

CHAPTER I

FINANCES OF THE STATE GOVERNMENT

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Profile of Tamil Nadu

Tamil Nadu is one of the most urbanised States in India. Tamil Nadu has a total of 32 districts. As indicated in **Appendix 1.1**, in the last ten years, the density of population in Tamil Nadu has increased from 480 persons per sq.km to 555 persons per sq.km. Tamil Nadu has lower poverty levels as compared to the all-India average. The State has shown marginally higher economic growth in the past decade as the compound annual growth rate of its Gross State Domestic Product (GSDP) for the period 2001-02 to 2010-11 has been 15.55 *per cent* as compared to 15.02 *per cent* in the general category states. During this period, its population grew by 15.60 *per cent* against 17.56 *per cent* in the general category states. The per capita income compound annual growth rate in Tamil Nadu (12.27 *per cent*) has been higher amongst the general category states (11.62 *per cent*) in the current decade. Also, per capita GSDP income/contribution during 2010-11 was slightly higher as compared to the general category states average. Tamil Nadu has lower urban inequality, but higher rural inequality as compared to all India average.

1.1 Introduction

This chapter provides a broad perspective of the finances of the Government of Tamil Nadu during the current year and analyses critical changes in the major fiscal aggregates relative to the previous year, keeping in view the overall trends during the last five years.

Some of the Acts and Rules which regulate the receipts of the State Government are the Tamil Nadu Value Added Tax Act, 2006, Tamil Nadu Motor Vehicles Act, 1974, Tamil Nadu Prohibition Act, 1937, Medicinal and Toilet Preparations (Excise Duty) Act, 1955, Indian Stamp Act, 1899 and the Registration Act, 1908.

All receipts of the Government of Tamil Nadu are accounted for in the Consolidated Fund of the State constituted under Article 266 (1) of the Constitution of India. Expenditure therefrom is authorised by the State Legislature through Appropriation Act. Money so authorised by the Appropriation Act is spent as per provisions contained in the Tamil Nadu Financial Code Vol. I and Tamil Nadu Financial Code Vol. II and instructions issued by the Finance Department from time to time. The Tamil Nadu Financial Code contains the financial regulations of general nature issued by the Finance Department for the guidance of various offices and departments.

Apart from the above, the Government of Tamil Nadu enacted the Tamil Nadu Fiscal Responsibility Act, 2003 (FRBM Act) to ensure long-term financial stability by achieving revenue surplus, containing fiscal deficit and prudential debt management. Subsequently, the Government of Tamil Nadu enacted the Tamil Nadu Fiscal Responsibility (Amendment) Act, 2010 and fixed the timeframe for achieving the fiscal targets set in 2003. The salient features of the FRBM Act, 2003 (as amended upto December 2010) are given in **Appendix 1.3 – Part B**.

The structure of Government Accounts and the layout of the Finance Accounts are shown in **Appendix 1.2**. The methodology adopted for assessment of the fiscal position of the State is given in **Appendix 1.3**. A time series data on the State Government finances is given in **Appendix 1.4**.

1.1.1 Summary of Current Year's Fiscal Transactions

Table 1.1 presents the summary of the State Government's fiscal transactions during the current year (2010-11) *vis-à-vis* the previous year. **Appendix 1.5** provides details of receipts and disbursements as well as the overall fiscal position during the current year.

Table 1.1: Summary of Current Year's Fiscal Operations

(₹ in crore)

2009-10	Receipts	2010-11	2009-10	Disbursements	2010-11		
Section-A: Revenue					Non Plan	Plan	Total
55,844	Revenue receipts	70,188	59,375	Revenue expenditure	58,649	14,267	72,916
36,547	Tax revenue	47,782	20,297	General Services	25,896	28	25,924
5,027	Non-tax revenue	4,652	22,957	Social Services	17,651	11,258	28,909
8,756	Share of Union Taxes/ Duties	10,914	12,122	Economic Services	9,749	2,473	12,222
5,514	Grants from Government of India	6,840	3,999	Grants-in-aid and Contributions	5,353	508	5,861
Section-B: Capital							
..	Misc. Capital Receipts	..	8,573	Capital Outlay	217	12,219	12,436
2,587	Recoveries of Loans and Advances	770	2,290	Loans and Advances disbursed	1,960	292	2,252
15,557	Public Debt receipts	14,492	2,512	Repayment of Public Debt	*	*	3,297
1	Contingency Fund	..	..	Contingency Fund	*	*	30
87,275	Public Account receipts	1,06,700	85,256	Public Account disbursements	*	*	1,04,959
16,229	Opening Cash Balance	19,487	19,487	Closing Cash Balance	*	*	15,747
1,77,493	Total	2,11,637	1,77,493	Total			2,11,637

(Source: Finance Accounts for the years 2009-10 and 2010-11)

* Bifurcation of Plan and Non- Plan not available

The significant changes during 2010-11 as compared to the previous year are given below:

- Revenue receipts of the State increased by ₹ 14,344 crore (25.69 *per cent*) over the previous year. This was mainly due to increase in the State's own tax revenue (₹ 11,235 crore), share of Union Taxes/Duties (₹ 2,158 crore) and grants from Government of India (₹ 1,326 crore). There were minor decreases in non-tax revenue (₹ 375 crore).
- Revenue expenditure increased by ₹ 13,541 crore (22.81 *per cent*) over the previous year, mainly due to increase in expenditure on General Services (₹ 5,627 crore) and Social Services (₹ 5,952 crore) and Grants-in-aid and contributions (₹ 1,862 crore).
- While the expenditure on General Services and Social Services registered an increase of 27.72 *per cent* and 25.93 *per cent* respectively, expenditure on Economic Services registered a marginal increase of 0.82 *per cent* only.
- Capital expenditure increased by ₹ 3,863 crore (45.06 *per cent*) over the previous year and Repayment of Public Debt increased by ₹ 785 crore (31.25 *per cent*). The rise in capital expenditure was mainly on Water Supply and Sanitation, Housing, Nutrition, Rural Development Projects, Flood Control Projects, Power Projects, Road Transport sector and Public Works.
- Recoveries of loans and advances decreased by ₹ 1,817 crore (70.24 *per cent*) over the previous year mainly due to decreases in recoveries under "Loans for food storage and warehousing" and "Loans for Power Projects", which was partly offset by increase in recoveries under "Other loans to Industries and Minerals".
- Public Account receipts and disbursements increased by ₹ 19,425 crore (22.26 *per cent*) and ₹ 19,703 crore (23.11 *per cent*) respectively. Net receipts under Public Account decreased by ₹ 278 crore over the previous year.
- The net impact of these transactions led to a significant decrease of ₹ 3,740 crore in the cash balance at the end of the year over the previous year.

1.1.2 Review of the fiscal situation

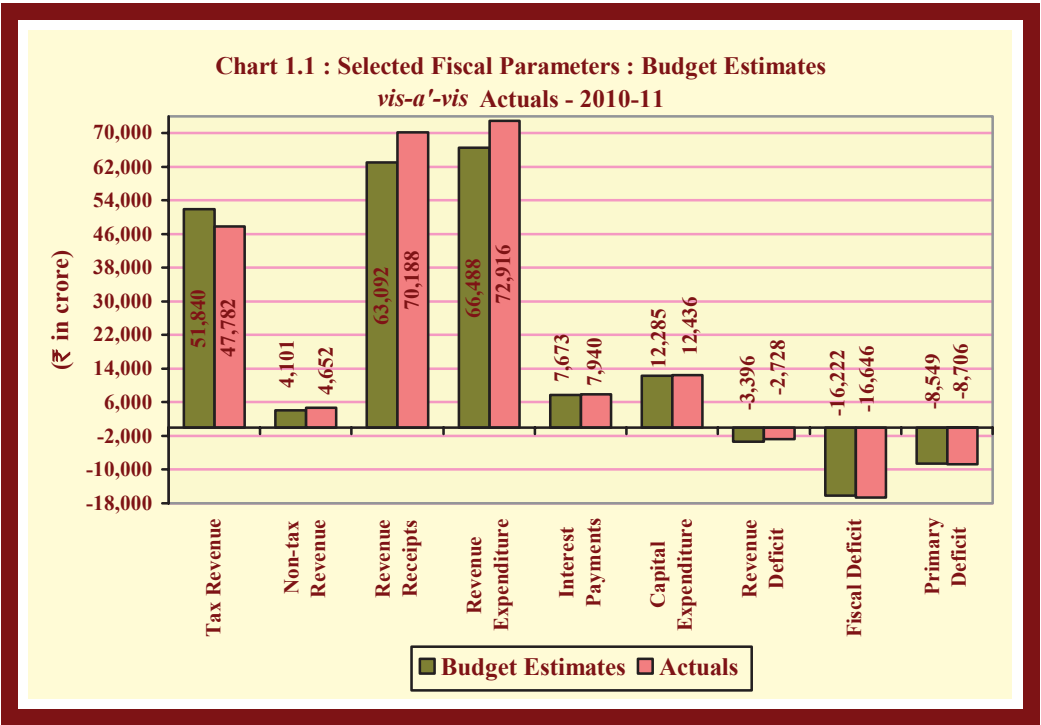
The State Government had enacted the Tamil Nadu Fiscal Responsibility Act, 2003 (FRBM Act) to ensure long-term financial stability by achieving revenue surplus, containing fiscal deficit and prudential debt management. In compliance of this Act, the State Government had prepared a Medium Term Fiscal Plan (MTFP) with the projections for the period 2010-13. In line with the recommendation of the Thirteenth Finance Commission (TFC) and as per MTFP, the State has to eliminate the revenue deficit by the end of 2011-12 and contain the fiscal deficit as a percentage of Gross State Domestic Product (GSDP) within three *per cent* by 2011-12.

Though the State was able to achieve revenue surplus till 2008-09, from 2009-10 onwards the State was experiencing revenue deficit. The revenue deficit of the State was ₹ 2,728 crore (0.50 per cent of GSDP) during 2010-11.

1.1.3 Budget Analysis

The budget papers presented by the State Government provide descriptions of projections or estimations of revenue and expenditure for a particular fiscal year. The importance of accuracy in the estimation of revenue and expenditure is widely accepted in the context of effective implementation of fiscal policies for overall economic management. Deviations from the Budget Estimates are indicative of non-attainment and non-optimisation of the desired fiscal objectives, due to a variety of causes, some within the control of the Government and some outside.

Chart 1.1 presents the budget estimates and actuals for some important fiscal parameter in 2010-11.



