# Improving Public Financial Management in India: Opportunities to Move Forward

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**Abstract**

In recent years the role of a sound PFM system to achieve the objectives of fiscal discipline, strategic planning, and improved service delivery has been getting increasing public attention in India. Since public financial management reforms undertaken intermittently over the years, have not delivered anticipated results in these areas, studies and recommendations of Government appointed committees and expert bodies have identified gaps that need attention to strengthen the PFM institutional framework and to improve the efficiency of government spending. This paper examines key PFM reform measures undertaken in India over the past few years and provides suggestions to enhance the effectiveness of these PFM systems. .

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**Keywords: Public Financial Management, Budgeting system, Performance Budgeting, Fiscal Rules, Audit, Accounting,**

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# *Improving Public Financial Management in India: Opportunities to Move Forward*

## 1. Introduction

Finding ways to improve delivery of public services, establishing an accountability framework, and proper implementation of pro-poor policies have remained key concerns in India. India's growth rate of more than 9 percent has declined due to the global financial crisis of 2008-09 and fiscal stress has been building up since then. Although there has been steady decline in the poverty level, more than 300 million people remain below the poverty line[1]. The progress in achieving improvements in human development has been slow and India lags behind several other Asian countries (UNDP, Human Development Report, 2007-08). The Government has expanded the scope of the key central programmes, particularly for social sector spending, it is increasingly apparent that in addition to a pertinent set of policies to address these issues, a sound public financial management (PFM) system that emphasizes institutional efficiency is important to design and implement appropriate polices to achieve the desired results.

While the PFM system appears to be consistent with well-established budgeting, accounting, audit, and legislative control systems (D. Swarup, 1990), recent studies point out that there is still considerable scope to improve the efficiency of government spending and public service delivery by strengthening the institutional framework for PFM. [2]. Reform initiatives to make the budget performance oriented, transition to accrual accounting, adopting rule based fiscal management, and strengthening budget management and expenditure control are noteworthy in this context. Still, not all of these efforts have resulted in enduring changes (Premchand 2008), and increasing demand for better accountability, good governance, and improved service delivery has made it imperative to explore more ways to strengthen India's PFM system. Reform recommendations by Statutory Body like Central Finance Commission and Government appointed Committees like Second Administrative Reform Commission (ARC) and Expert Committee on Expenditure Management in recent years need to be evaluated and implemented to bring in desired changes. The areas in need for reforms as identified by the PEFA report by measuring performance of PFM institutions at the Union level, provides another useful reference for reform initiatives.

This paper examines PFM reform measures that have been adopted over the past few years and proposes ways to enhance the effectiveness of India's PFM system.

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[1] Eleventh Five Year Plan (2007-12) documents mentions that 'the percentage of the population below the official poverty line has come down from 36% in 1993–94 to 28% in 2004–05.

[2] Report of the Second Administrative reforms Commission , "Strengthening Financial management Systems - 2009", and PEFA India report - 2010,

Given the complex nature of PFM, this paper addresses fundamental PFM issues discretely and does not purport to provide a comprehensive reform programme. The rest of the paper is organized as follows. Section 2 deals with various issues related to the budgeting system and Section 3 examines the effectiveness of the delegation of financial powers and the system of financial advisers. Section 4 addresses issues related to transitioning from cash based accounting to accrual accounting. Sections 5 and 6 analyze issues related to internal audit and external audit to enhance accountability. Section 7 outlines concerns with specific intergovernmental transfers and Section 8 notes some institutional changes in PFM that are currently underway and Section 9 contains concluding remarks.

