affecting PFM performance, such as the legal framework or human resource capacities within the government. It also does not involve fiscal or expenditure policy analysis that would determine whether fiscal policy is sustainable. It does not evaluate whether expenditures incurred through the budget ultimately have their desired effect on reducing poverty or achieving other policy objectives, or whether value for money is achieved in service delivery.

28. In view of above, it may be interesting to explore on how to bring in the issues relating to efficient service delivery in this framework since that is a stated objective of PFM. The regulatory part is covered by indicators relating to pay roll data and procurements. Keeping in view of the broad framework, an indicator could be added to address the issue of efficient service delivery within the Pillar V (Predictability and Control in Budget Execution). It may be called, "Efficiency of Service Delivery". The dimensions under this indicator may include the following:

i. Desirable outcomes against outlays

ii. Outturn of outcomes against the projected outcomes

iii. Monitoring and Evaluation Framework

29. The Global PFM Report 2020 has also suggested the areas which may require further research. One of the suggested areas is, "Role of PFM in Improving Service Delivery." PFM is an enabling element in the governance process. Fiscal discipline, improved service delivery, inclusive growth etc. have

been engaging attention of policy makers, academia and citizens for quite some time. It may be useful to add the indicator relating to service delivery with the suggested dimensions to the seven pillars of PEFA to make it more comprehensive.

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PUBLIC AUDIT: INCREASING NEED FOR STAKEHOLDERS' ENGAGEMENT

K.P. SHASHIDHARAN[*]

Part 1

Introduction

Let me begin asking a few fundamental questions of the raison detre of the government audit? For whom is the public audit meant for? Does the Supreme audit institution (SAI) of India – the office of the Comptroller and Auditor General (CAG) require more intense and extensive stakeholders' engagement if its mission is to make a difference in the lives of the citizens of India by improving the audit quality, content, outputs, outcome and outreach? Does CAG need more effective communication strategy to increase its visibility and impact? Does CAG provide adequate facilities for its stakeholders' sharing their inputs for selection of audit subject matter? Does CAG encourage red flags from the stakeholders on deficiencies on implementation of government programmes, projects and activities to be used as inputs in risk assessment, audit process and audit cycle for bringing in better citizen centric quality audit products? Will enhanced stakeholders' involvement result in value addition by bringing in more pragmatic audit recommendations to improve governance? Can the CAG website be transformed as an effective platform for more effective dissemination of tis audit activities, processes, products, audit recommendations and follow up? Does CAG provide a multi-layer interactive communication platform for its stakeholders including the

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common citizens to share their concerns and contribute in the on-going audit activities? Does CAG need to revamp its communication policy, strategy, methodology to allow print, electronic, social media to use the public domain of its website more effectively for grievance redressal of the citizens, Civil Society Organizations, Non-government Organizations and other stakeholders? Can CAG website be not extended to facilitate whistleblowing facilities with assured confidentiality to the aggrieved personnel from the public entities and the general public? These are pertinent issues to be deliberated and considered for suitable policy formulation by the nation's supreme audit intuition – the CAG of India.

Enhancing the quality of public audit outputs, audit outcome, impact and outreach is critical for any SAI. It is true of CAG as well. The question is how does the national audit office improve its visibility, contribution and impact to the lives of the citizens in the country. Purposeful engagement with its external stakeholders viz. legislators, civil society organizations, non-government organizations, academia, media, community leaders, citizens and most importantly the auditees in the audit process to the extent possible from the selection of subject matter for audit, planning, implementation, evidence gathering, reporting and follow up can increase value addition, more value for money and impact from government audit. Public audit products will become more people centric by adopting best practices in participatory audit methodology and practices. This will be in sync with CAG's constitutional and legal mandate, duties, role and responsibilities. Further increased stakeholders' engagement will synchronize with the governance goals of accelerating reforms, better performance and thereby making a difference in the lives of the public. Public audit must continue to increase its value for its main stakeholders, legislature, executive and citizens.

SAI’s increasing role

SAI has a significant role in ensuring public accountability, transparency, efficient and effective public administration, equitable and inclusive, principles and rules driven governance. The CAG of India’s role in public accountability architecture assumes greater significance by holding public functionaries who execute policies, programs and projects, expending substantial public funds to be answerable to the people’s representatives. CAG’s mandate is to “watch” over government accounts, operations, activities, expenditure, rule compliance and performance with reference to the policy objectives, envisaged outputs and outcome. Sustained interaction with the concerned stakeholders including the executive, legislature, media, civil society organizations and citizens is indispensable for citizen centric public audit output. INTOSAI had emphasized this concern way back at INCOSAI 2010[1], “The effectiveness with which SAIs fulfill their role of holding the government to account for the use of public money not only depends on the quality of their work, but also on how effectively they are working in partnership with the accountability functions of the legislature as well as the executive arm of government in making use of audit findings and enacting change.”

INTOSAI IFFP Core Principles governing SAIs: P - 12

CAG has been adapting INTOSAI good practices in stakeholder engagement in line with its mandate to continuously improve the quality of its audit reports. Stakeholder engagement is a priority of any SAI functioning as found out by INTOSAI-IDI global survey in 2014. INTOSAI core principle INTOSAI-

[1] XX INCOSAI in Johannesburg, South Africa (November 2010)

P-12 states that the value SAIs is making a difference to the lives of citizens. The following 12 principles are core for any SAI[2]:

"Principle 1: Safeguarding the independence of SAIs

Principle 2: Carrying out audits to ensure that government and public sector entities are held accountable for their stewardship over, and use of, public resources

Principle 3: Enabling those charged with public sector governance to discharge their responsibilities in responding to audit findings and recommendations and taking appropriate corrective action

Principle 4: Reporting on audit results and thereby enabling the public to hold government and public sector entities accountable Demonstrating ongoing relevance to citizens, Parliament and other stakeholders

Principle 5: Being responsive to changing environments and emerging risks

Principle 6: Communicating effectively with stakeholders

Principle 7: Being a credible source of independent and objective insight and guidance to support beneficial change in the public sector

Being a model organization through leading by example

Principle 8: Ensuring appropriate transparency and accountability of SAIs

Principle 9: Ensuring good governance of SAIs

Principle 10: Complying with the SAI's Code of Ethics

Principle 11: Striving for service excellence and quality

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2 https://www.issai.org/pronouncements/intosai-p-12-the-value-and-benefits-of-supreme-audit-institutions-making-a-difference-to-the-lives-of-citizens/

Principle 12: Capacity building through promoting learning and knowledge sharing."

Need for effective communication strategy with stakeholders

Good communication is essential with audited entities and other related stakeholders to inform them about the audit process. The legislature, its committees, audited entities' management and governing boards must know relevant information. Professional relationships with legislative oversight committees and audited entities' management and governing boards must be maintained to help them understand relevance of audit reports, recommendations and need for taking appropriate corrective and preventive actions on time. Audit reports must be available in a simple and clear language without terminology that can be understood by all stakeholders. CAG's website should make all its reports publicly accessible in a timely manner. Recently, CAG office decided not to put its defense reports on its website. This policy decision is not in sync with effective communication strategy with the stakeholders and the best practices of INTOSAI. All the defense reports of NAO, GAO, European Court of Auditors, CAG of Canada, Australia etc. are placed on the website for public access.

CAG institution should be able to facilitate access to its all reports by the stakeholders, choosing effective communication strategy, methodology, techniques and innovative digital platforms, apps and software tools. Involvement of stakeholders enable CAG for better information and evidence gathering. Communicating effectively with the stakeholders increases stakeholders' knowledge and understanding of the role and responsibilities of CAG as an objective, national accountability enforcing independent functionary. Communication should enable the stakeholders' awareness of CAG's role and the need to enforce transparency and accountability in the public sector. Communication with stakeholders ensures their understanding of CAG's audit

activities, intent, process, outputs and results. Interaction through electronic, print and social media facilitate better visibility of audit reports and knowing their significance as an instrument of effecting better governance. Periodical evaluation of communication and stakeholders' strategy is important for enhancing transparency and enforcing public accountability Communicating widely on audit activities and audit results through the all the media including digital media platforms, social media and websites will strengthen stakeholders' involvement in the audit process.

The United Nations Convention against Corruption, vide Article 2 requires 'developing coordinated anticorruption policies involving social participation'. Article 9(2) states on 'fostering transparency and accountability in the management of public finances. Article 13 focus on 'promoting civic engagement in the prevention and fight against corruption and providing wide access to information, promoting effective civic engagement in accountability processes, i.e., external auditing.

Stakeholders' engagement in public audit process

INTOSAI guideline on 'Communicating and Promoting the Value and Benefits of SAIs' discusses tools to promote stakeholder participation in auditing, such as:

"Facilitating civil complaints

Authorizing audit requests by citizens

Conducting joint/participatory audit projects with non-SAI organizations

Gathering feedback from citizens on issues under review by SAI[3] this strategic management framework envisages a well-

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[3] INTOSAI's IDI developed a SAI strategic management framework, aligned to the SAI Performance Measurement Framework (SAI PMF)

functioning SAI must be able to deliver value and benefits for the citizens of its country by conducting high-quality audits and reporting on them without fear or favour, in order to contribute to the accountability, transparency and ethical behavior of those charged with governance. CAG can also add value by contributing to the fulfilment of the commitments made by India towards achievement of the United Nations Sustainable Development Goals (SDGs) customized and contextualized for India by taking up crosscutting subject matter relating to 17 SDGs and 169 targets and using criteria developed for the nation by the indicators. Engagement with external and internal stakeholders by effective internal and external communication helps in achieving better audit outcomes, e.g.; implementation of audit recommendations, improvement in service delivery, and governance etc.