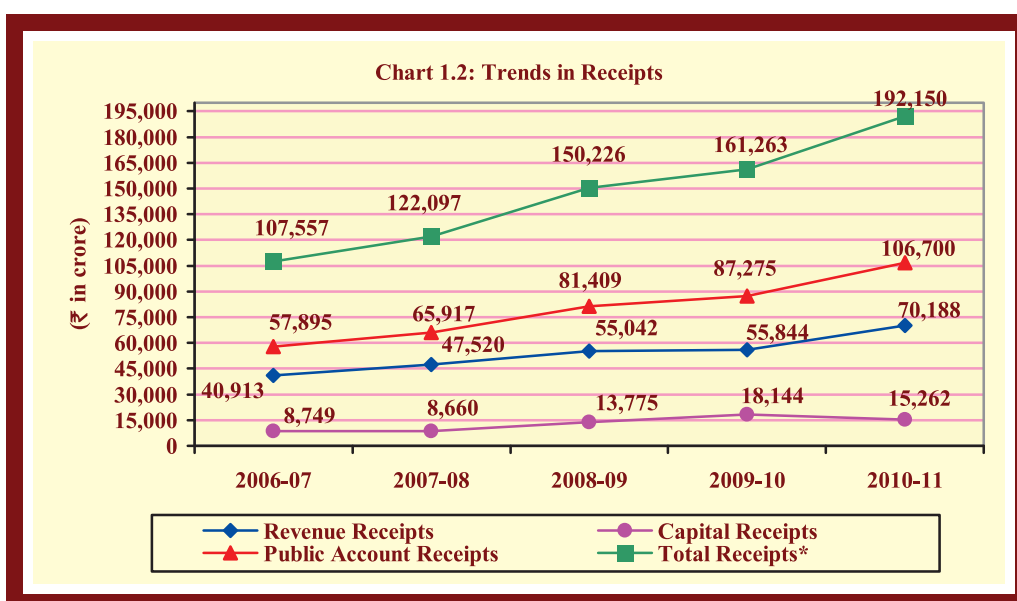
The actuals were fairly in line with the estimates, barring the following:

- Tax revenue fell short of the estimates by 7.83 per cent.
- Non-tax receipts surpassed the estimates by 13.44 per cent.
- Revenue receipts were more than the estimates by ₹ 7,096 crore (11.25 per cent) and revenue expenditure was more than the estimates by ₹ 6,428 crore (9.67 per cent).

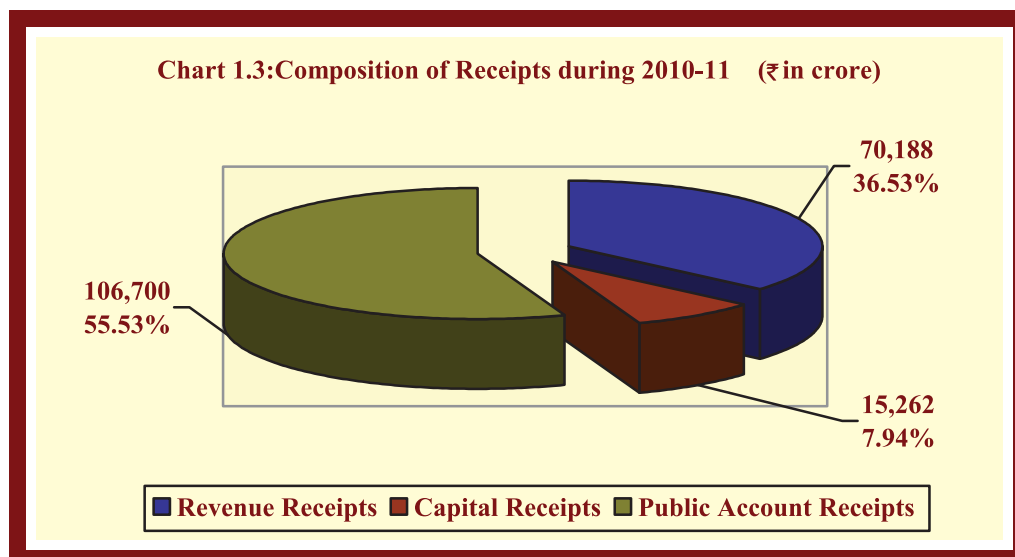
1.2 Resources of the State

1.2.1 Resources of the State as per the Annual Finance Accounts

Revenue and capital are the two streams of receipts that constitute the resources of the State Government. Revenue receipts consist of tax revenues, non-tax revenues, State's share of Union taxes and duties and grants-in-aid from the Government of India (GOI). Capital receipts comprise miscellaneous capital receipts such as proceeds from disinvestments, recoveries of loans and advances, debt receipts from internal sources (market loans, borrowings from financial institutions/commercial banks) and loans and advances from GOI as well as accruals from the Public Account. **Table 1.1** presents the receipts and disbursements of the State during the current year as recorded in its Annual Finance Accounts, while **Chart 1.2** depicts the trends in various components of the receipts of the State during 2006-11. **Chart 1.3** depicts the composition of resources of the State during the current year.



* Excludes receipt under Contingency Fund



- The total receipts of the State Government for the year 2010-11 were ₹ 1,92,150 crore. Of these revenue receipts were ₹ 70,188 crore constituting 36.53 *per cent* of the total receipts. The capital and public account receipts constituted 7.94 *per cent* and 55.53 *per cent* of the total receipts respectively.
- The total resources of the State increased by ₹ 30,887 crore (19.15 *per cent*) over the previous year, mainly due to increase of ₹ 19,425 crore (22.26 *per cent*) in Public Account receipts and ₹ 14,344 crore (25.69 *per cent*) in revenue receipts.
- The capital receipts decreased by ₹ 2,882 crore, a decrease of 15.88 *per cent* over the previous year. This was mainly due to decrease in Public Debt receipts by ₹ 1,065 crore, a decrease of 6.85 *per cent* over the previous year, mainly due to a substantial decrease in open market borrowings and also due to decrease in recoveries of loans and advances by ₹ 1,817 crore, a decrease of 70.24 *per cent* over the previous year.
- The State's tax revenue increased from ₹ 36,547 crore in 2009-10 to ₹ 47,782 crore in 2010-11 (increase of 30.74 *per cent*), while the percentage of tax receipts to revenue receipts increased only by 2.64 *per cent* i.e., from 65.44 *per cent* in 2009-10 to 68.08 *per cent* in 2010-11.

1.2.2 Funds transferred to State Implementing Agencies outside the State Budgets

The Central Government has been transferring a sizeable quantum of funds directly to State implementing agencies¹ for the implementation of various schemes/programmes in social and economic sectors which are recognised as critical. As these funds are not routed through the State Budget/State Treasury System, the Annual Finance Accounts do not capture the flow of these funds and to that extent, the State's receipts and expenditure as well as other fiscal parameters derived from them are underestimated. The funds directly transferred to State implementing agencies under eight major programmes assisted by Government of India are presented in **Table 1.2**.

¹ State implementing agencies include any organization/institution including Non-Governmental organisation which is authorized by the State Government to receive funds from the Government of India for implementing specific programmes in the State.

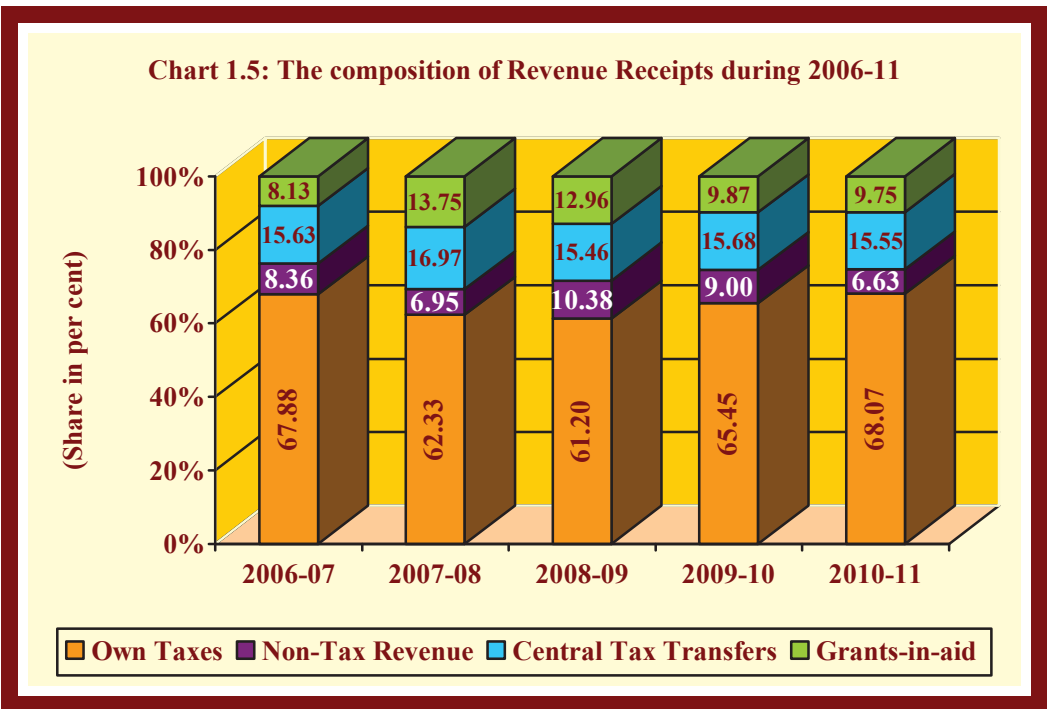
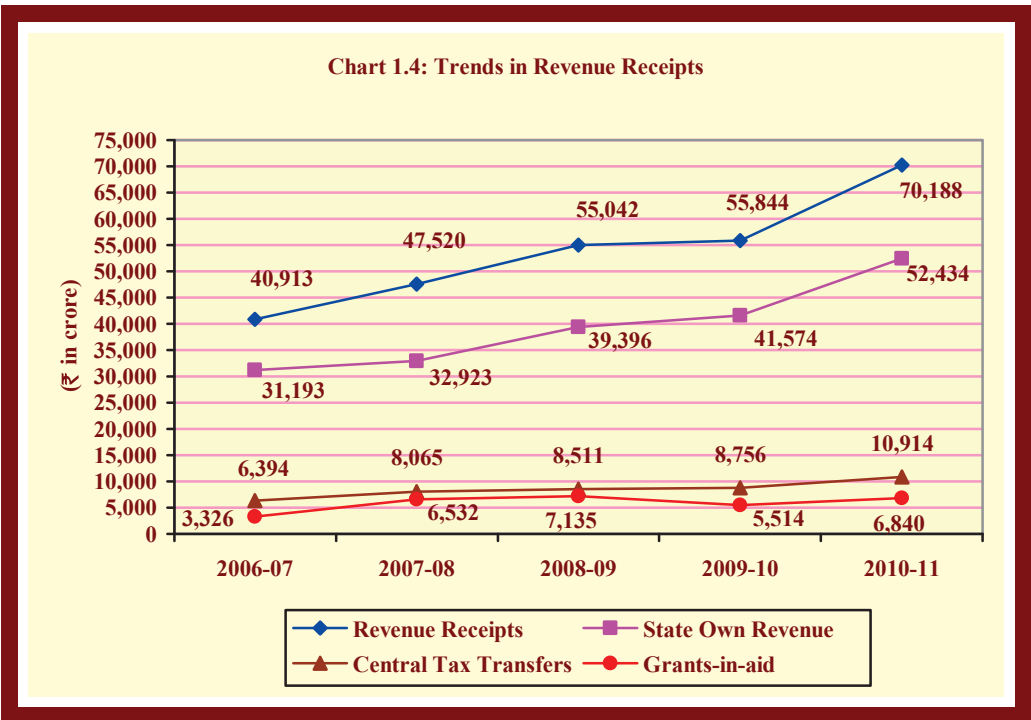
Table 1.2: Funds transferred directly to State Implementing Agencies**(₹ in crore)**

