Chapter 3
Financial Reporting

A sound internal financial reporting system based on compliance with financial rules is one of the attributes of good governance. This chapter provides an overview and status of compliance of the departments of the State Government with various financial rules, procedures and directives during the current year.

3.1 Non-submission of Utilisation Certificates

Financial Rules stipulate that for the grants provided for specific purposes, Utilisation Certificates (UCs) should be obtained by the departmental officers from the Grantees and, after verification, these should be forwarded to the AG (A&E) within 18 months from the date of their sanction unless specified otherwise. A comparison of pending UCs for the last five years is given in **Table 3.1**. As seen from the table, the position of pending UCs is improving with inter year variations. During 2018-19, due to action initiated by Government, out of 303 UC's awaited for the earlier years, 216 UCs were received. Hence as at the end of 2018-19, 110 UCs aggregating ₹764.81 crore were in arrears which is detailed in **Appendix 3.1**. The status of outstanding UCs is given in **Table 3.2**.

Table 3.1: Comparison of pending UCs for the last five years

Sl. No.	Year	No. of UCs awaited	Amount (₹ in crore)
1	2014-15	182	740.77
2	2015-16	124	487.91
3	2016-17	173	723.94
4	2017-18	303	2,585.26
5	2018-19	110	764.81

Table 3.2: Year-wise arrears of Utilisation Certificates

(₹ in crore)

Due Year	No. of utilisation certificates awaited	Amount
Up to 2016-17	55	195.91
2017-18	32	223.14
2018-19	23	345.76
Total	**110**	**764.81**

Source: Finance Accounts

The majority of cases of non-submission of UCs related to the Medical and Public Health Department (56 *per cent*) and the Urban Development Department (43 *per cent)*. Pendency in submission of UCs not only indicates absence of assurance on utilisation of grants released for intended purposes but also lack of monitoring of utilisation of grants released to the grantees by the department. Pendency in submission of UCs is fraught with the risk of fraud and misappropriation of funds.

Submission of UCs against the amounts drawn should be a budgetary exercise carried out at regular intervals of time.

The Finance Department replied (March 2020) that though there is a remarkable decline in the number of pending utilization certificates, it would issue reminder to all the defaulting departments to submit UCs.

3.2 Non-receipt of information pertaining to institutions substantially financed by the Government

To identify the institutions, which attract audit under Sections 14 and 15 of the CAG's (Duties, Powers and Conditions of Service) Act, 1971, heads of the Government Departments are required to furnish to audit every year information about the institutions to which financial assistance of ₹25 lakh or more was given, the purpose for which assistance was granted and the total expenditure of the institutions.

Ten Departments did not furnish the information pertaining to 484 institutions receiving grants aggregating ₹25 lakh or more for periods ranging from two years to more than 20 years, as detailed in **Appendix 3.2**. As seen from the appendix, the major defaulter was the department of Education.

Instructions were issued by the Finance Department (December 2017) to the Secretaries of Administrative Departments to furnish the required information to the Accountant General directly. However, there was no improvement in compliance.

The Finance Department replied (March 2020) that the departments would be instructed to furnish the necessary information to the AG at the earliest.

3.3 Status of submission of accounts of Autonomous Bodies and placement of Audit Reports before the State Legislature

Several Autonomous Bodies were set up by the State Government in the fields of Village and Small Industries, Urban Development, *etc*. The audit of accounts of 12 autonomous bodies in the State was entrusted to the C&AG under Sections 19 and 20 of the CAG's DPC Act, 1971. These are audited with regard to their transactions, operational activities and accounts, conducting of regulatory/compliance audit, review of internal management and financial control, review of systems and procedures, *etc*.

The status of entrustment of audit, rendering of accounts, issuing of Separate Audit Reports and their placement before the State Legislature is indicated in **Appendix 3.3**.

The accounts for the year 2006-07 were rendered for the first time by the Karnataka Text Book Society.