Stakeholders such as citizens, media and CSOs can put pressure on legislative, judiciary and executive agencies to help implement audit recommendations, enforce corrective actions, monitor the executive´s follow-up on audit reports, judgments/sanctions and subsequent decisions taken by parliamentary committees and other watchdog institutions created by the legislation responsible for oversight functions. As CAG makes its work visible and engages with external stakeholders, they can build trust, help reinforce CAG's autonomy and independence. Both external and internal stakeholders including citizens and CSOs can help in strengthening CAG's functional autonomy by lobbying for greater SAI independence. Stakeholders can help to improve service delivery and respect for democracy and human rights. Stakeholders can be trained in financial management and auditing. The control of public finances is done by the legislature

by performing effective oversight function. CAG can help the committees of Parliament such as PAC and CoPU.

The executive is charged with the execution of laws and policies and the administration for public affairs and responsible of implementing the audit recommendations. The Ministers and Departments, attached, subordinate offices and ABs encompassing the executive are responsible for effective follow up of audit recommendations.

The judiciary is responsible for administering the justice system deals with cases relating to fraud and corruption that the SAI may come across in the course of the audit. Civil Society Organizations comprising wide array of non-governmental and not-for-profit organizations express the interests and values of their members. CSOs are an important sector of the demand side of accountability and play a critical role in promoting transparency and holding the government entities accountable. The media who are non-state actors involved in the collection and communication of information to the citizens, such as newspapers, radio, TV channels, social media, websites, audio, text, podcast, digital platforms, Apps, etc. has a predominant role in ensuring public accountability and transparency and proper democratic process and functioning. Other accountability institutions (anti-corruption and internal control agencies, ombudsmen, etc. both internal control agencies including watchdog and investigation agencies can turn out to be allies in fostering effective accountability. They use CAG reports for follow-up action.

There are two types of identifiable relationship between CAG and its stakeholders: the relationship based on laws and regulations - institutionalized stakeholders; and the relationship that arises out of interactions that are not supported by law or regulations - non-institutionalized stakeholders. Stakeholders such as the legislature, executive, judiciary, and audited entities fall into the first category. Internal stakeholders include officers

and staff of CAG also belong to this category. In order to develop relationships with non-institutionalized stakeholders, there is no explicit law, regulation or policy. Based on the mutual interest for ensuring more accountability and transparency and democratic trends of increasing demands on good governance—these interactions can be formalized. In this category are the citizens, the media, community, academia, professional bodies and the cooperating parties.

Part - II

Expectations from stakeholders' engagement in public audit process

Enhanced stakeholder consultation and involvement in audit process can help in the following ways:

- Conducting quality audits help in strengthening the accountability systems of public resources, implementation of SDGs and the fight against corruption
- SAI can lead by example in professionalism, transparency and accountability, ethical commitment
- Uses stakeholder's information in selecting audit topics that are of public interest
- Complies with standards in conducting the audits
- Provides timely, quality and user-friendly audit reports
- Provides capacity-building for easy understanding of SAI mandate and products
- Offers technical support on specialized topics/reports for easy decision-making
- Provides reliable and easy access to all information on the mandate, activities and products of CAG of India
- Shares insights and key audit messages relating to the stewardship of public funds, implementation of

government policies and compliance with applicable legislation and regulatory regime

- Consistent support according to legal framework
- Support of CAG to take into account specific requests/topics of particular interest Judiciary
- Close coordination and exchange of information about issues that fall under the judiciary (fraud and corruption)
- Information to executive on the key financial and performance management risks faced by the ministries or any government agency
- Support of CAG to take into account specific topics of particular interest
- SAI Professional/academic bodies help in providing better technical support and feedback in the development of specialized themes
- Partnership arrangement with professional and academic bodies
- Internal stakeholders of CAG including officers and Staff in creating good leadership from top management and open culture
- Good internal governance and promotion of ethics within the SAI
- Citizens and CSOs increase in participation in the audits
- Establish complaint handling mechanism
- Cooperating partners provide advice and participation in the audit of projects funded by the donors
- Media help in translation of technical language for easier understanding by the public

- ➢ Using targeted platforms enable to engage members of the media on key audit messages
- ➢ Audited entities find audit findings and recommendations more understandable, fair, balanced, and possible to be implemented

CAG office's expectations from its stakeholders can be:

- ❖ Greater audit impact
- ❖ Give access to reliable and timely information
- ❖ Cooperate meaningfully during the audit process
- ❖ Implement recommendations and regulations
- ❖ Give priority to audit or cases that are of public interest to help in fighting fraud corruption
- ❖ Help to promote the independence of CAG
- ❖ Keep informed about the measures taken against cases reported by CAG
- ❖ Promote CAG's independence by not subject to political pressure
- ❖ Implement the audit recommendations and sanctions
- ❖ Comply with the applicable acts, rules and standards and enforce internal control
- ❖ Improve social control on public administration
- ❖ Give reliable information when providing inputs or complaints about the management of public funds
- ❖ Help raise public awareness of CAG's products and the need to promote greater SAI independence
- ❖ Demonstrate professionalism in conducting audits
- ❖ Comply with CAG's policies, rules and regulations

- ❖ Advocate for greater CAG independence
- ❖ Provide financial and technical support
- ❖ Coverage and disseminate

CAG's products to the citizens will help:

- Promote the mandate of the CAG in the national media agenda topics
- Identify significant issues/topics for inquiry
- Provide support in following up CAG's recommendations
- Provide support in formulating relevant laws and regulations
- Promote CAG independence

Building good links with stakeholders

CAG office needs to maintain good links with the executive, the judiciary, and with the legislature to facilitate effective governance, justice, oversight and accountability. Good relations with the media and CSOs ensure that CAG's audit findings reach the citizens. Cooperating partners, professional and academic bodies, and internal stakeholders also play a critical role in operations of CAG, such as conducting the audits, by acting as advocates in improving the SAI's own capacity, among others. Dissemination of audit reports via internet, writing summary reports, holding meetings with relevant Parliament committees, organizing press conferences, translation of audit reports to local languages, sending newsletters to journalists, disclosure of institutional information etc. help to inform the stakeholders. A two- way communication mechanisms like use of social media to get feedback and provide explanations to citizens, creating Citizen complaint mechanisms, holding meetings with CSOs/ relevant parliament

committees to get suggestions on future audit subjects, etc. will enable CAG to improve its visibility, citizen centric audit outputs, outcome and outreach.

Engaging with key stakeholders including citizen for strengthening the accountability, transparency and integrity of public sector entities will demonstrate relevance and benefit of public audit to citizens, Parliament and other stakeholders and help CAG of India to be perceived as model organization through leading by example. However, engaging with stakeholders in the audit process should not in any way allow to compromise or dilute the constitutional and legal mandate or autonomy and independence of CAG of India. The stakeholders' engagement policy must be clearly defined by CAG to achieve the identified outcome. The policy on engaging with stakeholders can assimilate suitably the good practices on stakeholder mapping, stakeholder management strategy, action plan, communication policy. Identification of the relevant stakeholders who can add value to the selected audit subject matter, modus operandi of engagement, assessment of its effectiveness with desired objectives, key domains where inputs to be obtained, issues and challenges in stakeholders' management practices can be addressed.

CAG's audit focus on internal control deficiencies, applicable legal and rule compliance, effective revenue assessment and collection, budgeting, public expenditure control, prudential financial management, procurement and project management, and service delivery. Public audit has designed 3 audit frameworks, financial audit, compliance audit and performance audit to achieve these audit objectives. While financial audits examine the financial statements of public entities to see whether they are prepared in accordance with a

Financial Reporting Framework[4] whose objectives include matters such as:

States' or entities' accounts or other financial reports not necessarily prepared in accordance with a general-purpose financial reporting framework;

1. Budgets, budget sections, appropriations and other decisions on allocation of resources and the implementation thereof;
2. Policies, programmes or activities defined by their legal basis or source of financing;
3. Legally defined areas of responsibility, such as the responsibilities of ministers; and
4. Categories of income or payments or assets or liabilities.

Compliance auditing is an independent assessment[5] of whether the subject matter chosen for audit is in compliance with the applicable authorities identified as criteria. SAI conducts compliance audits 'to assess whether activities, financial transactions and information comply, in all material respects, with the authorities which govern the audited entity'. The objective of public-sector compliance auditing is to 'assess whether the activities of public-sector entities are in accordance with the authorities governing those entities. This involves reporting on the degree to which the audited entity complies with established criteria. Reporting includes standardized opinions and various forms of conclusions concerned with regularity or adherence to formal criteria such as relevant laws, regulations and agreements or with propriety or observance of the general principles governing sound financial management and the conduct of public officials. Compliance auditing provides

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[4] ISSAI 200/4

[5] ISSAI 400/12/13/14 https://www.audit.gov.bz/wp-content/uploads/2018/06/ ISSAI-400- Fundamental-Principles-of-Compliance-Auditing.pdf

jurisdictional powers to SAI to pronounce judgments and sanctions on those responsible for managing public funds. In Performance Audit, auditor[6] should set audit objective relating to the principles of economy, efficiency and effectiveness. PA follows one of three approaches:

i. "a system-oriented approach, which examines the proper functioning of management systems, e.g., financial management systems;
ii. a result-oriented approach, which assesses whether outcome or output objectives have been achieved as intended or programmes and services are operating as intended;
iii. a problem-oriented approach, which examines, verifies and analyses the causes of particular problems or deviations from criteria."