Programme/scheme	Implementing agency in the State	Funds transferred directly by Government of India during 2010-11
Mahatma Gandhi National Rural Employment Guarantee Scheme	District Rural Development Agencies	2,024.90
Rural Housing - Indira Awaas Yojana	District Rural Development Agencies	348.01
Swarnajayanthi Gram Swarozgar Yojana (SGSY)	District Rural Development Agencies	112.69
Pradhan Mantri Gram Sadak Yojana (PMGSY)	State Rural Road Development Agency	469.53
Sarva Shiksha Abhiyan	Tamil Nadu State Mission of Education for all	690.69
National Rural Health Mission (NRHM)	State Health Society	407.39
National Rural Drinking Water Programme	Tamil Nadu Water Supply and Drainage Board	393.53
	Other Agencies	844.07
Total		5,290.81

- Out of ₹ 5,290.81 crore transferred to State implementing agencies, a major amount of ₹ 2,485.60 crore (47 *per cent*) was transferred to District Rural Development Agencies (DRDAs) in respect of the three programmes/schemes as mentioned in **Table 1.2** above. In respect of these three programmes, for which funds were transferred to DRDAs, the fund transfer was raised from ₹ 936 crore in 2008-09 to ₹ 2,485 in 2010-11 an increase of 165 *per cent* in three years. Direct transfer of funds from Government of India to State implementing agencies ran the risk of improper utilisation of funds by these agencies. Unless uniform accounting policies are followed by all these agencies with proper documentation and timely reporting of expenditure, it would be difficult to monitor the end use of these direct transfers.

1.3 Revenue Receipts

Statement-11 of the Finance Accounts details the revenue receipts of the Government. The revenue receipts consist of the State's own taxes and non-tax revenues, Central tax transfers and grants-in-aid from GOI. The trends and composition of revenue receipts over the period 2006-11 are presented in **Appendix 1.4** and depicted in **Charts 1.4 and 1.5** respectively.



- The compounded annual growth rate of revenue receipts stood at 15.73 per cent in the current decade which was more than the other general category states (15.20 per cent).
- The revenue receipts of the State grew by ₹ 14,344 crore in 2010-11 over the previous year. The growth was buoyant at 25.69 per cent as against the average annual growth of 13.48 per cent during 2006-10. The robust growth in revenue receipts was mainly due to improved tax revenue (30.74 per cent).

- The contribution of the state's own taxes and central tax transfers remained at the same level of 68 and 16 *per cent* respectively in 2010-11 as compared to 2006-07, while the contribution of grants-in-aid from GOI increased marginally from 8.13 *per cent* in 2006-07 to 9.75 *per cent* in 2010-11. The share of non-tax revenue increased from 8.36 *per cent* in 2006-07 to 10.38 *per cent* in 2008-09 and dropped to 6.63 *per cent* in 2010-11.

The trends in revenue receipts relative to GSDP are presented in **Table 1.3**.

Table 1.3: Trends in Revenue Receipts relative to GSDP

	2006-07	2007-08	2008-09	2009-10	2010-11
Revenue Receipts (RR) (₹ in crore)	40,913	47,520	55,042	55,844	70,188
Rate of growth of RR (<i>per cent</i>)	20.47	16.15	15.83	1.46	25.69
RR/GSDP ² (<i>per cent</i>)	13.17	13.55	13.71	11.79	12.83
Buoyancy Ratios³					
Revenue Buoyancy with reference to GSDP (ratio)	1.00	1.24	1.10	0.08	1.65
State's own tax buoyancy with reference to GSDP (ratio)	0.93	0.51	0.95	0.47	1.97
Revenue Buoyancy with reference to State's own taxes (ratio)	1.07	2.43	1.15	0.17	0.84

(Source: Finance Accounts of Government of Tamil Nadu)

- The GSDP at the current rate was estimated to increase from ₹ 4,73,519 crore in 2009-10 to ₹ 5,47,267 crore in 2010-11, representing an increase of 15.57 *per cent*.
- Though revenue receipts as a percentage of GSDP increased from 11.79 *per cent* in 2009-10 to 12.83 *per cent* in the current year, it remained more or less at the same level of 13 *per cent* during 2006-11 implying no major change.
- Revenue buoyancy with reference to GSDP and with reference to State's own taxes has gone up during the year. The revenue buoyancy with reference to state's own taxes which had started to decline from 2008-09 was showing a reversal in trend during 2010-11.
- The ratio of State's own tax to GSDP marginally decreased from 8.94 *per cent* in 2006-07 to 8.73 *per cent* in 2010-11.
- All the above factors suggest the necessity to improve the earnings from revenue receipts.

² Advance estimate of GSDP of ₹ 5,47,267 crore has been adopted for 2010-11.

³ Buoyancy ratio indicates the elasticity or degree of responsiveness of a fiscal variable with respect to a given change in the base variable. For instance, revenue buoyancy at 0.6 implies that revenue receipts tend to increase by 0.6 percentage points, if the GSDP increases by 1 *per cent*.

1.3.1 State's Own Resources

As the State's share in central taxes and grants-in-aid is determined on the basis of recommendations of the Finance Commission, collection of central tax receipts, central assistance for Plan schemes etc., the State's performance in mobilisation of additional resources was assessed in terms of its own resources comprising revenue from its own tax and non-tax sources. The gross collection in respect of major taxes and duties as well as the components of non-tax receipts are given in **Table 1.4**.

Table 1.4: Components of State's own resources

(₹ in crore)					
Revenue Head	2006-07	2007-08	2008-09	2009-10	2010-11
Tax Revenue					
Taxes on sales, trades etc.	17,727	18,156	20,675	22,662	28,614
State excise	3,986	4,764	5,756	6,741	8,116
Taxes on vehicles	1,261	1,483	1,710	2,025	2,660
Stamp duty and Registration fees	2,997	3,805	3,794	3,662	4,651
Land revenue	121	78	208	117	113
Taxes on goods and passengers	1,244	1,097	979	1,092	1,626
Other taxes ⁴	435	236	562	248	2,002
Total	27,771	29,619	33,684	36,547	47,782
Non-Tax Revenue					
Interest receipts	1,104	1,242	1,465	1,797	1,663
Dividends & Profits	30	40	36	48	27
Other non-tax receipts	2,288	2,022	4,211	3,182	2,962
Total	3,422	3,304	5,712	5,027	4,652

- As per the Medium Term Fiscal Policy Statement, tax revenue was projected as 10.10 *per cent* of GSDP. Against the projected revenue of ₹ 55,274 crore, the State could realise ₹ 47,782 crore, resulting in short earnings of tax revenue of ₹ 7,492 crore (13.55 *per cent*).
- The compounded annual growth rate of own tax revenue stood at 18.20 *per cent* in the current decade which was more than the other general category states (14.53 *per cent*).
- The own tax revenue of the State increased by ₹ 11,235 crore over the previous year. The growth rate of its own tax revenue, which averaged 9.62 *per cent* per annum during 2007-10 picked up to 30.74 *per cent* during 2010-11.

⁴ Other taxes include taxes on immovable property other than agricultural land, taxes and duties on electricity and agricultural income.

- The marked increase in the growth rate of own tax revenue was mainly due to increase in collection of taxes on sales, trade, etc. (26.26 *per cent*), stamps and Registration (27 *per cent*), taxes on goods and passengers (48.90 *per cent*).
- The non-tax revenue of the State decreased by ₹ 375 crore (7.46 *per cent*) over the previous year. The compounded annual growth rate of the State (12.92 *per cent*) was less than the other general category states (13.87 *per cent*). The decline in the growth rate of non-tax revenue was mainly due to decrease in non-tax revenue receipts under industries (₹ 120.07 crore), urban development schemes (₹ 115.81 crore) and interest receipts (₹ 134.52 crore).

1.3.2 Loss of Revenue due to Evasion of Taxes

Tax evasion leads to non-realisation of legally available revenue to the Government. As of 31 March 2010, the Commercial Taxes Department of the Government had detected 3,741 cases of evasion of sales tax / value added tax. During 2010-11, 7,097 new cases were detected. However, the department completed assessments only in respect of 4,562 cases leading to a pendency of 6,276 cases as at the end of March 2011. As assessments were not completed in a large number of cases, the extent of revenue realisable from tax evaders could not be assessed.

1.3.3 Revenue Arrears

As on 31 March 2011, revenue arrears amounted to ₹ 12,592.17 crore (Sales Tax: ₹ 10,132.34 crore; Mines and Minerals: ₹ 2,179.09 crore; Stamp duty and Registration fees: ₹ 213.92 crore; Others: ₹ 66.82 crore). Out of this, ₹ 7,412.65 crore was outstanding for more than five years (Sales Tax: ₹ 5,598.76 crore; Mines and Minerals: ₹ 1,606.20 crore; Stamp duty and Registration fees: ₹ 160.35 crore; Others: ₹ 47.34 crore). Tax amounting to ₹ 620.25 crore was proposed to be written off. Amount outstanding for more than five years has increased by ₹ 1,850.16 crore (33.26 *per cent*) over the previous year.

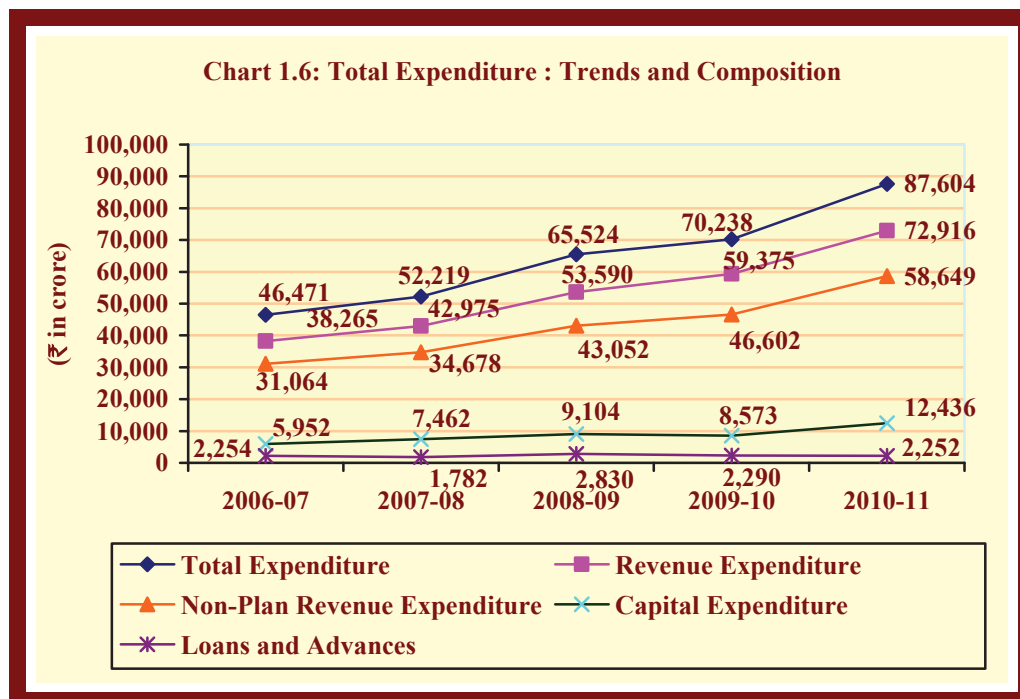
Considering the huge sums involved, Government needs to take note of these mounting arrears.