3.4 Departmental Commercial Undertakings

The departmental undertakings of certain Government Departments performing activities of commercial and quasi-commercial nature are required to prepare proforma accounts in the prescribed format annually, showing the working results of financial operations, so that the Government can assess their working. The finalized accounts of departmentally managed commercial and quasi-commercial undertakings reflect their overall financial health and efficiency in conducting their business. In the absence of timely finalization of accounts, the investment of the Government remains outside the scrutiny of Audit/State Legislature. Consequently, corrective measures, if any, required for ensuring accountability and improving efficiency cannot be taken in time. Besides, the delay renders the system vulnerable to the risk of fraud and leakage of public money.

The Heads of Departments in the Government are to ensure that the undertakings prepare and submit accounts to the Accountant General for audit within a specified time-frame. Out of the nine undertakings, which are closed/transferred/converted into co-operative federations, proforma accounts in respect of two undertakings were due from 1969-70. The position of arrears in preparation of proforma accounts by the undertakings is given in **Appendix 3.4**.

In reply to the audit observation at **Para 3.4** of the report on State Finances for the year ending March 2016, the Finance Department stated (March 2018) that in the meeting held on 18 August 2015, the departments were instructed to continue to furnish proforma accounts to AG and to send comprehensive proposals to Finance Department to close the units.

The Finance Department replied (March 2020) that the departments were instructed to take necessary action to clear the arrears in preparation and submission of proforma accounts.

3.5 Non-receipt of Stores and Stock Accounts

The annual accounts of Stores and Stock are required to be furnished by various departments to Audit by 15 June of the following year. In the case of the Karnataka Public Works, Ports and Inland Water Transport (PWP&IWT), Water Resources and Minor Irrigation Departments half yearly accounts are due to be received by 15 December of the year and 15 June of the following year. Delay in receipt of stores and stock accounts is commented upon in successive Audit Reports.

The position of arrears relating to submission of stores and stock accounts by nine departments involving 164 offices is indicated in **Appendix 3.5**. It was observed that in respect of two cases in Health and Family Welfare Department the accounts are due from more than 10 years (from 2008-09 to 2018-19).

3.6 Abstract Contingent Bills

Under Rule 36 of the Manual of Contingent Expenditure, 1958, the Controlling and Disbursing Officers are authorised to draw sums of money by preparing Abstract Contingent (AC) bills by debiting service heads and are required to present Non-payment Detailed Contingent (NDC) bills (vouchers in support of final expenditure) to the Pr. AG (A&E) through the treasuries before the 15th of the month following the month to which the bill relates. Controlling Officers should also ensure that no amounts are drawn from the treasury unless required for immediate disbursement. Detailed bills aggregating to ₹93.27 crore, drawn on 2,095 AC bills, were pending at the end of March 2019 as detailed in **Table 3.3** and **Table 3.4**.

Table 3.3: Pending AC Bills

(₹ in crore)

	Number	Amount
Opening balance as on 01.04.2018	3,276	84.00
AC bills drawn during the year*	2,286	188.64
Total	5,562	272.64
Submission of NDC bills against pending AC bills	3,467	179.37
Closing balance of Pending AC bills as on 31.03.2019*	**2,095**	**93.27**

Source: Finance Accounts

**excludes bills drawn during March 2019*

Table 3.4: Year-wise pendency of AC Bills

(₹ in crore)

Year	No. of pending AC Bills	Amount
Upto 2016-17	840	26.55
2017-18	648	14.35
2018-19*	607	52.37
Total	**2,095**	**93.27**

Source: Finance Accounts

While 36 *per cent* of the outstanding NDC bills pertain to Elections - Major Head 2015 (₹33.22crore), 36 *per cent* relate to Police - Major Head 2055 (₹32.93 crore) and seven *per cent* relate to Forestry and Wild Life – Major Head 2206 (₹6.80 crore).

The withdrawal of money on an AC bill is accounted for against the functional Major Head in the Consolidated Fund. Unless the accounts are settled within the time allotted, the expenditure stands inflated. Instructions were issued by the Finance Department to all Principal Secretaries/Secretaries to Government (August 2012) for settlement of accounts within the stipulated period, failing which action will be taken to stop the salary of the DDO concerned. However, it was observed in audit that the practice of drawal of salary by DDOs, who had substantial bills pending against them continued, indicating poor compliance with the instructions of the Finance Department.

The PAC in its 5th Report (July 2015) took a serious note on this issue and stated that strict action should be taken for non-submission of NDC bills by the DDOs.

