

# Chapter-1

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## **Overview of Finances of Local Bodies and their Accounting Arrangements**

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## 1.1 Finances of Local Bodies

### 1.1.1 Fund flow

Resource base of PRIs and ULBs consists of own revenue generated by collection of tax<sup>1</sup> and non-tax<sup>2</sup> revenues, devolution at the instance of State and Central Finance Commissions, Central and State Government grants for maintenance and development purposes and other receipts<sup>3</sup>. The authorities responsible for reporting the use of funds in respect of Zilla Praja Parishads (ZPPs), Mandal Praja Parishads (MPPs) and Gram Panchayats (GPs) are the Chief Executive Officer (CEO), Mandal Parishad Development Officer (MPDO) and Panchayat Secretary respectively. The Commissioner concerned is responsible in case of Corporations and Municipalities.

### 1.1.2 Sources and application of funds (PRIs)

#### 1.1.2.1 Sources of funds

Summary of receipts of PRIs during 2009-14 is given below:

**Table 1.1**

(₹ in crore)

S. No.	Receipts	2009-10	2010-11	2011-12	2012-13	2013-14
1	Own Revenue	928.33	955.77	1009.24	976.50	736.50
2	Assigned Revenue <sup>4</sup>	311.69	262.39	344.02	154.36	457.24
3	State Government grants	930.16	797.05	1185.85	343.97	350.59
4	GoI Grants					
	BRGF <sup>5</sup>	3070.50	2245.85	1913.90	1083.15	325.62
	12 <sup>th</sup> and 13 <sup>th</sup> Finance Commission	491.31	393.52	428.29	117.88	1005.24
5	Other Receipts	341.40	362.45	331.68	84.18	Nil
	<b>Total</b>	<b>6073.39</b>	<b>5017.03</b>	<b>5212.98</b>	<b>2760.04</b>	<b>2875.19</b>

Source: Commissioner, Panchayat Raj

It can be seen from **Table 1.1**, that there was marginal increase in total receipts of PRIs during 2013-14 compared to the previous year. While own revenue and BRGF grants from GoI declined during the year, grants under recommendations of the 12<sup>th</sup> and 13<sup>th</sup> Finance Commissions increased substantially during the year.

#### 1.1.2.2 Application of funds

Details of expenditure incurred by PRIs during 2009-14 are given in Table 1.2.

<sup>1</sup> House tax, advertisement fee etc.,

<sup>2</sup> Water tax, rents from markets, shops and other properties, auction proceeds etc.,

<sup>3</sup> Donations, interest on deposits etc.,

<sup>4</sup> Seigniorage fee and surcharge on stamp duty collected by Departments of Mines and Geology and Stamps and Registration are apportioned to Local Bodies in the form of assigned revenue

<sup>5</sup> Backward Region Grant Fund

**Table 1.2**

(₹ in crore)

S.No.	Type of expenditure	2009-10	2010-11	2011-12	2012-13	2013-14
1	Revenue expenditure	3054.78	3314.82	2968.66	1405.50	3562.39
2	Capital expenditure	1648.92	1545.82	1464.15	1033.47	1756.98
	<b>Total</b>	<b>4703.70</b>	<b>4860.64</b>	<b>4432.81</b>	<b>2438.97</b>	<b>5319.37</b>

Source: Data furnished by Commissioner, Panchayat Raj

As seen from **Table 1.2**, the revenue expenditure 2013-14 increased by more than 150 per cent over the previous year and more than made up for the decrease effected in 2012-13. Similarly, the capital expenditure of 2012-13 was also less than 29 per cent as compared to 2011-12 and increased by 70 per cent in 2013-14 as compared to 2012-13.

### 1.1.3 Sources and application of funds (ULBs)

#### 1.1.3.1 Sources of funds

Summary of receipts of ULBs during 2009-14 is given below:

**Table 1.3**

(₹ in crore)

S.No.	Receipts	2009-10	2010-11	2011-12	2012-13	2013-14
1	<b>Own Revenue</b>	1809.72	2013.74	2297.17	2898.52	3183.43
2	<b>Assigned Revenue<sup>6</sup></b>	377.80	684.00	795.70	819.28	695.66
3	<b>State Government grants</b>	350.00	430.00	608.00	921.00	1358.60 <sup>7</sup>
4	<b>GoI grants</b>					
	Scheme funds	1093.40	734.27	704.24	378.36	-
	12 <sup>th</sup> and 13 <sup>th</sup> Finance Commission	74.80	177.78	111.85	Nil	-
5	<b>Other Receipts</b>	Nil	Nil	Nil	Nil	275.60*
	<b>Total</b>	<b>3705.72</b>	<b>4039.79</b>	<b>4516.96</b>	<b>5017.16</b>	<b>5513.29</b>

Source: Data furnished by Commissioner and Director of Municipal Administration and Commissioner, GHMC

Note: \*other receipts include loans, accrued interest, penalties received, forfeited security deposits, contributions etc.