## 2. Budgeting System

### Attempts to Make the Budget Performance Oriented

Given the complexity of budgeting in the public sector where political choice plays crucial role in decision-making, fulfilling the basic objectives of budgeting functions remains arduous and depends heavily on the effectiveness of institutions to achieve better fiscal outcomes. The Indian approach in this context has been to supplement a line-item budget with a ministry-wise performance budget for the same budget session. The general budget presented in the Parliament can best be described as traditional budget (Wildavsky 1978) and displays characteristic problems. This system allows substantial adjustments in the budget during the year indicating the absence of a hard budget constraint (Jena, 2010), particularly since departments surrender substantial amount of unspent money under various programmes at the lapse of the financial year[3]. Unspent provisions are indicative of lack of efficiency in programme management at departmental level in a strict annual budget cycle. Revenue projection has always remained a challenge as the movement of economy and changes in tax administration determine the actual revenue collection.

Since the traditional budget does not provide information on results to be achieved from the use of public resources, one needs to look at the performance budgets of the ministries and departments. The performance budget in India was introduced in 1968 following the recommendations of the first Administrative Reform Commission. The objective of introducing the performance budget as a supplement to the traditional budget was to provide a link between the financial budget of the departments to tangible targets in order to enhance the effectiveness and efficiency of public spending. In addition to lack of adequate preparation and capacity development, major impediment experienced while preparing the performance budget was the absence of realistic performance measurement in terms of developing performance indicators for schemes and projects run by the departments (John Toye, 1981). Over the year it evolved as translation of departmental budgets by incorporating the general physical expectations from the plan schemes run by them. The preparation of performance budget had become a routine affair like compilation of another document without any discernible influence on resource allocation linked with results. .The weakness of the performance budget as practiced over the years became more

[3] Audit reports of appropriation accounts by the CAG bring out these amounts every year.

apparent when the Government decided to adopt another version of performance budget called the Outcome Budget in 2005[4].

The outcome budget has been designed to rise above the traditional line item system to define outcomes for all government programmes[5] and to bring about improvements in the quality of governance[6]. The outcome budget at the Central level is being considered as a model for State Governments to improve the framework for sub-national budgeting[7]. Preparation of outcome budget involves the following steps – defining measurable outcomes, standardizing the unit costs of delivery, benchmarking standards, capacity building for attaining the requisite administrative capacity ensuring necessary funding, effective monitoring, and evaluation and making the system far more intrusive through the participation of the community and the stakeholders[8]. Still, there are multiple difficulties associated with outcome budgeting as well. There are difficulties in measuring outcomes as compared to outputs and ensuring managerial accountability to link funds to outcomes for public programmes. The outcomes could be influenced by many external factors (Shah and Shen, 2007). In addition, establishing a direct link between the level of funding and performance may not be possible due to the role of political concerns and value judgments involved in trade-offs in budgetary decisions (Kelly 2003). Since the regular budget presented in the Parliament is a separate process from the ministry wise outcome budgets tabled later in the budget session, this relationship between the departmental outcome budget and the general budget decisions needs to be strengthened to improve the performance orientation of the budgeting system. An advanced statistical system is also required to collect appropriate data and utilize it to measure the cost of service provision in various sectors. The evaluation of the achievement of last year's results, a feature provided in the outcome budget, can be utilized in its true spirit to get the feedback to improve the policy design and measurement of performance indicators.

The Government of India has also attempted to address the issue of performance management by introducing the 'Performance Monitoring and Evaluation System (PMES)' for Departments in 2009. The PMES provides a framework to measure performance of all schemes and projects run by the departments. The key element of the PMES is the Results Framework Document (RFD), a record of understanding between the departmental Minister and the Secretary of the department, providing physical performance indicators to be achieved during a year[9]. While the RFD does not

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[4] Guideline for outcome budget 2006-07, Ministry of Finance (MOF), "a need has for some time been felt to address certain weaknesses that have crept in the performance budget documents such as lack of clear one-to-one relationship between the Financial Budget and the Performance Budget and inadequate target-setting in physical terms for the ensuing year. Besides, there is growing concern to track not just the intermediate physical "outputs" that are more readily measurable but the "outcomes", which are the end objectives of State intervention."