Public audit – stakeholders' impact survey

Measuring CAG's audit impact requires extensive survey and follow-up mechanisms of its audit reports on programs, projects and service delivery. SAIs can strengthen audit impact in different ways, such as conducting real-time audits; facilitate to take deterrent, detective, remedial and preventive actions against financial irregularities; building effective relationship with legislature and audited entities; adopting international and national benchmarked best practices for enriching audit reports; producing acceptable and practical recommendations; and engaging print, electronic and social media, involving Civil Society Organizations (CSOs)/NGOs and other stakeholders. Formulating efficacious stakeholder communication strategies is indispensable. It helps SAI India in enhancing its audit quality whether audit domain is relating to accounts, compliance, performance related issues, receipt and expenditure, or revenue, profit and loss or project management

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[6] ISSAI 300/25/26

or sustainable development inclusive and equitable governance concerns. Audit of Income tax or Value-Added Tax (VAT), or non-tax receipts, attestation of accounts of Public Sector Enterprises or Autonomous Bodies' or Urban and Rural Local Bodies, project management, or audit of import of crude oil, tax refunds, CAG's audit reports can add enhanced value and benefits to the stakeholders. The parliamentary committees, Public Accounts Committee and Committee on Public Undertakings will find CAG reports more valuable in enforcing parliamentary oversight and budgetary control over the executive. When the government dues like license fee form telecommunication companies, or contractual payments from oil exploration and extraction activities or mining activities, disinvestment or FDI in PSUs, the CAG reports can add more value by purposeful constructive engagement with its stakeholders.

CAG reports have a vital role in holding government entities and entities doing business with government accountable and promoting economy, efficiency and effectiveness. CAG reports help deter misuse and extravagance, assist decision-makers to perform better independent assessments and identify red-flags in public sector entities' functioning. Stakeholders involvement must be encouraged wherever audit impact can be enhanced. Media, CSO's, NGOs and the general public will be more involved CAG audit activities and reporting and will exert public pressure toward implementation of audit recommendations and thereby improve government resource management, add value and benefits to the lives of citizens.

CAG's website for public grievance management and whistle blowing

Grievance management mechanism can be enabled by CAG's website. CSOs, NGOs, citizens, community organizations and all other stakeholders can be allowed to access

the CAG's website and upload their inputs in texts, videos, audios, photos relating to complaints, grievances, corruption and other concerns. When public is able to express their concerns, perspectives and inputs. by using social media, electronic, print media and mobile apps etc.; they will increasingly be involved in CAG's audit activities, process, audit reports, recommendations, follow up and advocacy. The website can also enable hotline services sharing confidential information which may enable the public to help in whistleblowing activities. Ensuring confidentiality and safeguarding the identity of the whistleblower as required under the applicable laws are indispensable. The stakeholders including CSOs, NGOs, community leaders, employees of PSUs, Autonomous Bodies, Urban and Rural Local Bodies' and citizens must be able to access the public domain of the CAG's website and use them for grievance redressal. They should be able to find out the status of action taken on their complaints and the progress on them. The grievance redressal mechanism must ensure redressal of grievances within a reasonable time frame. The status of examination/resolution of the problems as the case may be shall be accessible on the website. The entire process can be monitored, reviewed by CAG office. CAG's website can enable uploading and sharing of various documents/evidence/inputs in text, audio, video, mobile apps, social media, emails, photo, documents in Word, Excel and other digital formats. Apps etc. The stakeholder engagement strategy then will facilitate CAG office to factor the inputs of the stakeholders in its audit process and activities based on risk assessment and in compliance with the professional standards and Code of Ethics. CAG's website has stopped sharing defense audit reports, but NAO, GAO, European Court of Audit and other SAIs do so. Published audit reports contain only shareable information and data. Ideally, CAG's audit activities and reports should be disseminated via effective communication policy including making them available in every Indian language including Hindi and English.

Audit reports reflect the other side of the coin of the government functioning. CAG reports must mirror the concerns of the public and address them. Deficit in governances must be addressed with desirable policy interventions as recommendations and solutions to observed implementation lacunae in government policies. Unless and until the contents of the reports are accessible and shared with the stakeholders for whom the public audit reports are produced, the constitutional mandate and legal mandate of the SAI of India as envisaged by the framers of the constitution and the best practices advocated by INTOSAI will not be fully achieved.

HIGH INFANT MORTALITY RATE – SYMPTOM OF POOR STATE CAPACITY

AKSHYA KUMAR PANDA[*] & MANISHA BOTHRA[**]

Many decades have passed by since Indian independence. Thirteen five year plans were executed. Millennium Development Goals, including IMR could not be reached. Yet, it is fashionable in Indian policy establishment to talk of India emerging as a Global Power. Many unabashedly talk of "World Class" facility in few occasions. No doubt India requires positioning itself as a global power, and set up global facilities for its citizens. But such talks have largely remained in the realm of no more than mere talk shows. Authors have modest hopes and do not talk of Indian students securing median ranking in PISA (Global competency Test). The modest focus is on simplest task and discussion is about performance of Indian States in protecting infants. The many children those who did not live to see their first birthday, could have been the like of Sir Jagdish Chandra Bose, had they been alive.

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Notes: views expressed are personal and in no way represent the organisation the authors belonged to.

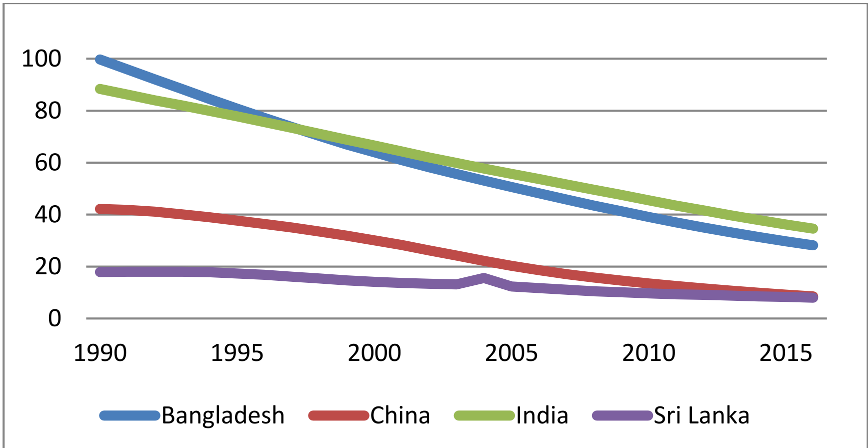
Infant Mortality Rate[1] (IMR) is one of the few crucial indicators to interpret the health status of an economy. Millennium Development Goals (MDGs) therefore focussed on reduction of child mortality[2]. Infant mortality rate along with under 5 mortality rate were identified as the key indicators of child mortality (UN Development Group). As per SRS 2016, the Infant Mortality rate (IMR) in India stood at 34. Clearly, India failed to achieve its MDG target of reducing Infant Mortality Rate to 27 per 1000 live births by 2015. Although, IMR has been reduced from 80 in 1990 to 34 in 2016 (SRS), the figure still remains very high compared to other countries like China, and Sri Lanka whose IMR was reported to be 8.5 and 8 respectively in 2016[3] (World Bank). Bangladesh, though started with an IMR level higher than that of India, has reduced its IMR at a faster rate as shown in Figure 1.

Figure 1: Trends in Infant Mortality Rate in Different Countries

[1] The infant mortality rate is the number of deaths under one year of age occurring among the live births in a given geographical area during a given year, per 1,000 live births occurring among the population of the given geographical area during the same year. (OECD Glossary)

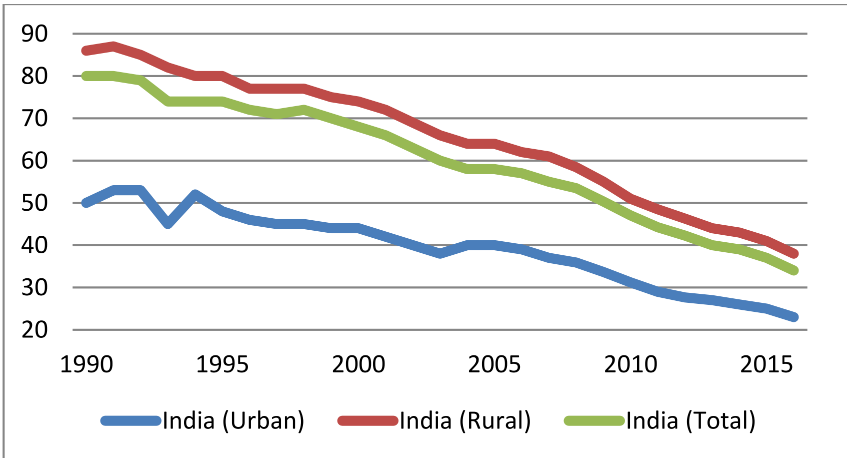
[2] World Health Organisation (WHO), See: http://www.who.int/topics/millennium_development_goals/about/en/

[3] http://data.worldbank.org



Source: World Bank

Figure 2: Rural-Urban Differences in Infant Mortality Rates in India



Source: SRS data, Niti Ayog (Former Planning Commission)

Not only IMR in India, is very high, but also there exists significant differences among Indian states and between rural and urban areas (Figure 2. Rural-Urban gap remained significant for the entire period from 1990 to 2016. The rural rate was 86 compared to 50 in urban areas, in the year 1990. The difference

though has narrowed over the years yet the gap still remains high. Thus even after more than 25 years, the rural-urban gap in IMR remained. Similarly, the state-level differences have also remained very high.