As seen from **Table 1.3**, there was decline in assigned revenue during 2013-14 in a reversal of the increasing trend seen in earlier years. Also, the break-up of grants (₹1,358.60 crore) received during 2013-14 from GoI and State Governments were not furnished by the Commissioners concerned separately.

#### 1.1.3.2 Application of funds

Details of expenditure incurred by ULBs during 2009-14 are given in Table 1.4.

<sup>6</sup> Seigniorage fee and surcharge on stamp duty collected by Departments of Mines and Geology and Stamps and Registration are apportioned to the Local Bodies in the form of assigned revenue

<sup>7</sup> This includes grants received from GoI

Table 1.4

(₹ in crore)

S.No.	Type of expenditure	2009-10	2010-11	2011-12	2012-13	2013-14
1	Revenue expenditure	2181.79	2621.40	2941.85	3153.33	3418.10
2	Capital expenditure	1313.38	1399.83	1253.08	1166.59	1573.30
	<b>Total</b>	<b>3495.17</b>	<b>4021.23</b>	<b>4194.93</b>	<b>4319.92</b>	<b>4991.40</b>

Source: Data furnished by Commissioner and Director of Municipal Administration

It can be seen from **Table 1.4** that the capital expenditure increased by 35 per cent in 2013-14 compared to 2012-13.

## 1.2 Devolution of Funds and Functions

Eleventh Schedule to 73<sup>rd</sup> Constitutional Amendment Act, 1992 listed 29 subjects for devolution to strengthen the PRIs. During 2007-08, State Government devolved 10<sup>8</sup> functions to PRIs and thereafter no initiative was taken for devolving the remaining functions. Funds relating to devolved functions are being released to PRIs through line departments concerned. As per the information furnished (November 2014) by the Government, only five departments released funds amounting to ₹28.67 crore to PRIs in eighteen districts<sup>9</sup> during 2012-14 (**Appendix-1.1**). While PRIs of all these eighteen districts (except Rangareddy) received funds from Fisheries department, releases by the four departments were only partial.

The 74<sup>th</sup> Constitutional Amendment Act, 1992 identified 18 functions for ULBs as incorporated in 12<sup>th</sup> Schedule to the Constitution. Except '**Fire Services**', all the functions mentioned in this Schedule were devolved to ULBs in the State.

## 1.3 Accounting arrangements

PRIs maintain accounts on cash basis. Model accounting system was prescribed by GoI in consultation with the Comptroller and Auditor General of India. State Government issued orders (September 2010) for adopting this format using PRIASoft, i.e., Panchayat Raj Institutions Accounting Software developed by National Informatics Centre (NIC). Government confirmed (September 2014) that online accounting was completed in all the PRIs (22 ZPPs, 1,096 MPPs and 21,567 GPs).

However, test check (2013-14) of accounts of 94 GPs using PRIASoft revealed that while 18 GPs were not implementing the system as of September 2014 mainly due to lack of computers/computer operators, in respect of 18 other GPs, there were discrepancies between PRIASoft generated accounts and manually prepared accounts for the years 2011-12 and 2012-13 (accounts of 2013-14 were yet to be finalised).

<sup>8</sup> (i) Agriculture (ii) Animal Husbandry (iii) Fisheries (iv) Rural Development (v) Drinking Water and Sanitation (vi) Primary, Secondary and Adult Education (vii) Health, Sanitation, Primary Health Centres, Dispensaries and Family Welfare (viii) Social Welfare (ix) Backward Classes Welfare (x) Women and Child Development.

<sup>9</sup> Adilabad, Anantapur, Chittoor, Guntur, Karimnagar, Khammam, Kurnool, Mahbubnagar, Medak, Nalgonda, Nellore, Nizamabad, Prakasam, Rangareddy, Visakhapatnam, Vizianagaram, Warangal and West Godavari Districts.