[5] Outcome budget, Ministry of Finance, 2007-08, "the Outcome Budget is an endeavor of the Government to convert the "Outlays" into "Outcome" by planning the expenditure, fixing appropriate targets, quantifying the deliverables in each scheme and bring to the knowledge of all, the "Outcomes" of the Budget outlays provided for each scheme/programme."

[6] Eleventh Five Year Plan (2007-12), Chapter -10 – Governance, pg 229.

[7] Some of the State Governments have started adopting the outcome budget, which are almost like replica of the Central one.

[8] Ministry of Finance, Department of Expenditure (2007), Guideline for Preparation of Outcome Budget 2007-08

[9] This is to concur the recommendation of the Second Administrative Reform Commission to have an annual performance agreement to be signed between the departmental minister and the secretary of the department on details of works done during the year.

specifically link with the outcome budget, it implicitly settles a debatable issue relating to output versus outcomes by emphasizing that the success indicators are physical achievement of government programmes through which managerial accountability can be ensured[10]. The PMES, properly integrated with the outcome budget, has the ability to boost the much sought after accountability framework in the budgeting system. Strengthening key features of PMES, such as a providing a robust mission and vision statement, designing an incentive system, and increasing transparency in result evaluation would improve its effectiveness. Still, even though the PMES provides for a performance related incentive system, it is still in its evolving stage, and its impact remains to be seen.

**Medium Term Perspective in Expenditure Planning**

Medium-term expenditure planning provides a perspective of projects spreading over a number of years and adjusts expenditure priorities. In India it was maintained that five year plans provide the basis for a multi-year perspective for resource allocation. The feature of breaking up the medium term five year plans into annual plans and integrating them annual budgets and further monitoring of their progress was an important innovation (Thimmaiah, 1984). The development planning-budgeting link in India, however, has not been smooth. While plans provide conceptual framework by focusing on various sectors in the economy, the budget is more concerned with systems of control over the use of funds by government and pay more attention to financial aspects (Premchand, 1983). In the current budgetary practice, the link between the plan and the budget is tenuous. Planned goals, objectives, outputs, and resources allocated to achieve them are not adequately integrated into the annual budgets. The basic feature of plan allocation through schemes and sectors does not remain the same when the budget is prepared under different heads and sub-heads following the existing budgeting classification. It is therefore, difficult to link the plan objectives of various schemes/projects to budgetary practice of allocating resources under various heads. It takes considerable effort to link objectives of the various schemes/projects to the expenditures under various heads and sub-heads[11].

Even though a fully programmatic MTEF requires developing and prioritizing expenditure plans and budgeting for results within the available resources, the experience of introducing MTEF in developing countries indicates it to be a costly affair without much of the perceived benefits (Salvatore 2009). Therefore, in 2011 the high level Expert Committee on Expenditure Management opted for a realistic approach more suited to India. It recommended removing the plan and non-plan distinction from the expenditure classification, and suggested taking a holistic view of expenditure for budgeting in a multi-year mode. The Committee also suggested developing a 3 year expenditure framework to be updated in the light of resource availability, with sectoral priorities and performance. The key feature of this plan is that the Ministry of Finance would estimate the budgetary resources and indicate the ceilings to ministries on three year rolling basis.

**Fiscal Rules and Budget Management**

[10] Guidelines for Results Framework Documents (RFD) 2011-2012, Cabinet Secretariat, GoI
[11] Government of India, Planning Commission, (2011), Report of the High Level expert Committee on efficient Management of Public Expenditure

The Fiscal Responsibility and Budget Management Act (FRBM) was adopted in 2003[12] in response to severe deterioration of public finance both at Central and State levels in late nineties and failure to salvage the situation through discretionary policy actions (Rao and Jena 2009, 12th FC, pp. 62). The combined (both Centre and States taken together) fiscal deficit crossed 9 per cent of GDP and debt-GDP ratio grew considerably with slowing down of the economy during early part of 2000s. The FRBM act was adopted with the objective to reduce fiscal deficit to GDP ratio at 3 per cent both by Central and State Governments by 2008-09 and to balance the current account, and to maintain long-run fiscal sustainability and prevent an increase in future indebtedness.