Objective: The present study aims to demonstrate differential performance in managing a simple task such as IMR across geography. While states like Karnataka, Tamil Nadu, and West Bengal have managed to reduce their Infant mortality rate significantly, other states like Odisha, Bihar, and Rajasthan lagged far behind. A simple measure of structural break is adopted to find an explanation for differing performance.

Literature Review: Existing literature attribute IMR outcome to medical and non-medical factors. Sabharwal & Lamba (2014) have found inequalities in access to healthcare as the reason. And conclude that inequalities in IMR outcome will continue till appropriate measures are taken to remove the unequal access to healthcare services. Singh, Pathak, Chauhan, & Pan, 2011 used geo-spatial techniques and concluded that the underendowed geographical locations are more likely to experience worse Infant death outcomes. They have demonstrated that regions having high incidence of child malnutrition, lower female literacy are likely to have higher child death. Mishra (2007) in her study, using data from 118 countries for the period 1973-2004, found statistically significant relationship between health aid and IMR. Similar results were inferred by Rajagopal (2016) particularly for India. Jain (2010), (Chatterjee A, 2011), (Sharma & Bothra, 2017) found non- medical factors in addition to medical factor as significant contributor to regional differences in the infant mortality rates in India. Statistically significant role of female literacy, availability of medical facilities, and vaccination, in reducing the IMR was established.

Krishna et. al. (2016) and Islam (2012) found socio-economic characteristics of households, particularly of the

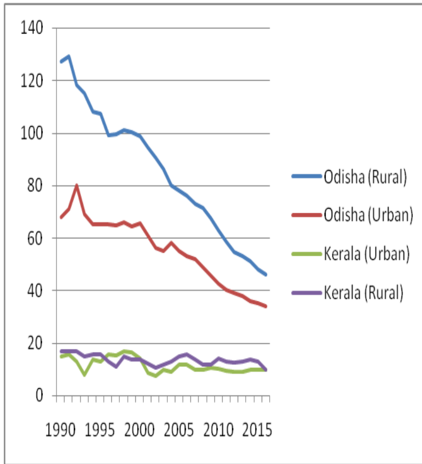
mother, having a strong impact on IMR (Krishna, Shashidhar, & Smitha, 2016) Chatterjee (2011). Among other factors are *low budgetary spending on health, poor nutritional* status of the family. Jamison et. al. (2006) used panel data regression to conclude that higher educational attainment is causally related to declining infant mortality rate in open economies.

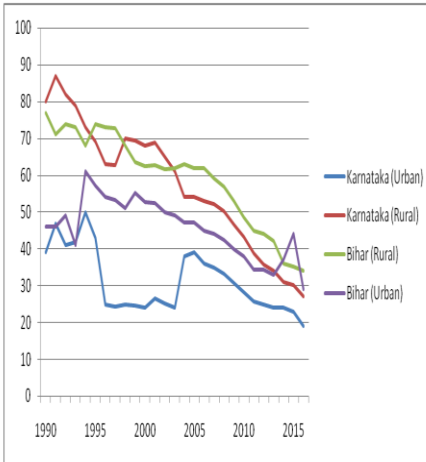
Methodology: In this study, very frugal method is used. The data for Infant Mortality Rate is taken from Sample Registration System, Reserve Bank of India, and Niti Ayog. The data was tabulated and analyzed using Excel and STATA. Zivot-Andrews Unit root test[4] to the pooled data for 1990-2016 is used to test the presence of a structural break in the series and identify the break year. CAGR is used as an aggregate measure to measure the performance of the different Indian states over period of time.

Results: The discussion is divided into four sections. The first section is focused on inter and intra states disparities in IMR. The second section studies the structural break and performance of different states after the break-point. The third section deals with trends in Gender Gaps (Male IMR-Female IMR) and how differences in broader factors like female literacy rate, per capita heath expenditure affect health outcomes. The fourth Section comprises of the conclusion and further research scope.

Figure 3: Rural-Urban Differentials across Selected States of India

[4] Detailed explanation of test is given in the Annexure





Source: SRS, Niti Ayog (Former Planning Commission)

Inferences from the graphs:

- The rate of decline in rural IMR has been very high in Karnataka and slow in Bihar
- The rural-urban differences in IMR continues to be very high in states like Odisha and Bihar, though, in general, the rural-urban gap has been narrowed over the years

- Kerala IMR (lowest; IMR=10) is influenced from its high priority to health care.
- West Bengal shares similar good outcome with Kerala (Fig-4).
- Odisha IMR is, on average, higher than India average but high IMR is prevalent in both rural as well as in urban locations.
- Gender differences in IMR are contrary to natural law of higher survivability of female over male.

The figure-3 shows that IMR in Odisha has, though, reduced over the years has remained consistently high. While Odisha's urban IMR is 34 in 2016, all India average urban IMR stood at 23 in the same year (SRS, Census of India). It is similarly observed with regard to the rural Infant Mortality rate which was 46 and 38 respectively for Odisha and average all India in 2016.

A simple eye ball view does not conceal the persistence of differences among Indian states. Some doing consistently well comparable to best in the world while others consistently lag behind their Indian peers. The question remains whether and when the laggard will experience change. A simple measure of break point test is adopted to see when there is structural break in the tendency among the Indian states. The break test identifies the time when policy intervention made a break to usual.

Figure 4: Break Point Year

Break Point Year (Z-Andrews Test)

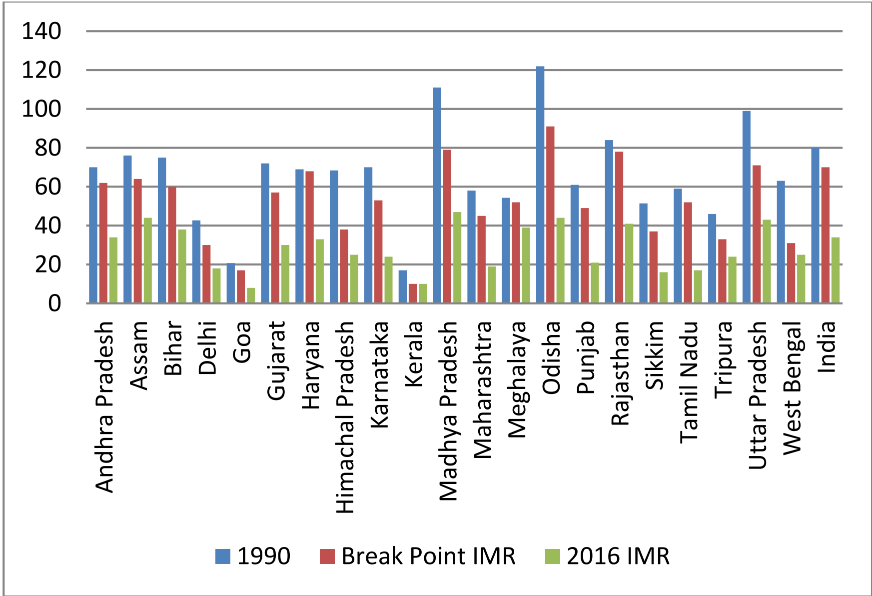
2015
2010
2005
2000
1995
1990
1985

1999

Karnataka
Arunachal Pradesh
Haryana
India
Odisha
Kerala
Tripura
Punjab
Madhya Pradesh
Bihar
Assam
Uttarakhand
West Bengal
Meghalaya

Source: Authors' calculations, SRS data

Figure 5: Infant Mortality Rate, 1990, Break Point, 2016



Source: Authors' calculations, SRS data

It is evident that different states had experienced different break-points and percentage decline, despite having a national policy on health as shown in Figure 4[5]. States like Karnataka, Goa, Tamil Nadu, and Sikkim have achieved their structural break in late 1990s. These states have recorded substantial decline (significant at 5% level) in Infant Mortality Rate, post the breakpoint (Table 1). States like, Odisha, Rajasthan and Uttar Pradesh had witnessed statistically significant structural breaks much later. In these states, though IMR has reduced significantly post the structural break, yet the levels remain high. Understandably so because as laggard political unit failed to step up effort to catch up. Haryana though had her structural break in early 1990s, but reduction in IMR in

[5] See Annexure2 for the Table

subsequent period had not been noteworthy despite the state becoming prosperous.

Figure 4 displays the Break year for different states, Figure 5 compares the infant mortality rate for the year 1990, rate in the structural break year, and figure reported in SRS 2016. Clearly Madhya Pradesh, Odisha, Uttar Pradesh and Rajasthan had the highest IMR in 1990 as compared to other Indian states. The IMR in these states was substantially higher than all India average also. The situation remains unaltered even in 2016.

Figure 5 further shows that Karnataka, and Tamil Nadu have shown substantial decline post the structural break. These states also experienced structural break earlier than many others. Unlike other states, the break point in these states are not a statistically significant. The progression to further lower levels compared to other states appear to signify better control over a simple but vital issue of society. The decline has been over uninterrupted continuum. One better performance reinforcing another leading to a type of cumulative causation.

A combined reading of Fig 4, Fig. 5, Table 1 and Table 2 demonstrate the performance of different Indian States on this simple yet vital issue of the political economy.

- States like Odisha, Uttar Pradesh Rajasthan and Haryana which started with substantially high IMR in 1990 has experienced a break in 2001, 2006, 2002 and 2006 respectively, nearly after a decade.
- Odisha has experienced the most statistically significant break in 2001 noting a decline of more than 50 percent in IMR post the break.
- States like Karnataka and Tamil Nadu which started with low IMR initially have their break points in 1996 and 199

respectively indicating the better performing states continue to observe a continuous decline.