1.4 Application of Resources

Analysis of the allocation of expenditure at the State Government level assumes significance since major expenditure responsibilities are entrusted with them. Within the framework of fiscal responsibility legislations, there are budgetary constraints in raising public expenditure financed by deficit or borrowings. It is, therefore, important to ensure that the ongoing fiscal correction and consolidation process at the State level is not at the cost of expenditure, especially the expenditure directed towards development of social sector.

1.4.1 Growth and Composition of Expenditure

Chart 1.6 presents the trends in total expenditure over a period of five years (2006-11) and its composition both in terms of 'economic classification' and 'expenditure by activities' is depicted in **Charts 1.7 and 1.8** respectively.



- During the five year period 2006-11, nearly 82 to 84 *per cent* of the total expenditure⁵ constituted revenue expenditure, whereas capital expenditure ranged between 12 and 14 *per cent* of the total expenditure during the same period.
- The total expenditure during 2010-11 increased by ₹ 17,366 crore (24.72 *per cent*) over the previous year. The revenue expenditure increased by ₹ 13,541 crore (22.81 *per cent*) and non-plan expenditure increased by ₹ 12,047 crore (25.85 *per cent*). The revenue expenditure was 83.23 *per cent* of the total expenditure, of which 80.43 *per cent* was on the non-plan component.
- The capital expenditure increased by ₹ 3,863 crore (45.06 *per cent*) and the loans and advances decreased by ₹ 38 crore (1.66 *per cent*).
- Revenue receipts of the State met 80.12 *per cent* of the total expenditure during 2010-11 as against 84 *per cent* during 2008-09 and 79.51 *per cent* during 2009-10.

⁵ Total expenditure includes revenue expenditure, capital expenditure and disbursement of loans and advances.

Chart 1.7: Total Expenditure : Trends in Share of its Components

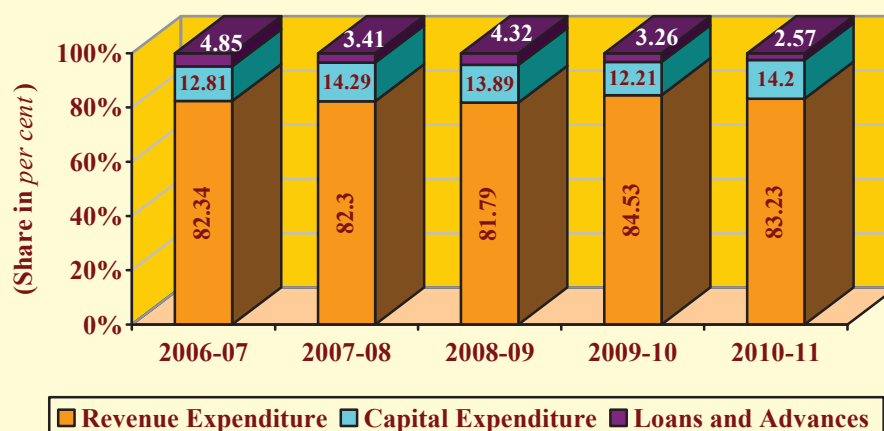
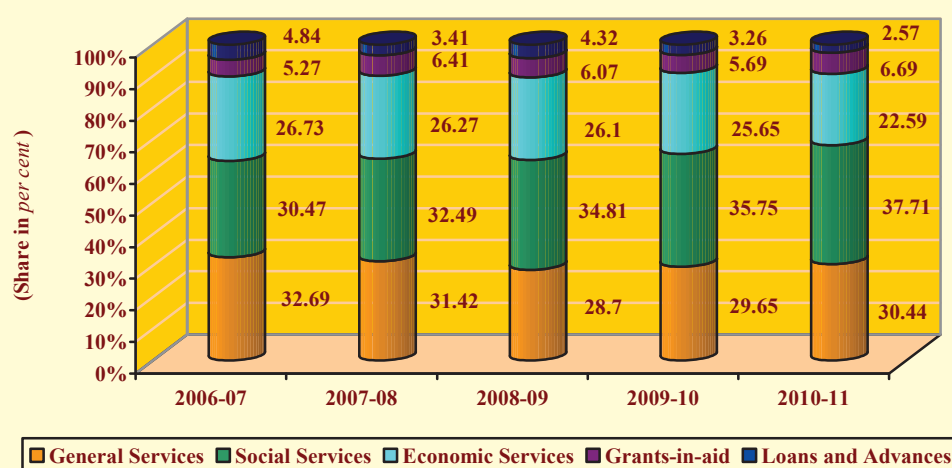


Chart 1.8: Total Expenditure: Trends by 'Activities'



- The expenditure on General Services, Social Services and Economic Services during 2010-11 grew by 28.04 per cent, 31.56 per cent and 9.88 per cent respectively over the previous year.
- The increase in the expenditure on Social Services was mainly on account of increased spending of ₹ 2,409 crore on General Education and ₹ 930 crore on Health and Family Welfare.

1.4.2 Committed Expenditure

The committed expenditure of the State Government on revenue account mainly consists of interest payments, expenditure on salaries and wages, pensions and subsidies. **Table 1.5** presents the trends in the expenditure on these components during 2006-11.

Table 1.5: Components of Committed Expenditure

Components of Committed Expenditure	(₹ in crore)				
	2006-07	2007-08	2008-09	2009-10	2010-11
Salaries and wages, of which	8,694 (21.25)	9,690 (20.39)	12,859 (23.36)	15,638 (28.00)	19,029 (27.11)
Non-Plan Head	7,673	8,641	11,470	14,141	17,150
Plan Head*	1,021	1,049	1,389	1,497	1,879
Salary grants**	1,863 (4.55)	2,072 (4.36)	2,756 (5.00)	3,219 (5.76)	4,017 (5.72)
Interest Payments	5,506 (13.46)	6,086 (12.81)	5,963 (10.83)	6,667 (11.93)	7,940 (11.31)
Expenditure on Pension	5,430 (13.27)	6,017 (12.66)	7,735 (14.05)	8,385 (15.01)	10,951 (15.60)
Subsidies	4,177 (10.21)	4,305 (9.06)	6,600 (11.99)	6,653 (11.91)	7,739 (11.02)
Total	25,670 (62.74)	28,170 (59.28)	35,913 (65.25)	40,562 (72.63)	49,676 (70.77)

(Source: Finance Accounts of Government of Tamil Nadu)

Figures in the brackets indicate percentage of revenue receipts

* Plan head also includes the salaries and wages paid under Centrally Sponsored Schemes

** Salary grants are released to aided educational institutions and Urban Local Bodies towards meeting the expenditure on salaries of teachers and staff.

- The committed expenditure (₹ 49,676 crore) stood at 70.77 per cent of the total revenue receipts (₹ 70,188 crore) of the State during 2010-11 as against 72.63 per cent during 2009-10. It had increased from 62.74 per cent in 2006-07 to 70.77 per cent of the total revenue receipts in 2010-11. As it leaves little amount to other purposes, there is a necessity to contain the committed expenditure particularly under the heads salaries and subsidies.
- The committed expenditure stood at 84.70 per cent of the Non-Plan revenue expenditure during 2010-11 as against 81.42 per cent during 2008-09 and 87.04 per cent during 2009-10 mainly due to increase of ₹ 4,189 crore in salary expenditure (22.21 per cent) consequent on implementation of sixth pay commission recommendations.
- The expenditure on salaries and wages, inclusive of salary grants was ₹ 23,046 crore and accounted for 42.65 per cent of the revenue expenditure net of interest and pension as against the TFC's normative prescription of 35 per cent.
- The expenditure on salaries and wages, inclusive of salary grants which marginally declined from the level of 25.80 per cent of revenue receipts in 2006-07 to 24.75 per cent in 2007-08, moved upward from 2008-09 and stood at 32.83 per cent during 2010-11. The increase was mainly due to implementation of the sixth pay commission recommendations.
- Subsidies were on a continuous increase. They went up by ₹ 1,086 crore (16.32 per cent) in 2010-11 when compared to the previous year. The subsidy paid under Public Distribution System Support and to Tamil Nadu Electricity Board alone accounted for ₹ 5,212 crore (67.35 per cent).

- The expenditure towards interest payments increased by ₹ 1,273 crore (19.09 *per cent*) over the previous year. This was mainly due to repayment of interest on market loans to the extent of ₹ 1,049 crore. As a percentage of Non-Plan expenditure, it decreased from 14.31 *per cent* in 2009-10 to 13.54 *per cent* in 2010-11.

1.4.3 Financial Assistance by State Government to Local Bodies and other institutions

The quantum of assistance provided by way of grants and loans to local bodies and others during the current year relative to the previous years is presented in **Table 1.6**.

Table 1.6: Financial Assistance to Local Bodies, etc

	(₹ in crore)				
Financial Assistance to Institutions	2006-07	2007-08	2008-09	2009-10	2010-11
Educational Institutions (Aided Schools, Aided Colleges, Universities, etc.)	570	605	433	703	940
Municipal Corporations and Municipalities	1,591	393	1,865	1,965	2,841
Zilla Parishads and Other Panchayati Raj Institutions	1,508	3,216	1,890	2,101	3,071
Development Agencies	295	920	217	286	190
Hospitals and Other Charitable Institutions	20	19	106	126	314
Other Institutions ⁶	4,753	3,248	5,726	5,636	6,559
Total	8,737	8,401	10,237	10,817	13,915
Assistance as per percentage of Revenue Expenditure	22.83	19.55	19.10	18.22	19.08

(Source: Accounts compiled by the Principal Accountant General (A&E), Tamil Nadu)

- Financial assistance to local bodies and other institutions increased from ₹ 8,737 crore in 2006-07 to ₹ 13,915 crore in 2010-11. As a percentage of the revenue expenditure, it decreased from the level of 22.83 *per cent* in 2006-07 to 19.08 *per cent* in 2010-11. Assistance to hospitals and other charitable institutions showed a quantum jump from ₹ 126 crore in 2009-10 to ₹ 314 crore in 2010-11. The assistance to development agencies decreased by 33.57 *per cent* over the previous year.

1.5 Quality of Expenditure

The availability of better social and physical infrastructure in the State generally reflects the quality of its expenditure. The improvement in the quality of expenditure basically involves three aspects *viz.*, adequacy of the expenditure (i.e. adequate provisions for providing public services), efficiency of expenditure use and its effectiveness (assessment of outlay-outcome relationships for select services).