Bills in support of the claim for the amounts drawn on AC Bills should be submitted within the period stipulated in the Manual of Contingent Expenditure.

The Finance Department replied (March 2020) that it would take necessary checks in the ensuing years to clear the bills within the stipulated period.

3.7 Personal Deposit Accounts

The Karnataka Financial Code (KFC) provides for opening of Personal Deposit (PD) accounts with permission from the Government in cases where the ordinary system of accounting is not suitable for transactions. PD accounts created by debit to the Consolidated Fund of the State should be closed at the end of the financial year. However, this rule is not strictly followed in the State as significant balances are carried forward to the subsequent year which are discussed in paragraphs below. Administrators of the accounts should intimate the Treasury Officer about the balance to be transferred to the Consolidated Fund. For continuation of PD accounts beyond the period of their currency, administrators are required to seek the permission of the Finance Department. Periodical reconciliation of PD accounts with treasury accounts is the responsibility of the administrators concerned.

3.7.1 Funds kept in Personal Deposit Accounts

The transactions relating to PD accounts for the period 2014-15 to 2018-19 are detailed in **Table 3.5**.

Table 3.5: Funds in PD accounts

(₹ in crore)

Year	Opening Balance	Receipts/Deposits	Withdrawals	Closing balance
2014-15	2,297.10	3,915.81	3,784.62	2,428.29
2015-16	2,428.29	6,368.39	6,061.07	2,735.61
2016-17	2,735.61	5,516.51	5,310.01	2,942.12
2017-18	2,942.12	4,194.46	4,395.06	2,741.52
2018-19	2,741.52	5,350.98	4,007.36	4,085.14

Source: Finance Accounts

During the year 2018-19, out of ₹5,350.98 crore credited to PD Accounts, ₹1,208.55 crore was transferred to PD accounts during March 2019. Further, as seen from the above table, though the balance in the deposit accounts showed a slight decrease during 2017-18 when compared to 2016-17, it however increased to ₹4,085.14 crore (49 *per cent*) during 2018-19.

The net closing balance in respect of some of the PD accounts of the administrators having high balances is in **Table 3.6**.

Table 3.6: Closing balances in PD Accounts

(₹ in crore)

Sl. No.	Administrators	Amount
1	Personal Deposits - General	555.50
2	PD Accounts of Deputy Commissioners	7,198.33
3	PD Accounts of Director, Department of Scheduled Tribes	409.75
4	PD Accounts of Director, Directorate of Minorities	215.70

Source: DDR Ledger

Non-transfer of unspent balances lying in PD Accounts to Consolidated Fund of the State entails the risk of misuse of public fund, fraud and misappropriation. The PAC has also expressed (January 2012 and July 2015) concern over the high outstanding balances in the PD accounts.

Action is required as per the provisions of the KFC for write back/cleaning up of balances in respect of funds, which have outlived their utility.

The Finance Department replied (March 2020) that though an effort to close 283 inoperative PD Accounts was made in 2016, due to non-reconciliation of balances with the books of Pr. AG (A&E), they could not be closed. Hence, it stated that the departments were requested once again to reconcile PD Accounts balances with that of Pr. AG (A&E) books.

3.7.2 Reconciliation of Personal Deposit Accounts

As per Article 286 of the KFC, the Administrators of PD accounts are required to reconcile cash book balances with reference to the monthly extracts of their accounts as appearing in the treasury records on the fifth of the succeeding month. Information on reconciliation of figures by the Administrators with the treasuries was not available.

As per Article 286A of the KFC, the State Government is required to close all PD accounts remaining inoperative for more than three years. As brought out in Notes to Accounts of Finance Accounts 2019, out of 73 PD Accounts, 21 PD Accounts (with an outstanding credit balance of ₹4.75 crore in 11 PD Accounts and debit balance of ₹1.24 crore in eight PD Accounts and two PD accounts with nil balance) were inoperative (**Appendix 3.6**). Action may be taken by the administrators to analyze and duly reconcile the balance, closure of accounts and write back the transactions to the Consolidated Fund of the State.