Post FRBM fiscal developments reveal that the success of fiscal rules was closely related with the growth performance of the country necessitating revision when the economy slowed down. Close scrutiny of fiscal data shows that significant improvement in the fiscal situation in the country since 2003-04 was mainly revenue driven, particularly due to income tax, riding high on buoyant economy and modernization of tax administration (Rao et al 2008). The consolidated gross fiscal deficit relative to GDP declined from 9.9 per cent in 2001-02 to 6.4 per cent in 2006-07 and further to 5.4 per cent in 2007-08. On the expenditure front, however, barring decline in interest payment due to debt swap programme and decline in interest rates, not much restructuring was evident. The real test of the fiscal rules came during 2008-09, when the national growth rate slowed down sharply to 6.7 per cent from an average of 9.4 per cent in the preceding three years, because of the international financial crisis. This has triggered an expansionary fiscal stance by the Central Government through fiscal stimulus packages comprising both tax cuts and expenditure hikes (Economic Survey, 2008-09, pp 35). The targets of the fiscal rules were considerably breached in the terminal year of the fiscal consolidation path as the combined fiscal deficit rose to 8.5 per cent of GDP in 2008-09 and further to 9.4 per cent in 2009-10.

Although fiscal stress has not been eased since the global economic slowdown of 2008-09, the Government has reemphasized the need to continue with fiscal rules by extending the time line and redefining the parameters. The revised road map for fiscal consolidation was suggested by the Thirteenth Finance Commission with an extended time horizon up to 2014-15 emphasizing curtailment of debt stock and fiscal deficit consistent with it[13]. The fiscal prudence requires political commitment without which it becomes difficult to adhere to fiscal rules for a long period (Von Hagen, 2007). The fact that the fiscal rules have been operating both at Central and State level in India and the Government has opted to reinvent it in difficult time, fixed constraints seems to have gained political acceptance. The reasons for the shift from a disciplined fiscal posture to large deficits in 2008 have been economic in nature. The Indian experience shows that automatic reduction in revenue collection and rise in expenditure through the stimulus package in the difficult year of 2008 produced large and unplanned deficit in excess of the level stipulated by the FRBM Act. While the modification in fiscal rules was necessary, it does not assure adherence on the face of adverse economic conditions in

[12] The central Act was followed by the sub-national Governments enacting FRBM Acts separately.
[13] The revised road map for fiscal consolidation charted by the TFC, which targets fiscal deficit consistent with debt-GDP ratio, was laid down as the fiscal roadmap by amending the FRBM Act for the next five years. In the fiscal restructuring plan the consolidated debt to GDP ratio is targeted to decline from 78.8% in 2009-10 to 67.8% in 2014-15. In line with this, the fiscal deficit is supposed to be reduced from 9.5% to 5.4% during the same period. The central government is required to reduce its outstanding debt to GDP ratio from 54.2% in 2009-10 to 44.8% in 2014-15, its fiscal deficit from 6.8% to 3% and its revenue deficit from 4.8% to a surplus of 0.5%.

the future. The tendency of expanding the scope of populist Government programmes and subsidies, which have large expenditure commitments in the future years, needs to be restricted to emphasize fiscal discipline.

## 3. Role of Integrated Financial Advisors in Financial Management

Through delegation of financial powers from the Ministry of Finance to agencies, the departments enjoy considerable freedom to spend their own budget allocations and maintain the accounts. To support the departments to exercise the enhanced powers delegated to them, a system of Integrated Financial Advisors (FA) was developed. This institutional form has assumed crucial role in developing financial management capability of departments spanning over policy formulation and implementation to functional oversight on accounting and budgeting aspects. While assisting the departments in achieving their goals and ensuring value for money, the FAs also act as representatives of the Ministry of Finance in all financial matters. Indeed balancing the dual role, advising the Secretaries of the departments and acting as 'eyes and ears' of the Ministry of Finance is a difficult job for the FAs.