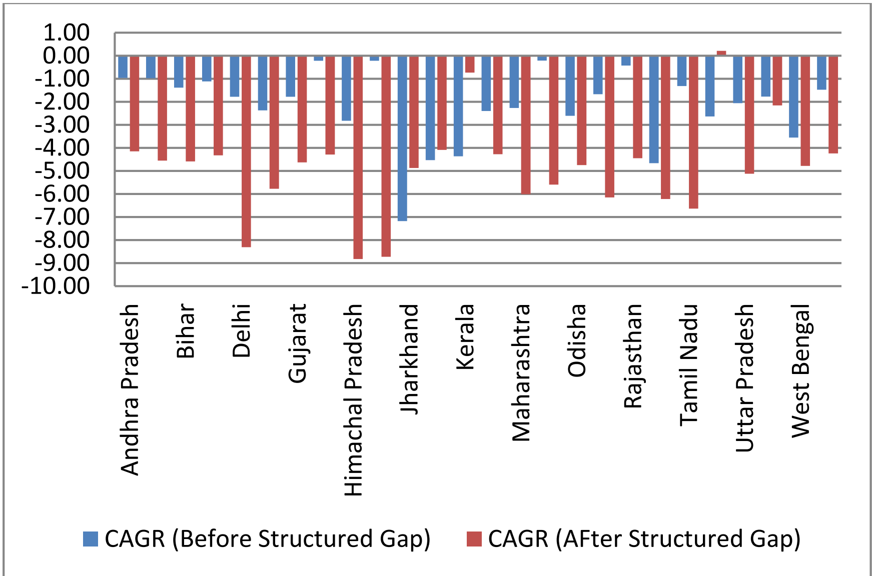
- Decline in IMR is more than 4 percent per year for all the state except Tripura post the structured break. The rate of decline before this period was around 2 percent or lower.

It is undeniable that IMR reduction does not require too much of resources, does not involve higher technology, does not require additional manpower deployment and the mechanism to control is known for a long time. Yet very varying performance among the regional political units. This brings in to sharp focus the concept called Government Effectiveness. What is Government Effectiveness? It is a measure that captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. India’s record on Government effectiveness is discouraging and the varying outcome can be attributed to it.

The states which started with lower IMR had no significant structural break. One common pattern that emerged for majority of Indian states was high rate of decline post the structured break as shown in Figure 6. The other states like Haryana, Karnataka, Maharashtra etc. has witnessed significant decline post the structural break.

The fact remains that reduction in IMR has been faster in post break point than the pre break point (Figure 6).

Figure 6 CAGR Before and After Structured Break

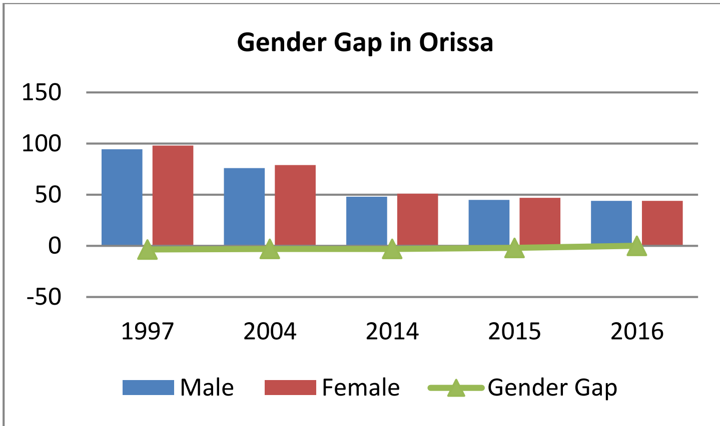


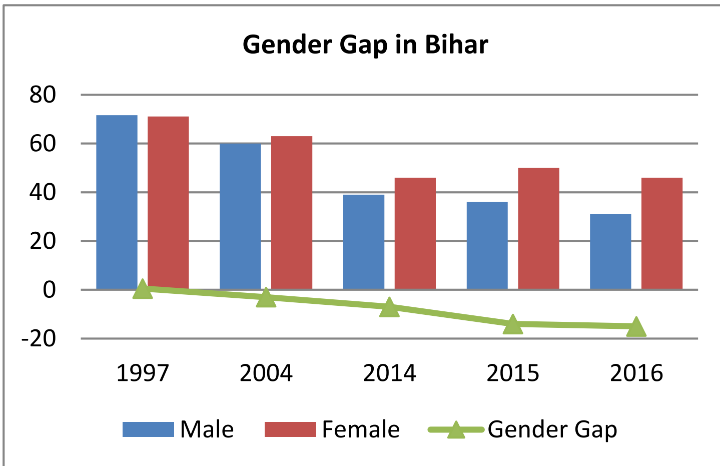
Source: Authors' calculations, SRS data

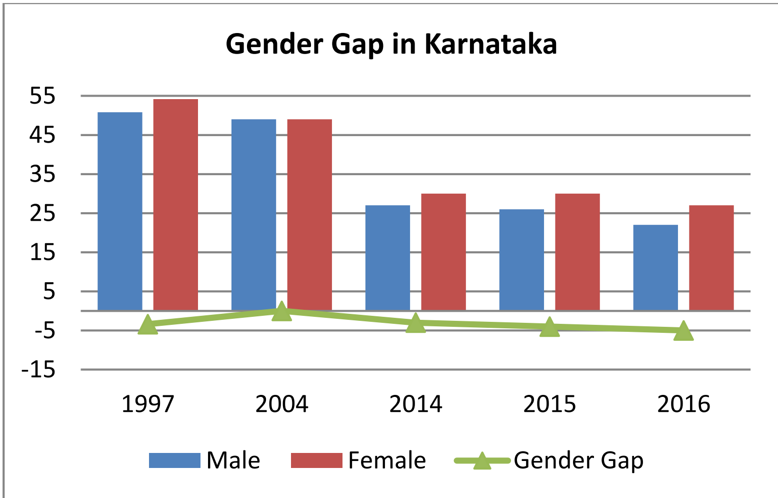
Another interesting finding is with regard to gender-gap in IMR. While for India as a whole IMR has declined from 81 to 39 and 78 to 35 per 1000 live births during 1990 to 2015 for female and male respectively (Millennium Development Goals - Final Country Report of India , 2017), the gender gap still persists and varies significantly across states.

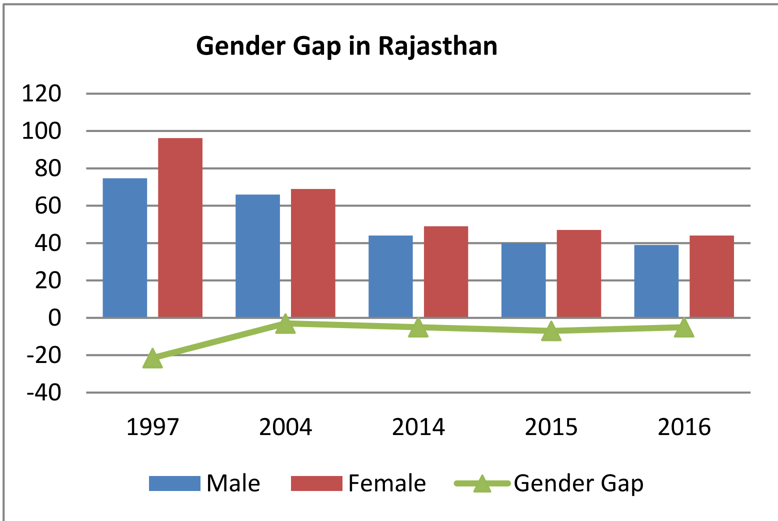
Figure 7 shows the gender gap across selected states in India. The gender gap is very high in states like Haryana, Uttar Pradesh, Rajasthan and Bihar. Surprisingly, the gender gap has increased even in Karnataka over the years while in Odisha there is no gap in male and female Infant Mortality rate (2016).

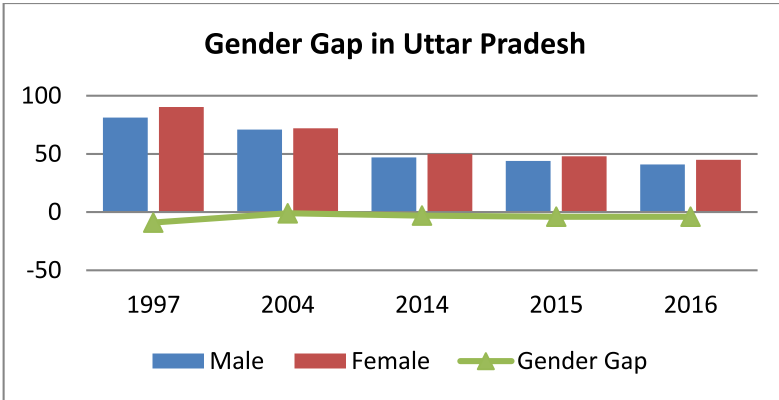
Figure 7: Gender Gap across Selected States in India

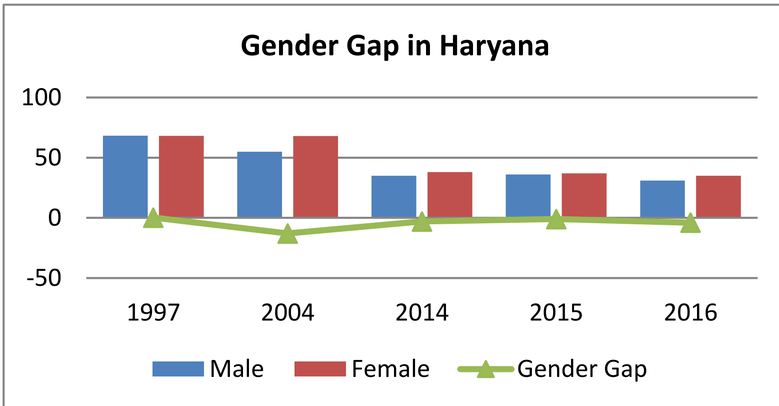

Gender Gap in Orissa
150
100
50
0
-50
1997
2004
2014
2015
2016
Male
Female
Gender Gap