As regards ULBs, GoI in consultation with the Comptroller and Auditor General of India, had formulated (December 2004) National Municipal Accounts Manual (NMAM) with double entry system for greater transparency and control over finances and requested (May 2005) States to adopt it with appropriate modifications to meet the State's specific requirements. Accordingly, a Steering Committee was constituted (May 2005) by State Government and Andhra Pradesh Municipal Accounts Manual (APMAM) was developed during 2006-07. State Government issued orders in August 2007 for adoption of APMAM in all the ULBs in State. Similarly, other manuals viz., Andhra Pradesh Municipal Budget Manual and Andhra Pradesh Municipal Asset Manual, were also accepted by State for implementation (August 2007) by ULBs. Though double entry book keeping system is being followed in all the ULBs, scrutiny of records of two (Khammam and Palamaneru Municipalities) out of eight ULBs test-checked during 2013-14 revealed the following:

- i. Schedule of assets did not depict the value of flyovers, bridges, subways constructed in municipality.
- ii. Taxes were not being accounted on accrual basis.
- iii. No schedule for depreciation was maintained.
- iv. Prepaid expenses were not booked despite payment of insurance for vehicles covering the future period.
- v. There were discrepancies between the data uploaded online and physical records.

## **1.4 Audit Mandate**

### **1.4.1 Statutory Audit**

Director, State Audit (DSA) functioning under the administrative control of Finance Department, is the statutory auditor for PRIs and ULBs under Andhra Pradesh State Audit Act, 1989. As per Section 11(2) of the Act, DSA is required to prepare a Consolidated State Audit and Review Report and present it to the State Legislature. The DSA has six Regional Offices, 22 District Offices and Sub/Resident offices of districts to conduct audit of all the PRIs and ULBs annually.

#### **1.4.1.1 Arrears in audit**

Certification of accounts gives an assurance that funds have been utilised for the purpose for which these have been authorised. However, as per the information furnished (December 2014) by DSA, audit of 220 accounts of ULBs was pending as the accounts were yet to be compiled by the ULBs. In case of GPs, audit of 5,613 accounts were in arrears as of December 2014. DSA attributed non-production of records by GPs for delay in audit of accounts of these GPs.

#### **1.4.1.2 Submission of Consolidated State Audit and Review Reports**

DSA has prepared and submitted Consolidated State Audit and Review Reports up to the year 2010-11 to Finance department and the Government tabled (February 2014)

the Report in the State Legislature. While the consolidation of Report for 2011-12 was completed and translation into vernacular language (Telugu) was in progress, it was yet to be taken up for the years 2012-13 and 2013-14. Some of the major findings relate to excess utilisation / non-utilisation / diversion / mis-utilisation of grants, non-collection of dues, advances pending adjustments, violation of rules, wasteful expenditure etc.

#### ***1.4.1.3 Issue of surcharge certificates***

As per Section 10 of the Act, DSA is empowered to initiate surcharge proceedings against the persons responsible for causing loss to the funds of local authorities or other authorities and such amounts are to be recovered by the executive authority concerned under Revenue Recovery (RR) Act. As of March 2014, there were 71,348 cases where surcharge certificates were issued to PRIs (71,034 cases) and ULBs (314 cases), but the requisite amount was not recovered. The amount involved in this regard is ₹92.71 crore.

### **1.4.2 Audit by CAG**

CAG conducts audit of Local Bodies (PRIs and ULBs) under Section 14 of CAG's (DPC) Act, 1971. Based on the recommendations of the Eleventh Finance Commission, State Government entrusted (August 2004) the responsibility for providing Technical Guidance and Supervision (TGS) in connection with the accounts and audit of Local Bodies under Section 20(1) of CAG's (DPC) Act.

CAG conducts only a test check and provides a consolidated report (TGS Note) at the end of each financial year to the DSA for improving the quality of their reports. TGS note for the year 2013-14 was issued in December 2014.

#### ***1.4.2.1 Planning and conduct of audit***

Audit process commences with assessment of risk of department/local body/scheme/programme etc., based on expenditure incurred, criticality/complexity of activities, priority accorded for the activity by Government, level of delegated financial powers and assessment of internal controls and concerns of stakeholders. Previous audit findings are also considered in this exercise. Based on this risk assessment, frequency and extent of audit is decided and an annual audit plan is formulated to conduct audit. During 2013-14, 293 PRIs (274 GPs and 19 Mandal Praja Parishads) and eight ULBs (five Municipalities and three Municipal Corporations) falling under the departments of Panchayat Raj and Rural Development and Municipal Administration and Urban Development were subjected to performance and compliance audit.