⁶ Institutions/agencies connected with water supply and sanitation, housing, social welfare, labour and employment, forestry and wild life, agriculture and allied activities, village and small industries, industries and minerals and relief on account of natural calamities.

1.5.1 Adequacy of Public Expenditure

The expenditure responsibilities relating to the social sector and the economic infrastructure assigned to the State Governments are largely State subjects. Enhancing human development levels requires the States to step up their expenditure on key social services like education, health etc. Low fiscal priority (ratio of expenditure category to aggregate expenditure) would be deemed to have been given to a particular sector if it was below the national average. **Table 1.7** analyses the fiscal priority of the State Government with regard to development expenditure, social sector expenditure and capital expenditure during 2010-11.

Table 1.7: Fiscal Priority of the State in 2007-08 and 2010-11

Fiscal Priority by the State	AE/GSDP	DE [#] /AE	SSE/AE	CE/AE	(In per cent)	
					Education/AE	Health/ AE
General Category States Average (Ratio) 2007-08	16.65	64.28	32.54	16.14	14.64	3.98
Tamil Nadu State's Average (Ratio) 2007-08	14.88	62.05	33.01	14.29	13.54	3.51
General Category States Average (Ratio) 2010-11	16.20	64.42	36.75	13.27	17.42	4.35
Tamil Nadu State's Average (Ratio) 2010-11	16.61	60.41	36.81	13.68	15.26	4.84
AE: Aggregate Expenditure DE: Development Expenditure SSE: Social Sector Expenditure CE: Capital Expenditure # Development expenditure includes Development Revenue Expenditure, Development Capital Expenditure and Loans and Advances disbursed. Source : For GSDP, the information was collected from the State's Directorate of Economics and Statistics						

- In 2010-11, Tamil Nadu had spent marginally higher proportion of its GSDP on Aggregate Expenditure as compared to the general category states. As compared to 2007-08, Tamil Nadu had spent higher proportion of its GSDP on Aggregate Expenditure in the year 2010-11, implying satisfactory level of adequacy when compared to the all India level.
- Development expenditure consists of both economic service expenditure and social sector expenditure. Development expenditure as a proportion of Aggregate Expenditure in Tamil Nadu has been lower than the general category states' average, implying low priority.
- In Tamil Nadu though adequate priority has been given to social sector but adequate priority has not been given to the education sector. As far as priority to health sector is concerned, there was improvement in 2010-11, as higher proportion of expenditure was spent on health sector as compared to general category states.
- In Tamil Nadu, the proportion of expenditure on capital has been lower in 2007-08 but marginally higher in 2010-11 as compared to the general category states. However, the proportion of capital expenditure in 2010-11 was lower than 2007-08. Increased priority to physical capital formation will further increase the growth prospects of the state by creating durable assets.

1.5.2 Efficiency of Expenditure Use

In view of the importance of public expenditure on development heads from the point of view of social and economic development, it is important for the State Governments to take appropriate expenditure rationalisation measures and lay emphasis on provision of core public and merit goods⁷. Apart from improving the allocation towards development expenditure⁸, particularly in view of the fiscal space being created on account of decline in debt servicing in recent years, the efficiency of expenditure use is also reflected by the ratio of capital expenditure to total expenditure (and/or GSDP) and the proportion of revenue expenditure on operation and maintenance of the existing Social and Economic Services. The higher the ratio of these components to the total expenditure (and/or GSDP), the better would be the quality of expenditure. While **Table 1.8** presents the trends in development expenditure relative to the aggregate expenditure of the State during 2006-11, **Table 1.9** provides the details of capital expenditure and the components of revenue expenditure incurred on the maintenance of the selected Social and Economic Services during 2009-10 and 2010-11.

Table 1.8: Development Expenditure

(₹ in crore)					
Components of Development Expenditure	2006-07	2007-08	2008-09	2009-10	2010-11
Development Expenditure (a to c)	28,835 (62.05)	32,464 (62.16)	42,736 (65.22)	45,412 (64.65)	54,917 (62.69)
a. Development Revenue Expenditure	20,823 (44.81)	23,497 (45.00)	31,032 (47.36)	35,079 (49.94)	41,131 (46.95)
b. Development Capital Expenditure	5,758 (12.39)	7,185 (13.76)	8,874 (13.54)	8,043 (11.45)	11,694 (13.35)
c. Development Loans and Advances	2,254 (4.85)	1,718 (3.29)	2,761 (4.22)	2,290 (3.26)	2,092 (2.39)

(Source: Finance Accounts of Government of Tamil Nadu)

Figures in brackets indicate percentage of aggregate expenditure

⁷ Core public goods are goods which all citizens enjoy in common in the sense that each individual's consumption of such a good leads to no subtractions from any other individual's consumption of that good, e.g., enforcement of law and order, security and protection of rights; pollution free air and other environmental goods, road infrastructure etc. Merit goods are commodities that the public sector provides free or at subsidized rates because an individual or society should have them on the basis of some concept of need, rather than the ability and willingness to pay the Government and therefore wishes to encourage their consumption. Examples of such goods include the provision of free or subsidized food for the poor to support nutrition, delivery of health services to improve quality of life and reduce morbidity, providing basic education to all, drinking water and sanitation etc.

⁸ The analysis of expenditure data is disaggregated into development and non-development expenditure. All expenditure relating to Revenue Account, Capital Outlay and Loans and Advances is categorized into Social Services, Economic Services and General Services. Broadly, the Social and Economic Services constitute development expenditure, while expenditure on General Services is treated as non-development expenditure.

Table 1.9: Efficiency of Expenditure Use in Selected Social and Economic Services
(Percentage)

Social/Economic Infrastructure	2009-10		2010-11	
	Ratio of CE to TE	Ratio of S&W to RE	Ratio of CE to TE	Ratio of S&W to RE
Social Services (SS)				
General Education	3.27	58.27	2.58	55.26
Health and Family Welfare	13.09	64.25	7.40	58.05
WS, Sanitation & HUD	29.29	1.66	59.03	2.29
Total (SS)	7.88	42.47	16.21	50.91
Economic Services (ES)				
Agri & Allied Activities	17.68	30.00	11.18	36.86
Irrigation and Flood Control	48.76	30.20	50.81	33.91
Power & Energy	9.31	0.11	51.29	0.13
Transport	69.40	14.61	69.71	26.18
Total (ES)	23.48	14.22	44.99	27.19
Total (SS+ES)	14.62	32.71	26.41	45.48

(Source: Finance Accounts of Government of Tamil Nadu)

TE: Total expenditure on the Sector/Service concerned; CE: Capital Expenditure;
RE: Revenue Expenditure; S&W: Salaries and Wages.

Though development expenditure, in real terms was increasing continuously during 2006-11, as a percentage of aggregate expenditure of the State it declined from 65.22 *per cent* in 2008-09 to 62.69 *per cent* in 2010-11.

However, the development capital expenditure as a percentage of aggregate expenditure of the State, which declined from the level of 13.54 *per cent* in 2008-09 to 11.45 *per cent* in 2009-10, increased to 13.35 *per cent* in 2010-11.

Expenditure on Social Services

- The capital expenditure on Social Services had increased from ₹ 2,151 crore in 2009-10 to ₹ 4,123 crore in 2010-11 (91.68 *per cent*) in real terms and as a percentage of aggregate expenditure of the State, it had increased from 3.06 in 2009-10 to 4.71 in 2010-11. As a percentage of total expenditure on Social Services, it increased from 7.88 in 2009-10 to 16.21 in 2010-11.
- Among the social services, while the capital expenditure on Water Supply, Sanitation and Housing and Urban Development had a steep increase from 29.29 *per cent* in 2009-10 to 59.03 *per cent* in 2010-11, the capital expenditure on General Education and Health and Family Welfare suffered a setback in 2010-11 as compared to 2009-10.

Expenditure on Economic Services

- The capital expenditure on Economic Services had increased from ₹ 5,892 crore in 2009-10 to ₹ 7,571 crore in 2010-11.
- The capital expenditure on Agriculture and Allied Activities declined significantly from ₹ 939 crore in 2009-10 to ₹ 459 crore in 2010-11. As a percentage of total expenditure on Agriculture and Allied Activities, it declined from 17.68 in 2009-10 to 11.18 in 2010-11. This was mainly due to decrease of ₹ 478 crore towards investments in credit cooperatives.
- The capital expenditure on Power and Energy increased from ₹ 135 crore in 2009-10 to ₹ 1,335 crore in 2010-11. The increase was mainly under “Share Capital Assistance to Tamil Nadu Electricity Board”.

1.6 Financial Analysis of Government Expenditure and Investments

In the post-Fiscal Responsibility and Budget Management framework, the State is expected to keep its fiscal deficit (and borrowings) not only at low levels but also meet its capital expenditure/investment (including loans and advances) requirements. In addition, in a transition to complete dependence on market-based resources, the State Government needs to initiate measures to earn adequate returns on its investments, recover its cost of borrowed funds rather than bearing the same on its budget in the form of implicit subsidies and take requisite steps to infuse transparency in financial operations. This section presents a broad financial analysis of investments and other capital expenditure undertaken by the Government during the current year *vis-à-vis* the previous years.

1.6.1 Financial Results of Irrigation Works

Ensuring the commercial viability of irrigation projects through realisation of adequate revenue by way of user charges has been a policy of Government of India. However, Audit observed that the revenue from irrigation projects (₹ 28.29 crore) during 2010-11 was only 3.64 *per cent* of the maintenance expenditure (₹ 777.61 crore).

Appendix IX of Finance Accounts depicts the financial results of five major and 47 medium irrigation projects. The revenue realised from these projects during 2009-10 was ₹ 11.80 crore. After meeting the working and maintenance expenditure (₹ 166.99 crore) and interest charges (₹ 118.97 crore), these 52 projects suffered a net loss of ₹ 274.16 crore during 2009-10.

1.6.2 Incomplete projects

The department-wise information pertaining to incomplete projects as on 31 March 2011 is given in **Table 1.10**.

Table 1.10: Department-wise profile of incomplete projects

(₹ in crore)

Department	No. of Incomplete Projects*	Initial Budgeted Cost	Revised Total Cost of Projects**	Cost Over-runs	Cumulative actual expenditure as on 31.3.2011
Buildings	27	138.14	139.94	1.80	82.77
Roads and Bridges	21	550.40	560.52	10.12	529.37
Irrigation (Water Resources) and Flood Control	14	733.46	813.17	79.71	596.54
Total	62	1,422.00	1,513.63	91.63	1,208.68

(Source: Finance Accounts of Government of Tamil Nadu).

* Only those projects which were scheduled to be completed before 31 March 2011 were included.

** Indicates the revised total cost of the projects as per the last revision by the State Government as of March 2011.

- Failure to complete the projects on time leads to escalation of project costs and delays the accrual of the projects' benefits to the society at large. Further, delays also result in postponement of revenue realization from the projects.