The role, authority, as well as accountability of the Financial Advisers were revised through a charter in 2006 to enhance their capacity to meet the challenges associated with this role[14]. Redefining the charter, as the official memorandum indicates, was intended to assist the departments in achieving their objectives, facilitating implementation of the approved programmes with due financial prudence, ensuring the monies allocated were spent on time and in prescribed manner, and ultimately ensuring `value for money'. The responsibilities assigned to the FAs through this revised charter have been ambitious since they include most of the financial activities starting from performance budgeting (outcome budget), expenditure control and cash management, to project formulation and appraisal and monitoring and evaluation functions. The revised charter has raised many questions regarding the expectations from FAs since the expansion of responsibilities does not match with existing powers and support systems. Since the effectiveness of the role of Financial Advisors is circumscribed by the management framework within which they function, addressing these concerns exclusively with FAs would not be too helpful. Rather, capacity building and support from the administrative ministry would be more helpful. In India, there is no separate cadre of Financial Advisers, and it should be recognized that financial management in the public sector can no longer be treated as a function of generalist officers. The lack of attention to the technical and professional skills of FAs compares unfavorably with the heavy and technical nature of responsibilities required of them.

## 4. Efforts to Adopt Accrual Accounting

In India, most government accounts are maintained on a cash basis, which is deficient in not being able to provide the complete picture of the financial position of the Government. It lacks complete information on assets and liabilities, and therefore makes

[14] Ministry of Finance, Office Memorandum of F(5)/L&C/2006 dated 1.6.2006

it difficult to ascertain the total cost of services provided by Government departments[15]. In 2005 the Government of India accepted the Twelfth Finance Commission's recommendation to switch to an accrual based accounting system. The Government entrusted the GASAB (Government Accounting Standards Advisory Board) to prepare a detailed roadmap and an operational framework to adopt accrual based accounting system.[16] While the benefits from using accrual accounting in the Government sector have been widely mentioned (Blondal, 2003, Paul Boothe (2007), Athukorala and Reid 2003), inadequate administrative capacity and skills required for bringing about such a major reform in accounting system and the high costs involved in its implementation and maintenance are cited as major impediments (Diamond, 2006: a). The benefits of accrual based accounts and reports have not been clearly established in practice. In the context of accrual accounting system concerns range from technical issues like valuation of assets to broader questions regarding differences in the requirements of the public sector versus the private sector and administrative accountability (Wynne, 2004). The susceptibility of cash accounting to manipulations of financial statements by managing the timing of transactions is considered as key criticism. However, the scope for manipulation in accrual accounting is also there in the formation of estimates of revenues and expenses due to considerable scope for judgment (Hepworth (2003). There is still limited unanimity at the political and administrative level, even after taking a principled stand to introduce accrual accounting, due to apprehensions regarding risks involved, likely costs involved, and requirement of administrative capacity.

A stage-by- stage approach to introduce accrual accounting is often advocated. The GASAB roadmap to introduce accrual accounting system envisages a transition period of 10 to 12 years divided into several stages. The operational framework details the plan of transition encompassing accounting and treatment of assets, liabilities, revenue and expenses and the final accounts of the Government consistent with the provisions of the Constitution. Progress seems to have been made in the case of Urban Local Bodies where introducing the accrual accounting system has gained momentum. The Comptroller and Auditor general of India (CAG) prepared National Municipal Accounting Manual incorporating the principles of accrual accounting in a stage-wise approach. Many State Governments have also shown interest in this direction. Some of the State Governments have adopted a double entry accounting system for their rural local bodies, which is amenable to conversion to accrual basis. Still, systematic efforts need to be made over a number of years to implement accrual accounting. Helpful steps to achieve this would include imparting necessary training, recruiting suitable professionals, preparation of accrual accounting manuals, getting together comprehensive data regarding assets and liabilities, establishing suitable accounting standards and norms, and using information and communication technology.