#### ***1.4.2.2 Response of departments to Audit findings***

After completion of audit, Inspection Reports (IRs) containing audit findings are issued to head of the unit concerned. Heads of offices and next higher authorities are required to respond to observations contained in IRs within one month and take appropriate corrective action. Audit observations communicated in IRs are also

discussed in meetings at district level by officers of the departments with officers of Principal Accountant General's office.

As of December 2014, 530 IRs containing 6,567 paragraphs pertaining to the period up to 2013-14 were pending settlement as detailed in **Table 1.5**. Of these, first replies have not been received in respect of 144 IRs and 3,009 paragraphs.

**Table 1.5**

Year	Number of IRs/Paragraphs				IRs/Paragraphs where even first replies have not been received			
	IRs		Paragraphs		IRs		Paragraphs	
	PRIs	ULBs	PRIs	ULBs	PRIs	ULBs	PRIs	ULBs
Up to 2009-10	270	103	1896	2023	22	52	223	1045
2010-11	88	14	694	405	20	10	199	253
2011-12	9	3	101	53	1	1	9	26
2012-13	0	35	0	1125	0	33	0	1077
2013-14	1	7	12	258	1	4	12	165
<b>Total</b>	<b>368</b>	<b>162</b>	<b>2703</b>	<b>3864</b>	<b>44</b>	<b>100</b>	<b>443</b>	<b>2566</b>

## 1.5 Financial Reporting

Best practices in matters relating to different elements of financial reporting like drawal of funds, form of bills, incurring of expenditure, maintenance of accounts, rendering of accounts by PRIs and ULBs (Municipal Corporations and Municipalities) are governed by the provisions of APPR Act, 1994, HMC Act, 1955 and Andhra Pradesh Municipalities Act, 1965 respectively, rules framed by State Government from time to time, Andhra Pradesh Treasury Code, Financial Code, Public Works Accounts Code, Public Works Departmental Code, Stores Manual, Budget Manual, other Departmental Manuals, standing orders and instructions.

Significant issues relating to financial reporting by PRIs and ULBs during 2013-14 are detailed below.

### 1.5.1 Creation of database of PRIs

State Government released (2002-10) Eleventh and Twelfth Finance Commission grants amounting to ₹57.80 crore<sup>10</sup> to Commissioner Panchayat Raj and Rural Employment (CPR&RE) for creation of database on finances of PRIs. CPR&RE kept these funds (₹67.37 crore including interest) in fixed deposits and flexi savings accounts with various banks. In addition to these funds, ₹2.27 crore received<sup>11</sup> from GoI under ePanchayat programme for creation of database was also parked in bank accounts.

<sup>10</sup> Eleventh Finance Commission grants ₹22.96 crore (2002-04) and Twelfth Finance Commission grants ₹34.84 crore (2005-10)

<sup>11</sup> Dates of receipt were not made available to audit



Of these funds, CPR&RE released ₹34.05 crore to Andhra Pradesh Technological Services (APTS) in January 2014 towards purchase of computers and ₹3.45 crore to Bharat Sanchar Nigam Limited (BSNL) (April 2014) towards annual fixation charges for broad band connections. As of December 2014, Andhra Pradesh had received ₹19.64 crore for developing ePanchayat database which was lying in bank accounts of Commissionerate.

Thus database was not created despite provision of funds by the GoI and thereby the objective of consolidating finances of PRIs remained unachieved for more than 13 years.

### 1.5.2 Advances pending adjustment

As per Andhra Pradesh Financial Code-1, advances paid should be adjusted without any delay and the DDOs concerned should watch their adjustment. Scrutiny of records of eight ULBs during 2013-14 revealed that in five ULBs, funds amounting to ₹47.66 lakh advanced to staff for various purposes during 2006 - 2013 remained unadjusted as of September 2014.

### 1.5.3 Cases of misappropriation

Andhra Pradesh Financial Code stipulates responsibilities of Government servants in dealing with Government money, procedure for fixing responsibility for any loss sustained by Government and action to be initiated for recovery. State Government ordered (February 2004) the Secretaries of all the departments to review the cases of misappropriation in their departments on a monthly basis and the Chief Secretary to Government to review these cases once in six months with all the Secretaries concerned.

Misappropriation cases in PRIs and ULBs noticed by Director, State Audit during 2011-12 to 2013-14 yet to be disposed off at the end of December 2014 are given in Table 1.6.