1.6.3 Investment and returns

As of 31 March 2011, Government had invested ₹ 10,222 crore in statutory corporations, rural banks, joint stock companies and co-operatives (**Table 1.11**). The average return on these investments was 0.22 *per cent*, while Government paid an average interest rate of 7.53 *per cent* on its borrowings during 2010-2011.

Table 1.11: Return on Investment

Investment/Return/Cost of Borrowings	2006-07	2007-08	2008-09	2009-10	2010-11
Investment at the end of the year (₹ in crore)	4,278.43	6,230.40	6,471.22	8,107.24	10,222.64
Return (₹ in crore)	26.32	22.10	35.59	30.18	22.33
Return (in <i>per cent</i>)	0.62	0.35	0.55	0.37	0.22
Average rate of interest on Government borrowing (in <i>per cent</i>)	8.56	8.86	7.71	7.29	7.53
Difference between interest rate and return (in <i>per cent</i>)	7.94	8.51	7.16	6.92	7.31

(Source: Finance Accounts of Government of Tamil Nadu)

As of March 2011, Government has invested in two statutory corporations (₹ 3,810 crore), 66 Government companies (₹ 3,391 crore), six Joint Stock companies (₹ 2 crore) and 9,133 co-operatives (₹ 3,020 crore). During 2010-11, Government infused an additional capital of ₹ 133.12 crore into seven ailing State Transport Undertakings, which had accumulated loss of ₹ 5,445.18 crore. Other major investments included ₹ 1,335.13 crore in Tamil Nadu Electricity Board and ₹ 600 crore in Chennai Metro Rail.

1.6.4 Loans and advances by State Government

In addition to investments in co-operative societies, corporations and companies, Government has also been providing loans and advances to many

of these institutions/ organizations. **Table 1.12** presents the outstanding loans and advances as on 31 March 2011 and interest receipts *vis-à-vis* interest payments during the last three years.

Table 1.12: Average interest received on loans advanced by the State Government

(₹ in crore)

Quantum of Loans/Interest Receipts/ Cost of Borrowings	2008-09	2009-10	2010-11
Opening Balance	6,918	7,814	7,517
Amount advanced during the year	2,830	2,290	2,252
Amount repaid during the year	1,934	2,587	770
Closing Balance	7,814	7,517	8,999
Net increase (+) / decrease (-)	896	(-) 297	1,482
Interest Receipts	205	266	78
Interest receipts as percentage of outstanding Loans and advances	2.78	3.47	0.94
Interest payments as percentage of outstanding fiscal liabilities of the State Government.	7.71	7.29	7.53
Difference between interest payments and interest receipts (<i>per cent</i>)	(-) 4.93	(-) 3.82	(-) 6.59

(Source: Finance Accounts of Government of Tamil Nadu)

- The quantum of loans advanced decreased from ₹ 2,290 crore in 2009-10 to ₹ 2,252 crore in 2010-11. Repayments also decreased from ₹ 2,587 crore in 2009-10 to ₹ 770 crore in 2010-11 (70.24 *per cent*), resulting in increase in the outstanding balance from ₹ 7,517 crore in 2009-10 to ₹ 8,999 crore in 2010-11. The difference between the interest payments and interest receipts increased from 3.82 *per cent* in 2009-10 to 6.59 *per cent* in 2010-11.
- The major recipients of loans and advances were (i) Social Sector- water supply, sanitation, housing and urban development (₹ 376 crore), out of which ₹ 115 crore were advanced to Tamil Nadu Cooperative Housing Federation Limited as Ways and Means Advance and ₹ 118 crore were advanced to Public Sector and other undertakings (ii) Economic Sector- (a) Agriculture and Allied Services (₹ 626 crore), out of which ₹ 500 crore was advanced for food storage and warehousing to statutory corporations, boards and Government companies, (b) Industries and Minerals (₹ 279 crore) and (iii) Transport Sector (₹ 759 crore), out of which ₹ 125 crore was given as short term loans to State Transport Undertakings and ₹ 634 crore as ways and means advance to Transport Corporations.

1.6.5 Cash Balances and Investment of Cash Balances

Table 1.13 depicts the cash balances and investments made by the State Government out of cash balances during the year.

Table 1.13: Cash Balances and Investment of Cash Balances

(₹ in crore)

Particulars	As on 31 March 2010	As on 31 March 2011	Increase (+)/ Decrease (-)
Cash Balances	19,487	15,747	(-) 3,740
Investments from Cash Balances (a to d)			
(a) GOI Treasury Bills	17,252	9,877	(-) 7,375
(b) GOI Securities	180	3,620	3,440
(c) Other Securities, if any specify	2,029	2,224	195
(d) Others - (Treasury/departmental cash balance, remittance etc.)	26	26	..
Funds-wise Break-up of Investment from Earmarked balances (a to c)			
(a) Sinking Fund	2,451	2,653	202
(b) Famine Relief Fund	..	..	..
(c) Infrastructure Development Fund	..	109	109
Interest realised	799	683	(-) 116

(Source: Finance Accounts of Government of Tamil Nadu)

- The cash balance as on 31 March 2011 decreased by ₹ 3,740 crore over the previous year. The cash balance (₹ 15,747 crore) available with the State Government continued to be heavy.
- The interest realised during the year on investment of cash balances decreased by ₹ 116 crore as compared to the previous year.

The State Government maintained the minimum required cash balance of ₹ 3.25 crore with the Reserve Bank of India during 2010-11 under an agreement with the Reserve Bank of India. No ways and means advance and overdraft was taken during the year.

1.7 Assets and Liabilities

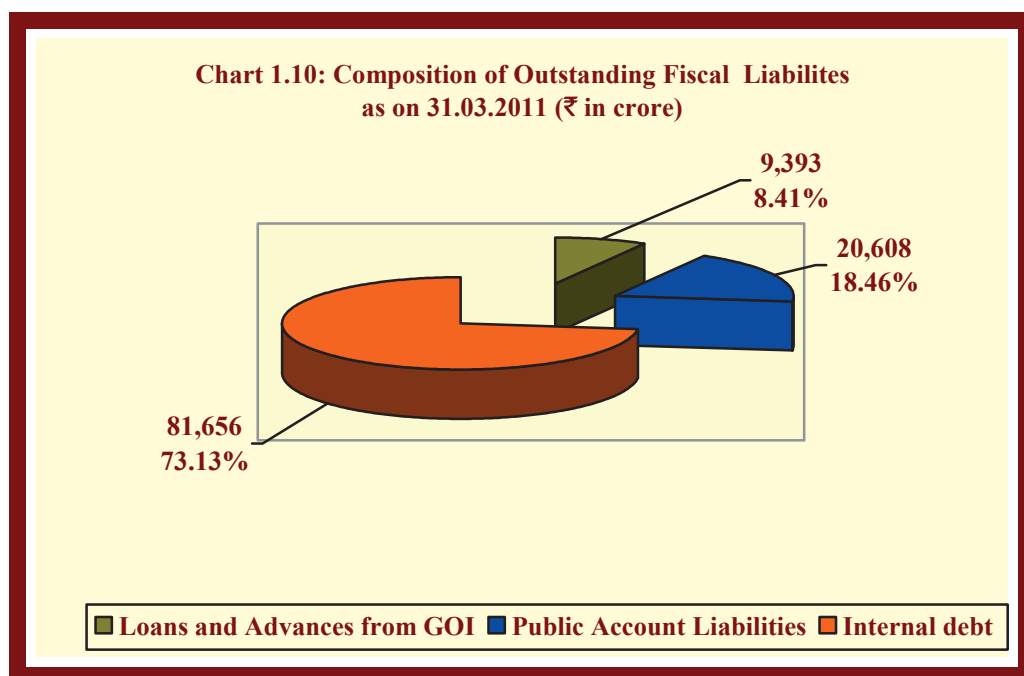
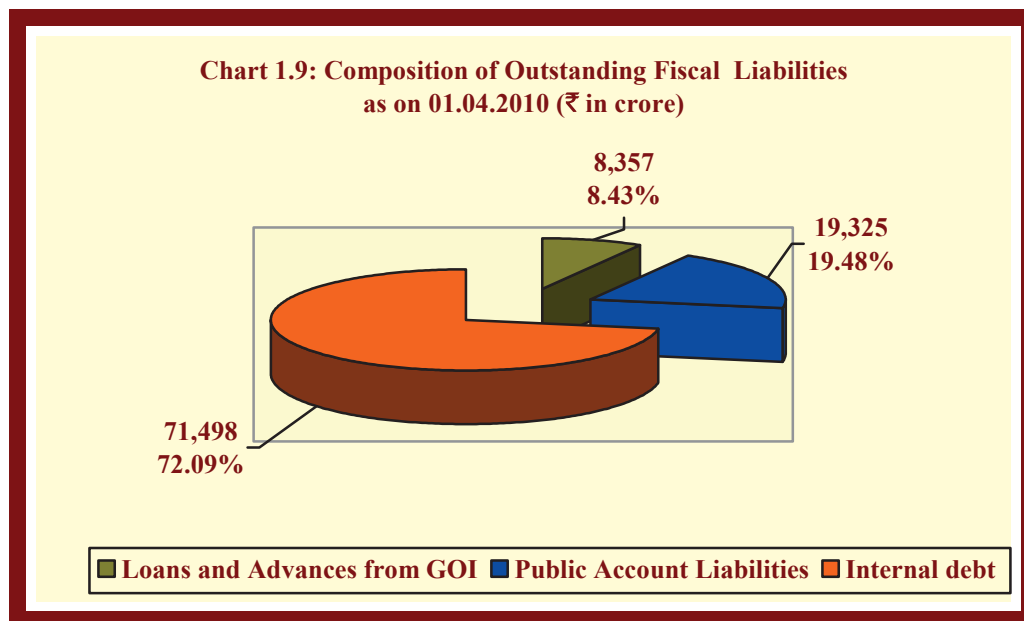
1.7.1 Growth and Composition of Assets and Liabilities

In the existing Government accounting system, comprehensive accounting of fixed assets like land and buildings owned by the Government is not done. However, the Government accounts do capture the financial liabilities of the Government and the assets created out of the expenditure incurred. **Appendix 1.5** gives an abstract of such liabilities and assets as on 31 March 2011, compared with the corresponding position on 31 March 2010. While the liabilities in this Appendix consist mainly of internal borrowings, loans and advances from GOI, receipts from the Public Account and Reserve Funds, the assets comprise mainly the capital outlay, loans and advances given by the State Government and cash balances.

The Tamil Nadu Fiscal Responsibility Act, 2003 defines the total liability of the State as ‘the liabilities under the Consolidated Fund of the State and the Public Account of the State’, which include loans and advances from the Central Government, open market borrowings, loans from financial institutions, Provident Fund balances of Government employees, Reserve funds, Deposits etc.

1.7.2 Fiscal Liabilities

The trends in outstanding fiscal liabilities of the State are presented in **Appendix 1.4**. The composition of fiscal liabilities during the current year *vis-à-vis* the previous year is presented in **Charts 1.9** and **1.10**.



- The outstanding fiscal liabilities have shown a steady increase from ₹ 66,320 crore at the end of 2006-07 to ₹ 1,11,657 crore at the end of 2010-11.