## 5. Updating the Internal Audit System

One of the main weaknesses of the internal audit system in India is that it has not kept pace with emerging international standards and practices (Ghosh and Jena, 2008). The modern concept of internal auditing goes far beyond its traditional limits. Internal audit is no longer considered as a mere routine review of financial and other records by

[15] See "Primer on Accrual Accounting", Government Accounting Standards Advisory Board (GASAB

[16] Operational Guidelines for Accrual based Financial Reporting in Government, 21 June 2011

specially assigned staff. The internal audit is emphasized as a management tool and an integral part of both management controls and communication processes (Diamond 2006).Internal audit is still conducted based on departmental codes and manuals, which are a legacy of the past. These codes mainly emphasize regularity audit and does not encompass management audit and operational audit, they also do not evaluate internal control systems of the units under audit or bind the audited entity to take action on the observations and recommendations of the internal audit.

The concern regarding role and function of internal audit led the Government to constitute a Task Force in 2006 to benchmark the status of internal audit in the Central Government and outline a roadmap for its improvement. The Task Force came to the conclusion that due to severely restricted mandate and lack of interest of the management, the internal audit has not been able to systematically evaluate the risks associated with various activities of the ministry/department for determining their audit strategies and thrust areas. There was no segregation of duties especially at supervisory levels between those who are responsible for internal audit and those responsible for pre-audit, disbursement and accounting functions suggesting lack of required independence for effective functioning. The recommendations of this Task Force subscribed to the modern view that internal auditing should not be restricted to financial issues alone, but should also extend to issues like cost benefit analysis, utilization and deployment of resources, matters of propriety, effectiveness of management etc. and the focus should be on risk, control and governance issues. It also provided other multiple recommendations including: segregating duties relating to internal audit from those relating to financial advice and accounting functions, setting up an Apex Board to prescribe internal audit standards and processes across jurisdictions, legislating internal audit standards and policies, establishing a Board of Internal Audit (BIA), and ultimately, appointing a Chief Internal Auditor (CIA) trained in auditing. The CIA would function in accordance with standards and procedures prescribed by BIA.

## 6. External Audit

The external audit by the Comptroller and Auditor General of India (CAG) has played crucial role in India and assisted the Parliament in exercising financial control over the executive. The recent performance audit reports by the CAG have raised nationwide debate on corruption in Government and the necessity of adopting strong measures to improve the accountability of the executive and the elected representatives. Two recent incidents include the license and allocation of the 2G spectrum by the Department of Telecommunications, and the performance audit of the Commonwealth Games 2010[17]. The CAG derives the position and authority in relation to the external audit from the Constitution of India[18], which ensures independence and autonomy of the public audit. The Parliament scrutinizes the audit reports through a committee called the Public Accounts Committee (PAC). The external audit by the CAG has contributed to

[17] Report No. -19 of 2010-11 for the period ended 2009-10 Performance Audit of Issue of Licenses and Allocation of 2G Spectrum by the Department of Telecommunications ( Ministry of Communications and Information Technology
Report No. - 6 of 2011-12 for the period ended 2010-11 - Performance Audit of XIXth Commonwealth Games 2010

[18] The duties and powers of the CAG are enshrined in Articles 148 to 151 of the Constitution and set out in the CAG's (Duties, Powers and Conditions of Service) Act, 1971.

transparent financial management by raising audit observations repeatedly relating to budgetary controls, deficiencies in revenue collection, wastage of public resources, inappropriate accounting, poor returns on investments, diversion of funds, and system deficiencies. The Second Administrative Reform Commission (ARC) in its report on financial management in the country, however, raised several issues relating to the external audit. It pointed out that, though the powers conferred on CAG are wide, they are not explicit. The other issues indicated by the ARC include improving timeliness of audit reporting, improving audit procedures to reflect the executive accountability, prescribing corrective actions for detected irregularities, carrying out risk analysis to highlight systemic issues and analyze causes in entirety, establishing operational synergy with the internal audit system of the departments. The ARC also expected the CAG to play a key role in the audit process of the decentralized governance in the country. These issues are important for effective functioning of the Supreme Audit Authority.