3.8 Reconciliation of Receipts and Expenditure

To exercise effective budgetary control over revenue/expenditure and to ensure accuracy in accounts, all Controlling Officers are required to reconcile every month, the receipts and expenditure recorded in their books with the figures accounted for by the Pr. AG (A&E). Reconciliation of receipts was completed for a value of ₹1,64,817.41 crore (99.91 *per cent* of total receipts of ₹1,64,973.15 crore). Reconciliation of expenditure was completed for a value of ₹1,97,933.22 crore (99.48 *per cent* of total expenditure of ₹1,98,959.17 crore). No reconciliation was carried out in respect of receipts (₹31.23 crore) and disbursements (₹4,487.23 crore) under loans and advances. Necessary action for reconciliation in respect of receipts and expenditure under loans and advances is required to be taken.

The Finance Department while accepting the recommendation (March 2020) stated that action to ensure reconciliation of receipts and expenditure of loans and advances would be taken.

3.9 Comments on Accounts

3.9.1 Erroneous procedure adopted for refund of Sales Tax to eligible industries

As per Paragraph 2.2 under General Instructions contained in the Compilation of List of Major Heads and Minor Heads(LMMH), ‘Refunds of Revenue’ shall, as a general rule, be taken in reduction of the revenue receipts. (Code 900- ‘Deduct-Refunds’). In respect of major/sub-major heads falling under the sector “A Tax Revenue”, the head ‘Deduct-Refunds’ should be opened as a distinct sub-head below the appropriate minor heads so that the net collection of each tax/duty is readily ascertainable from the accounts. In addition, Rule 301(4) of GFR also states refund of revenue are not to be regarded as expenditure.

During the year 2018-19, an expenditure of ₹299.46 crore was incurred under the head of account 2852-80-103-0-01 – ‘Refund of Sales Tax’ towards re-imbursement of VAT/Works Contract Tax/CST/Entry tax to eligible industries (Toyota Industries, TVS Motor Company, BEML, Toyota Kirloskar Auto Parts

Pvt. Ltd. *etc*.) who were eligible for special incentives and concessions and had paid the aforesaid taxes for the earlier period.

Since it was refund of revenue (Sales Tax), as per the instructions contained in LMMH stated above, the amount should have been reimbursed through executive order by following the normal procedure for refund of tax. Taking expenditure route for re-imbursement had resulted in overstatement of expenditure to an extent of ₹299.46 crore. Further it also had an effect on fiscal indicators like revenue surplus.

In reply, the department stated (May 2019) that the refund was not of excess tax paid by eligible industries but refund of tax paid as per special package of incentives provided under various policies of Government to promote investments in the State. The reply of the department is not acceptable as the issue relates to the wrong procedure adopted for refund by following the expenditure route through Legislature approval.

Subsequent to the Exit Conference, the Finance Department stated (March 2020) that the amount is given as incentive to the eligible industries. Hence, an erratum has been issued for the financial year 2019-20. In the budget 2020-21, the nomenclature of the detailed head has been indicated as 'Incentive to eligible industries' instead of 'Refund of revenue'.

3.9.2 Unnecessary provision for conversion of loan into grant

According to Rule 103 of General Financial Rules, which the State Government would generally follow in the absence of specific provisions for conversion of Loans into Equity in its rule books, a token provision would suffice for the purpose of such conversion. In such cases, the accounting adjustment is made by correcting the balances under loans/equity proforma without bringing the transactions into the current year's books.

A mention was made in the State Finance Audit Report for the year ending March 2018, wherein a comment on conversion of loans into equity was brought out. During the year 2018-19 also, it was noticed that under Grant 09 – Co-operation, a provision of ₹8.28 crore was made under HOA 2425-00-108-0-75-100 – Financial Assistance/Relief for conversion of soft loan given to rejuvenate the Indian Coffee Marketing Co-operative Ltd., (COMARK), Hassan, into a one-time grant. Since, it was a case of conversion of loan into grant-in-aid carried out through a book adjustment, the full provision of ₹8.28 crore made instead of a token provision was contrary to the principle of budgeting.