Gender Gap in Bihar
80
60
40
20
0
-20
1997
2004
2014
2015
2016
Male
Female
Gender Gap


Gender Gap in Karnataka
55
45
35
25
15
5
-5
-15
1997
2004
2014
2015
2016
Male
Female
Gender Gap


Gender Gap in Rajasthan
120
100
80
60
40
20
0
-20
-40
1997
2004
2014
2015
2016
Male
Female
Gender Gap





Source: SRS, Gender Gap= Male IMR-Female IMR

Conclusion: The varying IMR outcome across states remained a fact even after several decades of intervention. Some of the major factors influencing IMR outcomes across states are per capita health expenditure, Mother's education, Immunization, Health care infrastructure, Access to sanitation and clean drinking water.[6] Other reasons as noted in nationally representative mortality survey, 2010) are prematurity & low

[6]Apart from the abovementioned factors (Suriyakala, Deepika, Amalendu, & Deepa, 2016) in their study mentioned that in addition to female literacy rate other factors like Fertility rate, national income, women in labor force, expenditure on health care influences infant mortality rate

birth weight, Neonatal Infections, birth asphyxia & birth trauma, pneumonia and diarrhoeal diseases. There has been national level programme on all these thematic areas. Focussed fund transfer has been for long. Finance commission have earmarked specific fund allocation for improvement in health infrastructure. States have been experiencing sufficient cushion and fiscal space after 12th Finance Commission Award. What remains the difference between a good and a bad performer in addressing the simple issue is political influence of the bottom of the pyramid and the state capacity. This remains a further research topic.

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Annexure 1

Zivot-Andrews test was used since it "*identifies endogenously the point of the single most significant structural break in every time series examined*" (Waheed, Alam, & Ghauri, 2006) In order to conduct the test the IMR data for all states was taken from the year 1990 to 2016. The data was converted to time-series. The Zivot-Andrews test was applied to test the presence of a significant structural break.

The Z-Andrews test considers the full sample and creates a different dummy variable for each possible break point. It endogenises one structural break using the following equation:

$$yt = \mu + yt - 1 + \varepsilon t$$

The test uses a different dummy variable for each break point that is possible using following equation (Charles & Mosayeb):

$$y_t = \hat{\mu} + \hat{\theta} DU_t(\hat{T}_b) + \hat{\beta} t + \hat{\gamma} DT_t(\hat{T}_b) + \hat{\alpha} y_{t-1} + \sum_{j=1}^{K} \hat{c}_j \Delta y_{t-j} + \hat{e}$$

The break point is selected where the t-statistics from the test is at its minimum. The critical values are compared with the t-statistics value to test the null hypothesis of no structural break

To verify the presence of structural break the following regression was run where b is estimated break year from Z-Andrews test:

$$y = \{xt\beta, \quad if\ t < b\ x2\ (\beta + \delta), \quad t \geq b$$

The standardized beta coefficients were estimated and the structural break was tested using the following hypothesis:

H0: ™ = 0

HA: ™ ≠ 0

While for some states a structural break appeared at acceptable level of significance, but for some the break was not statistically significant. The data series was non-stationary and was affected by predictability and random changes in the series. There was no structured break point observed at acceptable level of significance by conducting the Z-Andrews test in such series. In order to identify if a structured break exists at an acceptable level of significance, the first level difference was taken. Computing the difference between the consecutive observations is known as differencing.

$$yt' = yt - (yt - 1)$$

The differencing adds the stationary component to the series and makes the results less biased and unaffected by seasonal and cyclical fluctuations in the data. For the IMR series structural break was insignificant majorly for the outperforming states and hence the authors tried to identify whether by making the series difference stationary. The results do indicate an existence of structural break at acceptable level of significance but the break comes at a recent time period indicating an absence of a significant change in IMR.

This could be due to the absence of any significant break and continuum of decline in those states with variations in

particular years. Hence, the authors have used the Z-Andrews test breakpoints for analysis purpose.

Annexure 2

Table 1: 1990 IMR, Structural Break, 2016 IMR and % change before and after structured break

State/UT	1990	% change before structured break	Break Point Year (Z-Andrews Test)	Level of Significance	Break Point IMR	2016 IMR	% change after structured break
Andhra Pradesh	70	-11.43	2002	0.01	62	34	-45.16
Arunachal Pradesh	43	0.00	1999	0.05	43	36	-16.28
Assam	76	-15.79	2008	0.05	64	44	-31.25
Bihar	75	-20.00	2006	Not Significant	60	38	-36.67
Chhattisgarh			2005	Not Significant	63	39	-38.10
Delhi	43	-29.81	2010	Not Significant	30	18	-40.00
Goa	21	-17.97	1999	0.01	17	8	-52.94
Gujarat	72	-20.83	2003	Not Significant	57	30	-47.37
Haryana	69	-1.45	1999	Not Significant	68	33	-51.47
Himachal Pradesh	68	-44.45	2011	0.01	38	25	-34.21
Jammu & Kashmir			2008	Not Significant	49	24	-51.02
Jharkhand			2004	0.01	49	29	-40.82
Karnataka	70	-24.29	1996	Not Significant	53	24	-54.72
Kerala	17	-41.18	2002	Not Significant	10	10	0.00
Madhya Pradesh	111	-28.83	2004	0.05	79	47	-40.51
Maharashtra	58	-22.41	2001	0.05	45	19	-57.78
Manipur	29		No Break	Gap		11	
Meghalaya	54	-4.31	2011	0.05	52	39	-25.00
Mizoram			No Break	Gap		27	
Odisha	122	-25.41	2001	0.01	91	44	-51.65
Punjab	61	-19.67	2003	Not Significant	49	21	-57.14
Rajasthan	84	-7.14	2002	0.1	78	41	-47.44
Sikkim	51	-28.02	1997	0.1	37	16	-56.76
Tamil Nadu	59	-11.86	1999	Not Significant	52	17	-67.31
Telangana			No Break	new state		31	
Tripura	46	-28.25	2002	0.1	33	24	-27.27
Uttar Pradesh	99	-28.28	2006	Not Significant	71	43	-39.44
Uttarakhand			2008	Not Significant	44	38	-13.64
West Bengal	63	-50.79	2010	Not Significant	31	25	-19.35
India	80	-12.50	1999	Not Significant	70	34	-51.43

Source: Authors' Calculations, SRS data

Table 2: State Wise Compound Annual Growth rate (CAGR in %)

State-wise growth rates.

Period		**Pre-Break**	**Post-Break**
1990 to 2016	Break Year	CAGR (in %)	CAGR (in %)
Andhra Pradesh	2002	-0.96	-4.15
Arunachal Pradesh	1999	0.04	-1.25
Assam	2008	-0.98	-4.55
Bihar	2006	-1.38	-4.59
Chhattisgarh	2005	-1.12	-4.33
Delhi	2010	-1.78	-8.31
Goa	1999	-2.37	-5.78
Gujarat	2003	-1.78	-4.63
Haryana	1999	-0.21	-4.29
Himachal Pradesh	2011	-2.82	-8.82
Jammu & Kashmir	2008	-0.22	-8.73
Jharkhand	2004	-7.18	-4.87
Karnataka	1996	-4.53	-4.08
Kerala	2002	-4.36	-0.73
Madhya Pradesh	2004	-2.40	-4.27
Maharashtra	2001	-2.27	-6.01
Meghalaya	2011	-0.21	-5.60
Odisha	2001	-2.61	-4.75
Punjab	2003	-1.67	-6.15
Rajasthan	2002	-0.42	-4.45
Sikkim	1997	-4.66	-6.22
Tamil Nadu	1999	-1.32	-6.64
Tripura	2002	-2.64	0.21
Uttar Pradesh	2006	-2.06	-5.12
Uttarakhand	2008	-1.78	-2.15
West Bengal	2010	-3.55	-4.78
India	**1999**	**-1.47**	**-4.24**

Source: Authors' Calculations, SRS data

AUDIT – A CATALYST OF GOVERNANCE

AJIT PATNAIK*

Audit is a rational and intellectual exercise, and the Indian Audit and Accounts Department is an intellectual tradition, engaged in promoting good governance and accountability as enjoined by the Constitution. Since independence, Audit has evolved in response to the demands of the mandate of the Constitution, reaching different aspects of governance like revenue audit, audit of Public Sector Undertakings, audit of Local Self-Government institutions, and developing new techniques and tools of audit like Performance Audit, Audit of Information Technology, etc. Audit has been a dynamic institution; it has been pro-active, apart from being unfailingly responsive responsibly. It has acted under the strict self-imposed bureaucratic ethics of anonymity; however, its reports have created reverberations in the milieu, by the inherent topicality and investigative explosive potential.

Audit is one point of the anti-deviation triad of governance, whose report cannot by itself achieve a total rectification sweep of cobwebs of governance, but in tandem with the sister agencies –CVC and CBI – forms a powerful weapon to promote probity and good governance. What Audit finds out is a potential base for the other two agencies and the

*Shri Ajit Kumar Patnaik, Former Deputy Comptroller and Auditor General and Chairman, Odisha Public Service Commission.
The Extract from Preface of book, 'Government Audit and Governance' printed as lead article in Virtual Newsletter of Indian Institute of Public Administration Karnataka Regional Branch Vol. 2 No. 1 January 2021.