Effectiveness of external audit largely depends on the interest it evokes and support it obtains from the Public Accounts Committee (PAC), a parliamentary committee scrutinizing the audit observations. The functioning of PAC over the year has shown that the percentage of audit observations (paras) being discussed in PAC has been reducing. The Ministries and Departments take only those audit paras seriously which were scrutinized by the PAC. Most important there is no law which binds the audited ministries/departments to follow up with actions recommended by the CAG. As a result the replies in the form of ‘action taken’ reports by the audited units come with a substantial time lag. Even when the Action Taken Notes are submitted, these are largely formal rather than substantive. While external audit has been a strong element of Indian PFM system, the follow-up process needs improvement to enable the external audit system to play its desired role.

## 7. Intergovernmental Transfers and PFM Concerns

The Intergovernmental resource transfer system in India continues to be complex, which involves several conduits like the Finance Commission, Planning Commission and several Central Ministries. In addition to devolution of central taxes determined by the Central Finance commission and plan assistance determined by the Planning Commission of India, Centrally Sponsored Schemes (CSS) have emerged as a key source of funds in social and economic sectors for States. These are specifically designed programmes for employment generation, primary education, basic health services and rural infrastructure and run by the concerned central ministries. The CSS form part of the Central Plan as they are meant to provide additional resources to the states for implementing programmes that are considered by the Government of India to be of national/regional importance. Over the years the CSS has become an important tool of the central Government to influence polices and expenditures on subjects constitutionally allocated to the States. The funds under these programmes are provided in respective budgets of Central Government Ministries, implemented at state level by specifically created implementing agencies and rural local bodies. The budgetary provision for direct transfers to implementing agencies has increased from Rs.1890 billion in 2010-11 to Rs.1246 billion in 2011-12[19].

[19] Expenditure Budget, Vol – I, 2011-12, Ministry of Finance, GoI

The PFM concerns are many in this type of funding through central programmes. The funding of the big ticket CCS bypass the state budgets and are routed through implementing agencies such as missions or autonomous societies created under the provision of the specific schemes, and local bodies. A direct transfer of resources to state budgets would seem to have merit in terms of accountability. However, apprehensions regarding timely release of central funds by the States to the designated central programmes led to creation of implementing agencies in States and directly routing funds to their bank accounts outside state budgets. This funding arrangement is considered efficient so far as fund utilization is concerned in a timely manner. Although state functionaries predominantly man these agencies, the financial management of the implementing agencies remains outside the formal accountability structure of both the central and state governments. Mere release of funds to the agencies at central level is considered as expenditures, which is not reflected in the state budgets. A certain level of utilization in the form of an unaudited certificate is needed for the next level of funding. Rather than the CAG, the empanelled chartered accounts audit such bodies. The information on availability funds and actual expenditure by the service delivery units, a school or a health service unit, at the far flung areas is sketchy. Given the diversity in the implementation hierarchy, the number of implementing units and the geographical reach of central schemes, it has remained a challenge to have meaningful information on these schemes and support informed planning. Further many a times these programmes are caught in political tangle as regards their ownership and accountability in delivering services.