3.9.3 Non remittance of unspent amount to Government Account

The Government accorded (October 2014) administrative approval for construction of two new wards and four additional rooms in the Government Dental College and Research Institute(Institute), Bengaluru at an estimated cost of ₹2.25 crore and released the funds between 2015-16 to 2017-18 to the Institute. The work was entrusted (November 2014) to PWP&IWTD as a Deposit Contribution work and ₹1.99 crore was released to PWP&IWTD by the Institute during 2015-16 and 2016-17. The work was completed (September 2017) at a cost of ₹1.65 crore and the balance amount of ₹0.34 crore was refunded (November 2018) to the Institute by the PWP&IWTD. Further, during 2017-18, ₹0.26 crore was released (December 2017) to the Institute which was deposited in the savings bank account of the Institute. Thus, as of May 2019, the Institute had an unutilised amount of ₹0.60 crore in its bank account which is yet to be remitted to the Government Account.

The Institute replied that after obtaining approval from the department concerned, action would be taken to utilize the balance amount. The reply of the Institute is not acceptable as the funds released by the Government is meant for a specific purpose, the unutilized amount was required to be remitted to Government Account. Non-refund of unutilised amount resulted in Government money (₹0.60 crore) being kept outside Government Account.

The Finance Department replied (March 2020) that efforts will be made to recover the unutilized amount deposited in the savings bank account. It further stated that needful corrective measures would be taken to ensure proper utilization of the funds in the coming years.

3.10 Important factors affecting accuracy of accounts

The accounts of the Government are kept on cash basis. In case of certain transactions that arise in the Government Account, for which the receipts and payments cannot at once be taken to a final head of receipt or expenditure owing to lack of information as to the nature or for any other reasons, these are to be booked temporarily under the suspense head. This head is cleared on receipt of relevant details/information.

Debt, Deposit and Remittances (DDR) are heads of account for such transactions where the Government, as a custodian of public money, receives and holds such money in trust.

The accuracy of the State Finance Accounts 2018-19 was adversely affected by factors like (i) large number of transactions under suspense heads awaiting final classification and (ii) increasing number and magnitude of adverse balances under DDR heads. On a general review of the transactions, the following were observed:

a) Outstanding balances under major suspense accounts

Certain intermediary/adjusting heads of accounts known as ‘Suspense Heads’ are operated in Government accounts to reflect transactions of receipts and payments, which cannot be booked to a final head of account due to lack of information as to their nature, or for other reasons. These heads of accounts are finally cleared by minus debit or minus credit when the amounts under them are booked to their respective final heads of accounts. If these amounts remain un-cleared, the balances under the suspense heads would accumulate and would not reflect the Government’s receipts and expenditure accurately. The balances under certain major suspense heads of accounts, as recorded in the ledger maintained by Pr. AG (A&E), are indicated in **Table 3.7**.

Table 3.7: Suspense Head (8658 – Suspense Accounts)

(₹ in crore)

Name of the Minor Head	2016-17		2017-18		2018-19	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
101-Pay and Accounts Office Suspense	118.86	0.45	189.66	0.25	288.08	16.93
Net	Dr.118.41		Dr.189.41		Dr. 271.15	
102-Suspense Account (Civil)	17.22	60.78	17.37	175.77	17.76	296.45
Net	Cr.43.56		Cr.158.40		Cr.278.69	
110-Reserve Bank Suspense	41.02	148.41	44.53	151.18	91.41	183.28
Net	Cr.107.39		Cr.106.65		Cr.91.87	

Source: Finance Accounts (Vol. I)

The Finance Accounts reflect the net balances under these heads. The outstanding balances are worked out by aggregating the outstanding debit and credit separately. The implications of the balances under these heads are discussed in the succeeding paragraphs:

❖ **Pay and Accounts Office (PAO) Suspense**

This head is intended for settlement of transactions between the Accountant General and the various separate Pay and Accounts Officers of GoI. The transactions initially recorded under this head in the books of the AG are cleared on receipt of the Cheque/Demand Drafts from the Pay and Accounts Officer and on the issue of Cheque/Demand Draft in respect of amounts received in the State Treasuries on behalf of the Pay and Accounts Officer. Outstanding debit balance under this head would mean that payments were made by the AG on behalf of a PAO, which were yet to be recovered. Outstanding credit balance would mean that payments have been received by the AG on behalf of a PAO, which were yet to be paid. The net debit balance under this head showed an increasing trend. On clearance/settlement of this, the cash balance of the State Government will increase. The transactions mainly related to National Highways, and payments made by the State Government to Central Government Civil Pensioners.