Courts to take to finality, as has been evidenced in the Audit Reports relating to Bofors Guns of 1989, 2G Telecom Scam of 2009, and Allocation of Coal Blocks of 2012, to mention a few.

Audit has a major role in promoting Good Governance as mandated by the Constitution, recognized by the Apex Court (Arvind Gupta PIL case) and also with its assiduously cultivated attributes of independence, objectivity, and professionalism. Audit employs the approaches of Compliance Audit, Financial Audit, and Performance Audit to find out deficiencies and suggests improvements in governance and accountability. It publishes annually approximately 150 Audit Reports for all layers of government touching every branch and every office to verify and certify to promote good governance.

Auditors are like 'itinerant therapists' who go round the offices looking into their books and reporting the findings, and suggesting measures to improve governance, like Emerson's 'traveling geologist' who passing through an estate, shows good slate, or limestone or anthracite in the estate. He thought the geologist should be welcomed, instead of feeling 'poverty in his presence'; similarly, audit should be welcomed instead of being looked at as unwanted interference. Auditors because of job requirements necessarily have to look and behave like - what Bertrand Russell said about happiness-seekers - billiard balls vis-a-vis auditees. A friendly audit is a contradiction in terms and may invite the ire and suspicion of superiors and behind-the-back scorn of clients. The objective for both - audit and executive - is better governance but the path is of dialectics. *Does an audit make the executive pusillanimous, and decision-averse?* Audit and well-formulated and well-reasoned decisions have common ground and common objectives. The end of audit is the right decision in the right manner on the right base, having each block properly set.

However, Audit carries the burden of promoting good governance, like Atlas. Every year we visit and discover to our

dismay, like Sisyphus, the roll down of the accountability and governance stone which was carried up the year before. We work like Hercules to produce gargantuan Audit Reports to find that reports have remained not presented to the legislature, not discussed or partially discussed in Public Accounts Committees, etc. We have to tell the new entrants to audit in their induction classes to take a dose of Bhagavad Gita– '*karmanye vadhikaraste*' etc. Yours is to audit and acting on that is for the Legislature. Of course, we have had our moments of glory in Audit Reports like Bofors, 2G, Allocation of Coal Blocks, Fodder Scam, etc., when it shook the conscience of the nation.

We may be faulted on assigning value, but when we are factorizing the future into assigning numbers, it cannot have formulaic precision; without values, an audit report will be more a literary paper than an audit report. In any case, while there can be many methods of assigning value, the audit point of unjustified decision-making has to be appreciated. There can be an annual notional small loss of value but it cannot be argued that it should not be projected to the life of the mine on the ground that it will throw up a 1.85 lakh crore figure, part of which would have gone to the government, in case auction had been resorted to. Audit reports and numbers are inseparable. Mr. Anil Swarup in *Not Just A Civil Servant* argues that if there is consensus in Inter-Ministerial Screening Committee meetings, no reason for the decision in the allotment is to be recorded. This rebuttal of audit shows indefensible arguments advanced against audit conclusions. Should there be a vituperative, bilious public criticism of Audit as in Bofors, 2G, and Coal block allocation reports? Mr. Vinod Rai who was the CAG at the time of the Coal Block Report in his book *Not Just an Accountant* feels the criticisms have been unfair, which have not appreciated the audit thrust.

Should Compliance Audit give audit space to Performance Audit on the ground that limited audit resources

should be deployed for review of schemes audit? It is fashionable to cut jokes about narrow audit mentality to object TA bills etc. but as the Gita says "*Gahanna karma no gatih*" (difficult to track is the path of work); it is an impossible job to anticipate the way Chanakya's public functionary will swallow what has reached the tip of his tongue. If it is one of the functions of Audit to prevent fraud and corruption and keep executive exuberance in prescribed limits, Audit has to keep the focus on this core function instead of having what Dr. B.P. Mathur says a platonic approach in his book, '*Government Accountability and Public Audit'*. It may be more appropriate to have a 'Total Audit' approach where there is a suitable mix of Performance Audit and Compliance audit, which, while keeping our focus on scheme audit, also comments on the major irregularities; as has been aptly stated by Tulsi Das in Ram Charit Manas - '*Bin bhay ho nahin priti*' (without fear, no love rises).

To make audit more effective, should CAG be part of Parliament as in the UK as per the National Audit Act 1983? Should we have a new Audit Act bringing in some provisions of *Cour des Comptes* of France, Japan, New Zealand, etc. to empower audit with punitive quasi-judicial powers of the surcharge and to adjudicate in cases of loss of revenue? *Should audit extend to everywhere where government money is spent? But unfortunately, major areas of expenditure like PPP, local self-government, regulatory bodies have been kept out*. Wisdom, faithfulness, and economy of expenditure certification remain incomplete in the present arrangements of Audit. *Can Audit question policy*? The familiar tune of the executive is that Audit is crossing their *Lakshman Rekha* and encroaching on the executive domain of policymaking. Audit may not question policy; but if in policy formulation, appropriate diligence has not been done, e.g., financial implications, and if, in the policy implementation, deficiencies of the policy are found, it will obligate audit to raise the red flag.

CAG is the friend, philosopher, and guide of the Public Accounts Committee and the Committee on Public Undertakings, rendering all assistance in the discharge of their function of discussion of Audit Reports. PAC takes up for discussion selected audit paras for evidence, because of the paucity of time available to it to apportion for audit reports. Should it be made mandatory for the government to present Action Taken Reports on all audit paras to the PAC and the Parliament? Should it be provided that there should be a discussion of the ATR of the government in the Parliament with Chairman, PAC initiating the discussion as is the practice in the UK? *Should we interact with the public through the media to apprise them about audit reports? Does audit have this obligation to the ultimate masters of democracy or stay behind the veils of bureaucratic anonymity? Will it be audit overreach or discharge of duty as per the constitution to contribute to the objective of good governance and enforcement of accountability?* Auditors are engaged, as Bhagwad Gita says in '*lokasangraha*" (welfare of the people) through their audit efforts; their 'labour of love' must not be left unnoticed 'by the people'; the 'gems concealed' with "burning rays' in audit reports in labyrinthine ways of government must be seen by all stakeholders.

The perceived and pronounced gaps which stand in the way of audit realizing its realizable and desirable potential as an engine promoting governance and accountability have led to the necessity for amendments to the CAG DPC Act of 1971. The suggested amendments by the audit and others relate to timely submission of records to audit parties, timely tabling of audit reports, a collegium for choosing CAG on the lines of CVC and bring all PPP projects, Panchayati Raj institutions, and societies with government grants, under the audit jurisdiction of CAG, to mention a few. The need for these amendments is incontestable, but these are gathering dust in governmental shelves. Change for improvement while it may be external in the shape of amendments to the DPC Act, the audit organization has also to be inward-looking to meet the challenges

of evolving times. While it should be uncompromising on the basic principle of functional specialization, it should gear itself up by way of technological up-gradation in both accounts and audit to match up to the executive thrusts of computerization and for timely delivery of audit efforts.

Audit as one of the pillars of the Constitution has been at its job since independence working with Herculean spirit to produce reports on the functioning of government, commenting on areas that needed to be looked into, to ensure financial prudence and probity. Audit has been profusely producing voluminous reports for all layers of government. Had the reports got the attention they deserve from authorities that be, the governmental functioning would have been at a much higher level of efficiency and rectitude, and there would not have been scams, big or small, which the country has witnessed. Audit works in the spirit of Bhagwad Gita - '*yathecchasi tatha kuru'* (act as per your wish; the decision is yours) - audit has given its views, it is for the executive to act and implement. It is more often a case of audit proposes, executive disposes; but the stubborn horse has to decide to drink or not, though waterhole has been shown.

Report of the Comptroller and Auditor-General of India (CAG) on Public Undertakings in Karnataka for the year ended 31st March 2019

THAYYIL SETHUMADHAVAN*

The famous statement attributed to Margaret Thatcher, former Prime Minister of the United Kingdom, that "government has no business to be in business" will come to mind while going through the Report of the CAG on the Public Sector Undertakings (PSUs) of Karnataka for the year 2018-19. The Government of Karnataka (GOK) had 101 functional PSUs and 13 non-functional or dormant PSUs at the end of March, 2019. These PSUs together registered a turnover of Rs.70,599 crores during the year as per their financial accounts which came to 5 per cent of the SGDP, and provided employment to 2.02 lakh employees. They had an accumulated loss of Rs.2,366 crores at the end of the year.

CAG carries out the audit of PSUs under Section 619 of the Indian Companies Act, 1956, read with Sections 139 and 143 of the Companies Act, 2013, as a superimposed audit, over and above the commercial audit carried out by Chartered Accountants, who are selected from a panel maintained by the CAG. CAG also conducts Performance Audits of selected PSUs. In the Report for 2020, CAG has included findings in respect of two such audits, one on the creation of infrastructure, 220 KV and 110 KV substations and transmission lines, by the Karnataka Power Transmission Corporation Limited (KPTCL) and another on the development of state highways through Public Private

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Partnership (PPP) by the Karnataka Road Development Corporation Limited (KRDCL)

The Report was tabled in the State Legislature on 03rd February, 2021. Based on its review of the final accounts of the PSUs, CAG concludes in the Report that the quality of accounts of PSUs is below par and needs improvement.