- The fiscal liabilities at the end of 2010-11 represented 159.08 *per cent* of the revenue receipts during the year as against 177.60 *per cent* of the revenue receipts during 2009-10.
- Public Account Liabilities as a percentage of the fiscal liabilities decreased from 19.48 *per cent* in 2009-10 to 18.46 *per cent* at the end of 2010-11. Internal debt at 73.13 *per cent* of fiscal liabilities was marginally higher than that of the previous year (72.09 *per cent*), whereas outstanding loans and advances remained the same as that of the previous year.

1.7.3 Status of Guarantees – Contingent liabilities

Guarantees are liabilities contingent on the Consolidated Fund of the State in cases of defaults by borrowers for whom the guarantees have been extended.

As per Statement 9 of the Finance Accounts, the maximum amount for which guarantees were given by the State and the outstanding guarantees for the last three years is given in **Table 1.14**.

Table 1.14: Guarantees given by the Government of Tamil Nadu

(₹ in crore)			
Guarantees	2008-09	2009-10	2010-11
Maximum amount guaranteed	11,062	12,830	16,884
Outstanding amount of guarantees	4,633	6,297	15,955
Percentage of maximum amount guaranteed to total Revenue receipts of previous year	23.28	23.31	30.16
Criteria as per the TN Fiscal Responsibility Act, 2003	Cent <i>per cent</i> revenue receipts of previous year or 10 <i>per cent</i> of GSDP, whichever is lower.		

(Source: Finance Accounts of Government of Tamil Nadu)

- Government has constituted (March 2003) a “Guarantees Redemption Fund” for discharge of invoked guarantees. An amount of ₹ 133.74 crore was credited to the fund during 2010-11 and ₹ 223.44 crore was disbursed from the fund. The balance in the Fund as of March 2011 was ₹ 19.24 crore.
- The maximum amount guaranteed was well within the stipulations (i.e. cent *per cent* revenue receipts) of the Tamil Nadu Fiscal Responsibility, Act 2003. As a percentage of revenue receipts, it increased from 23.31 in 2009-10 to 30.16 in 2010-11. Similarly as a percentage of GSDP, it increased from 2.71 in 2009-10 to 3.09 in 2010-11.
- As against a guarantee fee of ₹ 22.68 crore receivable only ₹ 3.92 crore was realised during the year 2010-11.

1.7.4 Off-Budget Borrowings

The borrowings of a State are governed under Article 293 of the Constitution of India. In addition to the liabilities shown in **Appendix 1.5**, the State guarantees loans availed of by Government companies/corporations. These

companies/corporations borrow funds from the market/financial institutions for implementation of various State Plan programmes projected outside the State budget. Although the State Government projects that funds for these programmes would be met out of the resources mobilized by these companies/corporations outside the State budget, in reality, the borrowings of many of these concerns are repaid by the Government and ultimately turn out to be liabilities of the State Government termed as 'off-budget borrowings'. Though off-budget borrowings are not permissible under Article 293 (3), the State continues to undertake such off-budget borrowings. Details of borrowings collected from Tamil Nadu Water Supply and Drainage Board (Board) disclosed that as of 31 March 2011, the Board owed ₹ 84.29 crore to two financial organisations towards its borrowings for executing various water supply projects. The State Government had undertaken to repay the principal and interest and the off-budget borrowings, which add to the fiscal liability of the State are not captured in the Finance Accounts of the State.

1.8 Debt Sustainability

Apart from the magnitude of debt of the State Government, it is important to analyze the various indicators that determine the debt sustainability⁹ of the State. This section assesses the sustainability of debt of the State Government in terms of debt stabilization¹⁰; sufficiency of non-debt receipts¹¹; net availability of borrowed funds¹²; burden of interest payments (measured by interest payments to revenue receipts ratio) and the maturity profile of State Government securities. **Table 1.15** analyzes the debt sustainability of the State according to these indicators for a period of three years beginning from 2008-09.

⁹ Debt sustainability is defined as the ability of the State to maintain a constant debt-GSDP ratio over a period of time and also embodies the concern about the ability to service its debt. Sustainability of debt, therefore, also refers to the sufficiency of liquid assets to meet current or committed obligations and the capacity to keep a balance between the costs of additional borrowings and the returns from such borrowings. It means that the rise in fiscal deficit should match the increase in the capacity to service the debts.

¹⁰ A necessary condition for stability states that if the rate of growth of the economy exceeds the interest rate or cost of public borrowings, the debt-GSDP ratio is likely to be stable provided primary balances are either zero, positive or moderately negative. Given the rate spread (GSDP growth rate – interest rate) and the quantum spread (Debt X rate spread), the debt sustainability condition states that if the quantum spread together with the primary deficit is zero, the debt-GSDP ratio would be constant or the debt would stabilize eventually. On the other hand, if the primary deficit together with the quantum spread turns out to be negative, the debt-GSDP ratio would be rising. In case it is positive, the debt-GSDP ratio would eventually be falling.

¹¹ Adequacy of incremental non-debt receipts of the State to cover incremental interest liabilities and incremental primary expenditure. Debt sustainability could be significantly facilitated if incremental non-debt receipts could meet the incremental interest burden and the incremental primary expenditure.

¹² Defined as the ratio of the debt redemption (principal + interest payments) to total debt receipts and indicates the extent to which the debt receipts are used in debt redemption, indicating the net availability of borrowed funds.

Table 1.15: Debt Sustainability: Indicators and Trends

(₹ in crore)

Indicators of Debt Sustainability	2008-09	2009-10	2010-11
Debt Stabilization (Quantum Spread + Primary Deficit)	7,195	(-) 1,300	(-) 732
Sufficiency of Non-debt Receipts (Resource Gap)	(-) 4,862	(-) 3,259	(-) 4,839
Net Availability of Borrowed Funds	6,627	7,287	4,375
Burden of Interest Payments (IP/RR Ratio)	10.8	11.9	11.3
Maturity Profile of internal debts & GOI loans (in years)			
0 – 1	1,629 (2.44)	1,997 (2.79)	2,800 (3.08)
1 – 3	5,148 (7.71)	5,966 (8.35)	7,658 (8.41)
3 – 5	7,632 (11.42)	7,101 (9.93)	7,944 (8.73)
5 – 7	7,870 (11.78)	9,778 (13.68)	10,865 (11.93)
7 and above	44,531 (66.65)	46,656 (65.25)	58,384 (64.12)
Year wise details not available			3,399 (3.73)

(Source: Finance Accounts of Government of Tamil Nadu)

Figures in brackets represent percentage of total outstanding internal debts and GOI loans

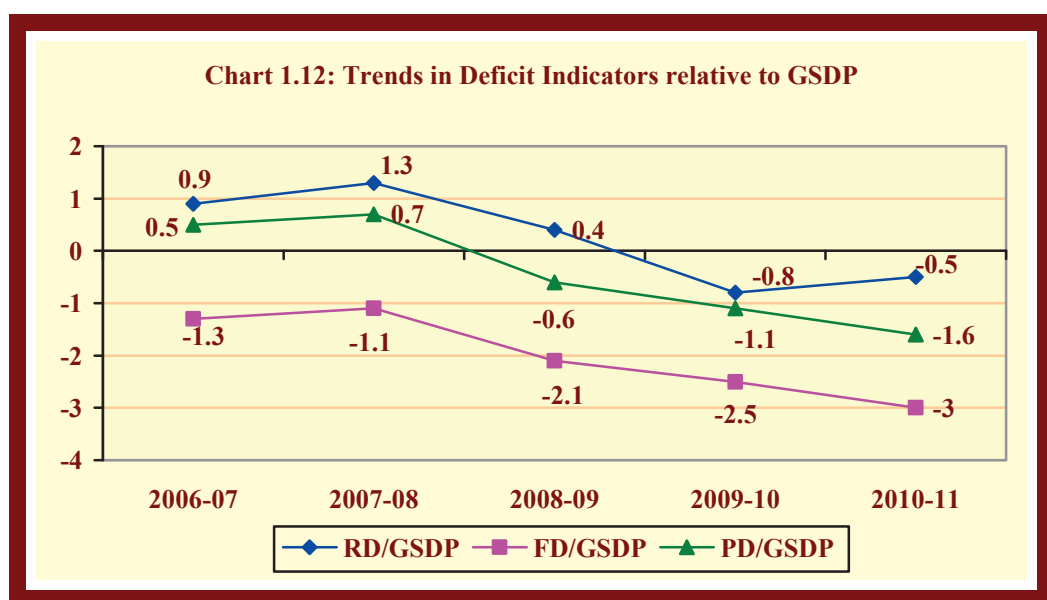
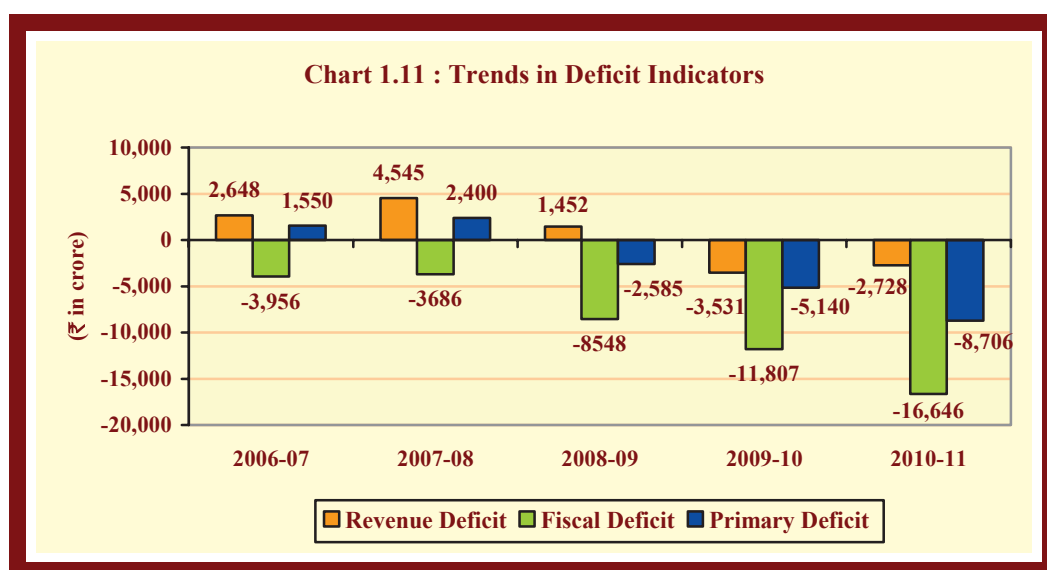
- The quantum spread together with the primary deficit which remained positive in 2008-09 turned to negative during 2009-11 indicating rising dept-GSDP ratio.
- Another indicator for debt stability and its sustainability is the adequacy of incremental non-debt receipts of the State to cover the incremental interest liabilities and incremental primary expenditure. The debt sustainability could be significantly facilitated if the incremental non-debt receipts could meet the incremental interest burden and the incremental expenditure. Positive resource gaps strengthen the capacity of State to sustain the debt. The State experienced a negative resource gap in 2008-09 and it continued to be so in 2010-11. These trends indicate that the State needs to make sustainable efforts to mobilise more resources to meet the incremental liabilities arising on account of additional primary expenditure and interest payments during the year. If the negative resource gap persists in the ensuing years, the State's capacity to sustain the additional debt liabilities would tend to deteriorate.
- The net availability of borrowed funds during 2010-11 was ₹ 4,375 crore, a decrease of ₹ 2,912 crore. This was a result of decrease in receipts under internal debts from ₹ 14,527 crore in 2009-10 to ₹ 13,045 crore in 2010-11 and increase in expenditure on repayment of internal debts from ₹ 2,180 crore in 2009-10 to ₹ 2,887 crore in 2010-11. Further, the interest payments, increased from ₹ 6,667 crore in 2009-10 to ₹ 7,940 crore in 2010-11.
- All the above mentioned factors suggest that the State's sustainability of debt is strained.
- Bunching of repayments in any particular year will cause financial stress to that year's budget. The maturity profile of the State's debt indicates a year-on-year increase in its repayment burden. Hence, the greater the awareness of future debt payments, the Government will be in a position to ensure that fresh borrowings do not have to be paid back in those years where maximum repayment is due. In Tamil Nadu, greater portion of repayments would happen beyond seven years. The State did not have details of repayment schedule for an amount of ₹ 3,399 crore.