❖ **Suspense Account (Civil)**

Transactions where full particulars of the classification are not available, or where the relevant vouchers/schedules in support thereof are not available or where there is some discrepancy between the figures reported in the Treasury Schedules of payment/cash accounts and those appearing in the supporting vouchers, schedules, *etc*. constitute the major portion of outstanding under this head.

Transactions taking place at State Treasuries on behalf of Railways, Defence and Posta l& Telegraph are also initially classified under this head, pending settlement of claims by these authorities.

The net credit balance under this head increased by ₹120.29 crore during the year. In so far as accounts with Railways (₹3.15 crore) and accounts with Defence (₹1.20 crore) are concerned, the cash balance will increase on clearance. There is no impact on cash balance in respect of the rest.

❖ **Reserve Bank Suspense, Central Accounts Office**

This head is operated for recording inter-governmental transactions where monetary settlement between the cash balances of two Governments is done by sending advice to the Central Accounts Section of the Reserve Bank of India. This head is cleared by transferring the amount to the final head of account on receipt of intimation of the monetary settlement having been carried out by the RBI. The main transactions, which get settled through this suspense head are grants/loans received from the Government of India and their repayments, discharge of securities and interest paid thereon by the Public Debt offices of RBI, and payments made by the Director General of Supplies and Disposals for materials supplied to Government Departments.

During 2018-19, the credit balance under this head was ₹91.87 crore, and has come down by ₹14.78 crore compared to previous year.

b) Adverse Balances under DDR Heads

Adverse balances are negative balances appearing under those heads of accounts, where there should not be a negative balance. For example, against the accounting head of any loan or advance, a negative balance will indicate more repayment than the original amount advanced. As revealed by Finance Accounts for the year 2018-19, adverse balance of E- Public Debt amounting to ₹174.40 crore (Major Head 6003-Internal Debt- debit) was on account of credits of the direct release of loans by National Co-operative Development Corporation (NCDC) to loanee entities without routing these loans through the Consolidated Fund of the State, while repayments are made through the Consolidated Fund.

The adverse balance of ₹11.69 crore - debit (Major Head 6004- Loans and Advances from Central Government) was on account of write-off of Central Loans on the recommendations of XIII FC (balances outstanding as per books of accounts as on 31 March 2010). The excess payments made during 2010-12 to various PAOs are to be adjusted against the dues of the Finance Ministry, GoI.

In respect of loans and advances, the adverse balance was ₹96.74 crore, which was on account of non-reconciliation/misclassification in accounts.

3.11 Conclusion

In spite of the Finance Department issuing instructions to Administrative Departments to furnish information to audit about the Institutions which were substantially financed by the Government, 10 Departments had not furnished information in respect of its 484 Institutions. At least one SAR issued for each of the 12 ABs was yet to be placed before the Legislature. Though delay in respect of Stores and Stock Accounts is being commented upon in successive audit reports, the delay continued to persist.

Although the action initiated by the Government has resulted in clearance of AC Bills which were pending for long periods, NDC bills against 25 *per cent* of the AC bills drawn during 2018-19 were found wanting. The closing balance in the PD Accounts showed an increasing trend from 2014-15 to 2018-19.

During 2018-19, the closing balance in the PD accounts increased by 49 *per cent* when compared to the previous year and was at ₹4,085.14 crore. Hence, large sums of money were being retained which was against the principle of Legislative financial control. There were adverse balances in certain DDR heads which required remedial action for clearance.

3.12 Recommendations

- ***The Government should ensure adjustment of Abstract Contingent Bills within the stipulated period.***
- ***Cleaning up of balances in the PD Accounts which have outlived their utility needs to be examined and steps need to be taken for review of the status of PD accounts and closure of inoperative ones after reconciliation of balances and in consultation with the Administrators and Treasury;***
- ***Review of suspense heads needs to be done to bring the transactions to final heads in the accounting year itself.***

Bengaluru
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