Total investment of the GOK in the 11 power sector companies (which were subjected to performance audit) came to Rs.55,574 crores. Five of them made profit in 2018-19 (Rs.1,087 crores) while the rest were under loss (Rs.2,929 crores). In the case of 103 PSUs in sectors other than power, total investment including equity and long-term loan assistance was Rs.77,268 crores. Out of 90 non-power sector functional PSUs, 49 earned nominal profits totaling to Rs. 870 crores, while 28 incurred losses totaling to Rs. 1,374 crores. On the whole, the Return on Investment (ROI) was negative during the period 2014 to 2019. As many as 50 functional PSUs were in arrears of 78 accounts starting from 2013-14 onwards.

In the Performance Audit of the transmission infrastructure, CAG observed systemic failures to prepare perspective and rolling plans periodically as required, unplanned creation of infrastructure which led to overloading of substations and sub-optimal utilization elsewhere, among other things. As on 31st March, 2019, there was excess transmission capacity of 5,230 MVA as compared to CEA norms, entailing an avoidable capital burden of Rs.3,870 crores which ultimately impacts the power tariff. CAG also noticed perpetual delays in project implementation, such as delays in approval of designs of substations, failure to identify, during surveys, forest lands and railway projects along the routes, delays in getting statutory clearances, etc. which have been quantified in the Report. The Report also brings out that implementation delays were noticed in 50 out of 53 projects verified in audit with consequential loss of energy savings valued at Rs.556 crores in respect of them.

CAG also found that though the Electricity Supply Companies (ESCOMs) incurred an expenditure of Rs.582 crores (including interest) on implementation of Distribution Transformer Centres' (DTC) metering with recurring annual interest burden, the project did not yield the desired results, since the ESCOMs could not measure the DTC losses accurately due to incomplete consumer mapping of DTCs, poor network communication and software integration; in addition, they had also to pay penalty amounting to Rs.375 crores due to non-achievement of the targeted reduction of distribution losses.

In respect of the performance review on road development through PPP mode, the failure to assess potential traffic accurately led to underutilization. There was also non-adherence to Operation and Maintenance conditions by the concessionaires, absence of monitoring during the pre-project stage of implementation, etc.

The Report is enriched with abundant data by way of Appendices, including details of investments and financial position of individual PSUs, detailed information of the DTCs subjected to audit, observations on operation and maintenance etc., among other things.

The Report will be of interest to those following the performance of PSUs in the State.

Book Review

GOVERNMENT AUDIT AND GOVERNANCE

Edited by

Ajit Patnaik, Nandini Y. Kapdi and **M. Naveen Kumar**

Institute of Public Auditors of India
New Delhi,

D JEEWAN KUMAR

The book under review is a sequel to a seminar on '*Public Audit and Governance'* which was held in August 2019, under the auspices of the Institute of Public Auditors of India. The year 2019 is a landmark in Indian Public Audit; it marks the completion of a century since statutory audit was established by the British Raj, way back in 1919.

The book is divided into four sections dealing with (1) Audit and Governance; (2) Public Finance and Governance; (3) Sectoral Audit and Governance; and (4) A Look at Reforms. There are 20 contributions, in all, penned by competent experts, well-versed in the intricacies of audit and its operative mechanisms.

In a lengthy Preface, the Editor-in-Chief, **Ajit Patnaik** presents an overview of the book, and prepares the reader for what is to follow. According to him, Audit is a rational and intellectual exercise, engaged in promoting good governance and accountability, as enjoined by the Constitution. Audit employs the techniques of Compliance Audit, Financial Audit, and Performance Audit to find out deficiencies; it also suggests improvements in governance and accountability. Although the CAG has generally acted under the strict self-imposed bureaucratic ethics of anonymity, some of its reports did hit the

headlines, as in the Audit Reports relating to Bofors Guns of 1989, 2G Telecom Scam of 2009, and Allocation of Coal Blocks of 2012, to mention a few, all of which did, indeed shake the conscience of the nation.

Consequently, and even otherwise, several questions lurking in the background continue to be in the public domain. *Can audit question policy? Does audit make the executive pusillanimous, and decision-averse? Should the auditor interact with the public through the media to apprise them about audit reports? Does audit have this obligation to the ultimate masters of democracy, or stay behind the veils of bureaucratic anonymity? Will it be audit overreach or discharge of duty as per the Constitution, to contribute to the objectives of good governance and enforcement of accountability?* All these, and several other questions, have been raised and discussed within the covers of this very informative and enlightening book.

Section I, dealing with '**Audit and Governance'**, has contributions by S.P. Jakhanwal, T. Sethumadhavan, Pranab Mukhopadhyay, R.N. Ghosh, Parimal Brahma, Sheela Reddy, T.N. Thakur and K.P. Shashidharan. The second section of the book deals with **Public Finance and Governance**. There are three articles here by B.P. Mathur, Subhash Chandra Pandey and Parag Prakash. The third section of the book deals with **Sectoral Audit and Governance.** There are contributions here by Dhirendra Krishna, Meenakshi Gupta, Sangita Choure, Ajit Patnaik and Nandini Kapdi. **Section IV** of the publication takes **A Look at Reforms.** The contributors here are Mukesh Arya, Govind Bhattacharjee, Sudanshu Mohanty, Himanshu Upadhyaya and Abhishek Punetha.

The book is educative and informative, and would be invaluable to teachers and students of Indian Government and Politics, Public and Financial Administration, and Public Policy, and more particularly, to all those engaged in Policy Formulation and Policy Implementation, apart from audit

personnel themselves. Most of the articles in the book carry a set of recommendations, for improving the present eco-system of Audit and Governance, which leaves much to be desired. As a follow-up of the 2019 seminar and the current publication, the Institute of Public Auditors of India could think of bringing out a set of recommendations, as a separate volume, and open up for public debate and discussion, the much-needed area of reform.

One area where the book falls short is in terms of professional publishing. An academic audit of this book on audit has given scope for the following observations: Articles are not prefaced by Abstracts; there is no uniform system of Footnotes and References; there is no Glossary of Terms which figure in the volume; there is no Index; and there is no ISBN number[28*]. The year of publication is not mentioned. These lapses may appear to be minor in nature, but professional publishers do ensure that books do not fall short on these counts. The Institute of Public Auditors of India may wish to look into these matters too, in future publications.

[28*] Note:- The ISBN obtained

P. SESHKUMAR*

The Institute of Public Auditors of India (IPAI) must be complimented on bringing out a well designed and topical compilation of well researched articles by eminent senior officers mostly drawn up from IAAS, the premier Indian Audit and Accounts Service assisting the Comptroller and Auditor General of India (CAG) in discharging his onerous responsibilities laid down in CAG's (Duties, Powers and Conditions of Service) Act and the Regulations made thereunder.

There are 20 articles written mostly by an array of officers of great repute, who have wide ranging experience and exposure to the functioning of both Central and State Governments at a very senior level (Additional Secretary and Secretary).

Included therein are 3 articles (Public Audit: A Help or Hindrance in Governance? Experience of an Administrator', ‘Inordinate delays in Tabling of CAG' Audit reports in the Legislatures' and ‘Asking for Trouble: The Paradox of IFA Architecture') which are contributed by authors who are not from IAAS—thus imparting a sense of bipartisan flavour to the chosen theme of the compilation: ‘Government Audit and Governance'.

The contributions to Good Governance through the medium of Audit Reports have been brought out eminently well by each author. Almost all imaginable areas of Governance—Panchayat Raj, Statutory Audit, Public sector audit, Revenue audit, Power sector issues, Project Management, Public Debt, Need for revamping Budget Management system, Social audit, Gender Governance, Information Technology Audit and delays

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in tabling CAG's reports in Legislature, in particular, have been examined, studied and issues relevant to and having an impact on Governance have been brought out exceedingly well. Even a lay man can understand and empathize.

It is however, the contributions through well explained articles on Audit report on Allocation of Coal blocks and Allocation of 2G spectrum resources---two seminal contributions by IAAS/CAG, which have explained the rationale behind the audit findings and conclusions in a forceful and effective manner—that stand out because of the impact and some controversy these generated. These deserve to be read by especially those people who have taken to unjustified criticism of the conclusions and reporting by CAG, sometimes even without taking pains to read the reports.

The value of the compilation would have increased manifold for a general but interested reader, if it contained contributions from more officers from the Executive side involved directly in Policy making and implementation, making known their views of how Government Audit could more effectively contribute to Governance.

This would avoid the compilation from being categorized—of which there is a propensity--as essentially an one sided eulogy of Audit efforts and results. The more the efforts of Government Audit in refining their risk assessment processes, matching Auditing standards with International standards, introduction of concepts of credible Peer Reviews of Reports of Government Audit, continuous up gradation of auditing skills and meaningful two way interaction with Audited entities were highlighted, the more would have been the value of the compilation.

Contribution in specific terms of improvements brought out in Statutes, Procedures, Monitoring, MIS, reporting and accountability regime through Government audit interventions

and recommendations (other than 2G and Coal block allocation) would have enabled greater appreciation of efforts towards Good Governance.

Perhaps, IPAI is contemplating to bring out a separate compilation covering these and other significant areas that contribute to transparency and increased accountability within Government Audit. It is hoped that the present compilation is the first of a series of such work, as Government audit has also to continuously improve and refine itself to meet the demands and challenges of Good Governance.

On the whole, the compilation is a great addition to the almost non existent literature on the very significant area of public policy, viz, Government Audit and Good Governance. The publication should find a prominent place in Educational Institutions, Libraries and Central and State Government departments as a valuable reference tool.