1.9 Fiscal Imbalances

Three key fiscal parameters - revenue, fiscal and primary deficits - indicate the extent of overall fiscal imbalances in the finances of the State Government during a specified period. The deficit in the Government accounts represents the gap between its receipts and expenditure. The nature of deficit is an indicator of the prudence of fiscal management of the Government. Further, the ways in which the deficit is financed and the resources raised are applied are important pointers to its fiscal health. This section presents trends, nature, magnitude and the manner of financing these deficits and also the assessment of actual levels of revenue and fiscal deficits *vis-à-vis* targets set under FRBM Act/Rules for the financial year 2010-11.

1.9.1 Trends in Deficits

Charts 1.11 and 1.12 presents the trends in deficit indicators over the period 2006-11.



- The revenue surplus, which prevailed during 2006-07 to 2008-09 turned into negative in 2009-10 and continued to be negative during 2010-11 with a deficit of ₹ 2,728 crore.
- The fiscal deficit which represents the total borrowings of the State Government and its total resource gap increased heavily from ₹ 3,956 crore in 2006-07 to ₹ 16,646 crore in 2010-11.
- The primary surplus of ₹ 1,550 crore in 2006-07 turned into primary deficit of ₹ 2,585 crore in 2008-09 and the deficit increased further in 2009-10 and then to ₹ 8,706 crore in 2010-11.
- Though the ratio of fiscal deficit to GSDP increased from 1.27 in 2006-07 to 3.04 in 2010-11, it was almost same as the target of 3 per cent to be achieved by 31 March 2012 as envisaged in FRBM Act. However, the State is still experiencing revenue deficit.

1.9.2 Composition of Fiscal Deficit and its Financing Pattern

The financing pattern of the fiscal deficit has undergone a compositional shift as reflected in **Table 1.16**.

Table 1.16: Components of Fiscal Deficit and its Financing Pattern

		(₹ in crore)				
	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
Decomposition of Fiscal Deficit		(-) 3,956	(-) 3,686	(-) 8,548	(-) 11,807	(-) 16,646
1	Revenue Surplus/Deficit (-)	2,648	4,545	1,452	(-) 3,531	(-) 2,728
2	Net Capital Expenditure	(-) 5,952	(-) 7,462	(-) 9,104	(-) 8,573	(-) 12,436
3	Net Loans and Advances	(-) 652	(-) 769	(-) 896	297	(-) 1,482
Financing Pattern of Fiscal Deficit*						
1	Market Borrowings	1,372	4,127	8,792	11,725	8,704
2	Loans from GOI	(-) 213	469	724	698	1,036
3	Special Securities issued to National Small Savings Fund	3,898	(-) 782	(-) 173	271	1,540
4	Loans from Financial Institutions	(-) 2,600	287	282	351	(-) 85
5	Small Savings, PF etc	256	383	578	980	1,272
6	Deposits and Advances	1,130	138	1,576	712	1,426
7	Suspense and Miscellaneous	963	162	194	(-) 547	18
8	Remittances	52	(-) 130	78	57	131
9	Reserve Funds	168	130	553	817	(-) 1,106
10	Contingency Fund	16	-	-	1	(-) 30
	Total	5,042	4,784	12,604	15,065	12,906
11	Overall Surplus/Deficit (-) (Cash Balance)	1,086	1,098	4,056	3,258	(-) 3,740

(Source: Finance Accounts of Government of Tamil Nadu)

* All these figures are net of disbursements/outflows during the year.

- The factor contributing to the increase in fiscal deficit was the increase in capital expenditure which increased from ₹ 8,573 crore in 2009-10 to ₹ 12,436 crore in 2010-11.
- The fiscal deficit was largely managed by market borrowings, loan from GOI and Special securities issued to National Small Savings Fund (NSSF) which constituted 67.76 *per cent* of the fiscal deficit during 2010-11.

1.9.3 Quality of Deficit/Surplus

The ratio of revenue deficit to fiscal deficit and the decomposition of primary deficit into primary revenue deficit and capital expenditure (including loans and advances) would indicate the quality of deficit in the States' finances. The ratio of revenue deficit to fiscal deficit indicates the extent to which borrowed funds were used for current consumption. The bifurcation of the primary deficit (**Table 1.17**) would indicate the extent to which the deficit had been on account of enhancement in capital expenditure, which may have been desirable to improve the productive capacity of the State's economy.

Table 1.17: Primary deficit/Surplus – Bifurcation of factors

(₹ in crore)

Year	Non-debt receipts	Primary Revenue Expenditure	Capital Expenditure	Loans and Advances	Primary Expenditure	Primary revenue deficit (-) / surplus (+)	Primary deficit (-) / surplus (+)
1	2	3	4	5	6 (3+4+5)	7 (2-3)	8 (2-6)
2006-07	42,515	32,759	5,952	2,254	40,965	9,756	1,550
2007-08	48,533	36,889	7,462	1,782	46,133	11,644	2,400
2008-09	56,976	47,627	9,104	2,830	59,561	9,349	(-) 2,585
2009-10	58,431	52,708	8,573	2,290	63,571	5,723	(-) 5,140
2010-11	70,958	64,976	12,436	2,252	79,664	5,982	(-) 8,706

(Source: Finance Accounts of Government of Tamil Nadu)

- During the period 2006-07 to 2010-11, non-debt receipts increased from ₹ 42,515 crore to ₹ 70,958 crore (66.90 *per cent*) against an increase of 98.35 *per cent* in primary revenue expenditure, 108.94 *per cent* in capital expenditure and 94.47 *per cent* in primary expenditure.
- Capital expenditure as a percentage of primary expenditure marginally increased from 14.53 in 2006-07 to 15.61 in 2010-11. Loans and advances as a percentage of primary expenditure decreased from 5.50 in 2006-07 to 2.83 in 2010-11.
- The adequacy of non-debt receipts to meet the primary expenditure led to the emergence of primary surplus during 2006-07 and 2007-08. However, the non-debt receipts were not enough to meet expenditure requirements from 2008-09 onwards, resulting in primary deficit. The primary revenue expenditure and capital expenditure increased by 23.28 *per cent* and 45.06 *per cent* whereas disbursement of loans and advances decreased by 1.66 *per cent* over the previous year.

1.10 Conclusion and Recommendations

Revenue Receipts: During the current year, the State's revenue receipts (₹ 70,188 crore) increased by 25.69 *per cent* over the previous year. The robust growth in revenue receipts was mainly due to improved tax revenue. However, the non-tax revenue (₹ 4,652 crore) of the State decreased by 7.46 *per cent* over the previous year. The State's revenue receipts as a percentage of GSDP marginally declined from 13.17 *per cent* in 2006-07 to 12.83 *per cent* in 2010-11, which indicates that the growth in tax revenue had not kept pace with that of GSDP. ***Concerted efforts to increase the tax revenue by collecting the arrears, disposal of pending assessment etc. and efforts to collect the non-tax resources could improve State finance.***

Revenue expenditure: Of the total expenditure of ₹ 87,604 crore during 2010-11, revenue expenditure (₹ 72,916 crore) accounted for 83.23 *per cent* of the total expenditure. Nearly 71 *per cent* of the revenue receipts of the State were spent on committed expenditure such as interest payments, salaries, pension and subsidies leaving little for other purposes. ***There is a necessity to contain the committed expenditure particularly the salaries and subsidies.***

Capital expenditure: Capital expenditure (₹ 12,436 crore) during the current year increased by ₹ 3,863 crore (45.06 *per cent*) over the previous year and it accounted for 14.19 *per cent* of the total expenditure of the State. However, the ratio of capital expenditure as a proportion of aggregate expenditure in the current year was lower than 2007-08. ***Increased priority to physical capital formation will further increase the growth prospects of the State by creating durable assets.***

Adequacy and priority of expenditure: In the year 2010-11, the State had spent more or less the same proportion of its GSDP on aggregate expenditure as compared to the general category states in the country, implying satisfactory level of adequacy. But the development expenditure (expenditure on social and economic services) as a proportion of the aggregate expenditure in the State had been lower than the general category states, implying low priority. ***The State should plan its expenditure in such a way that the expenditure is uniformly distributed across all services.***

Investment and returns: As of March 2011, the State had invested ₹ 10,222 crore in various Government Companies and Corporations and the outstanding loans and advances due to be recovered was ₹ 8,999 crore. But the average returns from the investments and outstanding loans were only 0.22 *per cent* and 0.94 *per cent* respectively when Government paid an average interest rate of 7.53 *per cent* on its borrowings during 2010-11. ***Government needs to monitor payment of dividends on its investment and repayment of outstanding loans and advances.***

Debt Management: The outstanding fiscal liabilities steeply increased from ₹ 66,320 crore in 2006-07 to ₹ 1,11,657 crore at the end of 2010-11. The State continued to experience a negative resource gap in 2010-11 also and its fiscal deficit as of March 2011 was ₹ 16,646 crore. The net availability of borrowed

funds had decreased from ₹ 7,287 crore in 2009-10 to ₹ 4,375 crore in 2010-11. The continued negative resource gap, reduction in net availability of borrowed funds and continued high burden of interest payments indicate risk of straining of sustainability of debt. *A clear understanding of the maturity profile of debt payment with restricted borrowings will go a long way in prudent debt management.*

Fiscal imbalances: The State experienced revenue deficit in 2009-10 and it continued to be so in 2010-11 with a deficit of ₹ 2,728 crore. The fiscal deficit increased from ₹ 11,807 crore in 2009-10 to ₹ 16,646 crore in 2010-11. Similarly, the primary deficit had been on the increasing trend since 2008-09 and it reached to ₹ 8,706 crore in 2010-11.