The newly launched Central Plan Monitoring System has attempted to address deficiencies in the existing accounting system for the CSS and its inability to support informed planning, budgeting, and effective monitoring. This web-enabled application has features to map flow of funds, releases and expenditure details, payment to the ultimate beneficiary through banking channels, and enhance report generation capabilities integrated into the transaction databases. In spite of this effort to reinforce the information base of the central plan schemes, the overall financial management of CSS and its integration with the State level systems continues to be weak. The performance management framework in CSS is stretched over various agencies starting from the central to State Government for which monitoring the service delivery and fixing accountability for results has become difficult. Therefore, there is an increasing demand for direct routing of funds under these flagship programmes through State budgets. The Expert Committee on expenditure management has also favored this arrangement to bring these schemes under the mandated financial control of the Government.

## 8. Institutional Changes underway for Better PFM

There have also been attempts to improve the institutional framework in some other areas. The Government's establishment of the Debt Management Office in the Ministry of Finance is an attempt to delink debt and cash management from monetary management controlled by the Reserve bank of India and to change the existing debt management system. The independent debt management office is expected to formulate a long term debt management strategy consistent with sustainability requirements, create an annual borrowing calendar, forecast cash and borrowing requirements, formulate risk management strategy, and develop and disseminate debt related information and data.

Another initiative to pursue a sustained dialogue on fiscal policy and to promote independent review and monitoring of the implementation of various measures is the creation of a Fiscal Council, as recommended by the Thirteenth Finance Commission. . This Commission recommended that a committee should be established to review and monitor the implementation of the FRBM process[20], and to, over time, evolve into a full-fledged autonomous Fiscal Council to assist the Government in addressing its fiscal tasks in a professional, transparent and effective manner. The Commission has referred to examples of such pertinent institutional measures in many countries like Brazil, Japan, Korea, Mexico, and Sweden. The Fiscal Council is expected to become a forum to facilitate implementation of PFM reforms.

Changes are also expected in the area of procurement by various ministries and departments. With the exception of the rules and directives in the General Financial Rules (GFR), 2005, there is no law that governs public procurement exclusively. These rules indicate that the ministries or departments have full power to make their own arrangements to procurement goods. With the exception of limited control and oversight functions carried out by the Central Vigilance Commission (CVC), there is no central authority exclusively responsible for defining procurement policies and for overseeing compliance with the established procedures. Acknowledging the weakness in procurement process, the Central Government is planning to pass legislation to regulate public procurement by all Ministries and Departments of the Central Government. While the draft bill prescribes an open competitive bidding as the preferred method of procurement, for low-value procurement the existing methods of procurement as specified in the GFR will continue This legislation, once passed, is expected to improve transparency and accountability. It includes provisions that emphasize publishing procurement details in a web-based format starting from the bidding stage to the ultimate award of contracts. The bill also endorses establishing appropriate grievance redressal procedures and anti-corruption mechanisms. While a central Law for procurement is always better than rules and executive decisions dispersed across the departments, its usefulness will depend on the extent to which it is heeded and monitored.

## 9. Concluding Remarks

While the reform initiatives undertaken to strengthen PFM institutions over the years in India have yet to meet their full potential, they underline the intent of the Government to boost the efficiency and effectiveness of the system. There are gaps and unfinished agenda that need further action and refinement. These include producing suitable performance measures that will influence budgetary decisions; continuing with

[20] Report of Thirteenth Finance Commission, Chapter – 9, pp: 137

existing efforts to expand accrual accounting, modernizing internal audit and control, improving the effectiveness of external audit, and introducing an exclusive procurement law. . In contrast to the intermittent nature of past efforts, the future agenda should focus on continuously evaluating the outcome of these changes in order to take corrective action as soon as possible. At the same time, expectations of immediate results from these reforms may be misplaced. There is always a time lag for institutions to deliver expected results. In a large country like India where the fiscal federal nature of the country puts large functional responsibility on sub-national Governments, a coordinated approach is needed to focusing the ability of the PFM system in delivering quality services at the State level. The capacity and willingness to internalize and change at State level, and political involvement and willingness to steer the changes are also key to facilitate the reforms.

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