Table 1.6

(₹ in lakh)

Unit	2011-12		2012-13		2013-14	
	No. of cases	Amount	No. of cases	Amount	No. of cases	Amount
<b>Panchayat Raj Institutions</b>						
Zilla Praja Parishads	1	0.18	26	108.08	3	4.82
Mandal Praja Parishads	20	32.78	39	38.85	21	12.79
Gram Panchayats	9344	559.39	1272	195.51	307	192.06
<b>Urban Local Bodies</b>						
Municipal Corporations	0	0	8	117.91	45	68.09
Municipalities	76	125.06	152	350.87	61	391.63
<b>Total</b>	<b>9441</b>	<b>717.41</b>	<b>1497</b>	<b>811.22</b>	<b>437</b>	<b>669.39</b>

Source: Information furnished by Director, State Audit

Urgent action needs to be taken by the Government in this regard.

#### **1.5.4 Physical verification of stores and stock**

Article 143 of Andhra Pradesh Financial Code Volume I stipulates that all stores and stock should be verified physically once a year and a certificate to this effect be recorded by the Head of the Office in the Register concerned. Scrutiny of records of 94 GPs during 2013-14 revealed that annual physical verification of stock and stores was not being conducted in any of these GPs.

#### **1.5.5 Non-reconciliation of departmental figures with treasury**

As per paragraph 19.6 of Andhra Pradesh Budget Manual, Drawing and Disbursing Officers (DDOs) are required to reconcile departmental receipts and expenditure with those booked in treasury every month to avoid any misclassification and fraudulent draws. Scrutiny of records of 94 GPs during 2013-14 revealed that in respect of 50 GPs (53 per cent), reconciliation was pending for two to three years.

#### **1.5.6 Preparation of budgets by GPs**

As per Section 77 of Andhra Pradesh Panchayat Raj Act, 1994, the budget proposals containing detailed estimates of income and expenditure (with explanatory notes for each head of account) for the ensuing year are to be prepared every year by executive authority (Panchayat Secretary) and this draft budget is discussed in GP (elected members) before submission to Divisional Panchayat Officer (DLPO) on or before 25 December. DLPO shall make such suggestions, as he may deem fit and return the Budget to GP within one month. Later the GP considers the same and approve the budget with or without modifications which is final. If the budget is not prepared and placed before GP, the executive authority is liable for action as per Para 4 (b) of Andhra Pradesh Gram Panchayat, Preparation and Submission of Budget Rules, 2000.

Scrutiny of the records of 94 GPs test-checked during 2013-14 revealed that in respect of 10 of these, budgets were not prepared for the period covered in audit (2010-13) and 16 GPs prepared for one or two years. In the absence of approved budgets, authenticity for incurring expenditure by these GPs during 2010-13 could not be verified in audit.

#### **1.5.7 Non-finalisation of accounts**

According to Rule 4 of Andhra Pradesh Municipalities (Preparation and Submission of Accounts and Abstracts) Act, 1970, ULBs are to compile their Accounts annually and forward a copy to Audit not later than 15 June. While there were arrears of more than two decades in compilation of accounts by Gudur Municipality, in respect of Greater Hyderabad Municipal Corporation (GHMC), Greater Visakhapatnam Municipal Corporation (GVMC) and Kadapa Corporation, they were more than a decade. Unit wise details of pendency in compilation of accounts are given in *Appendix-1.2*.

#### **1.5.8 Non-conducting of inspections**

As per Section 44(2)(a)(b) of Andhra Pradesh Panchayat Raj Act, 1994 the Government should appoint District Panchayat Officer, Divisional Panchayat Officer

and Extension Officers as Inspecting Officers for overseeing the operations of Gram Panchayat (GP). Test-check of the records of 94 GPs revealed that in respect of 19 of these (20 *per cent*) inspections were not conducted by any of the above authorities, while no inspection reports were found in support of inspections conducted by the authorities concerned in 23 GPs.

## **1.6 Conclusion**

As can be seen from the above paragraphs, out of 29 functions listed in Eleventh Schedule to 73<sup>rd</sup> Constitutional Amendment Act, 1992, Government devolved PRIs only functions relating to 10 subjects. Model accounting system (PRIA Soft) adopted by State Government is yet to be implemented by many GPs. Also, the database of finances was not created even after lapse of 13 years of releasing the funds. As regards ULBs, there were delays in compilation of accounts, with consequent delay in their audit by DSA.

Financial reporting in test-checked PRIs/ULBs during 2013-14 was inadequate as evidenced by non-adjustment of advances, non-preparation of budget, non-finalisation of accounts, non-conducting of physical verification of stores and stock, and non-reconciliation of departmental figures with treasury etc.