

ANNUAL SURVEY OF INDIA'S CITY-SYSTEMS

Municipal Finance Brief

October 2017

The Annual Survey of India's City-Systems (ASICS) evaluates the quality of city systems in India across 18 states. ASICS serves as a diagnostic to identify the systemic issues preventing cities from providing good quality of life to their citizens. Urban planning & design, urban capacities & resources, empowered political leadership and transparency, accountability & public participation are the four city-system components covered under ASICS. The ability of Urban Local Bodies (ULBs) to invest adequately in providing infrastructure and services to its citizens is one of the key diagnostic parameters assessed by ASICS. This brief – a precursor to ASICS 2017 – analyses the financial management of ULBs and presents key insights on the state of Municipal Finances based on the audit reports of the CAG on their audits of ULBs in 21 states. Pursuant to recommendations of the 13th Finance Commission (FC), state governments have transferred technical guidance and supervision of the audit of local bodies to the CAG. The CAG undertakes annual audits of local bodies, both ULBs and PRIs, on a sample basis. These reports are presently the only comprehensive and regular source of information on the financial position and financial performance of ULBs in India.

This brief provides 5 insights and recommendations on analysis of the data sets from CAG audit reports. Insights have been drawn from analysis of the following three critical data sets from the CAG audit reports:

1. Own Revenue of ULBs
2. Status of Accounts of ULBs
3. Status of Audits of ULBs

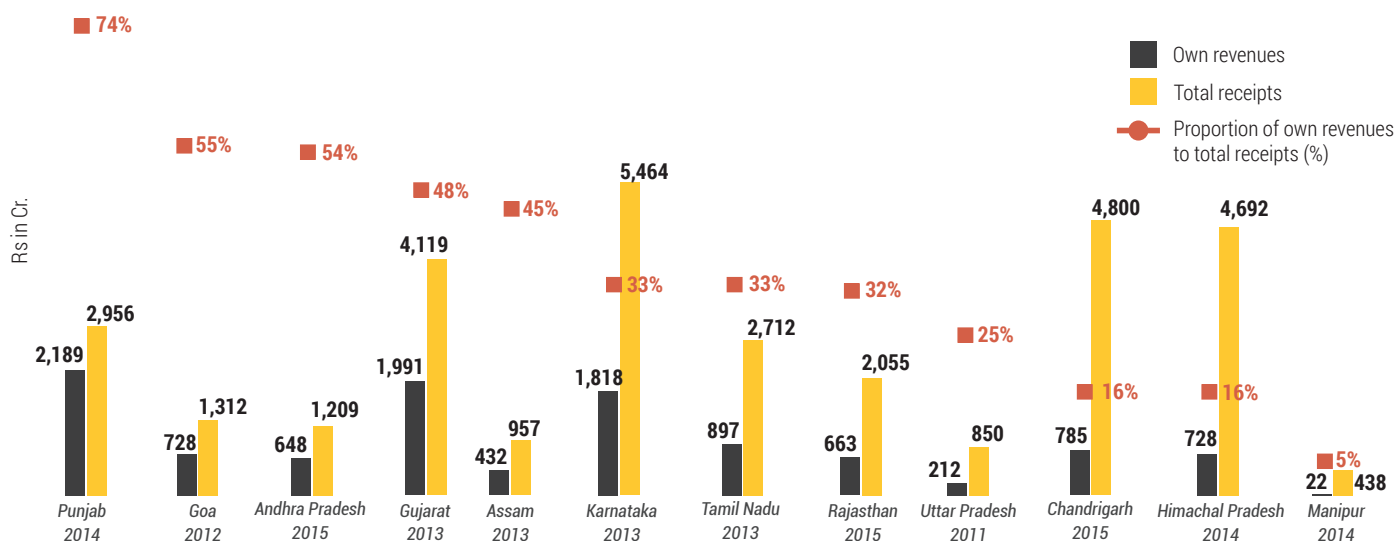
INSIGHT #1:

Own revenues on average contribute to less than 37% of the total receipts of ULBs, ranging from a low of 5% in Manipur to a high of 74% in Punjab; only 3 states record > 50% share of own revenues

Impact:

ULBs depend on State and Central grants to a significant extent, constraining their ability to make capital investments to improve infrastructure services and other investments to improve their functioning.

Per capita own revenue and per capita total receipts of urban local bodies across states



Source: CAG reports

Out of 21 states, data on proportion of own revenues and per capita total receipts of ULBs was available only for 12 states

Recommendation:

- ULBs need to improve collection efficiencies of own revenues, mainly, property tax, advertising tax and parking fees.
- Buoyant sources of revenues such as stamp duties and entertainment taxes should be devolved to ULBs.
- States need to embark on systematic fiscal decentralisation.

INSIGHT #2

On average (across 12 states), ULBs of capital cities spend 253% higher per capita, on infrastructure and services, as compared to average per capita spend by all ULBs in the corresponding states

Impact:

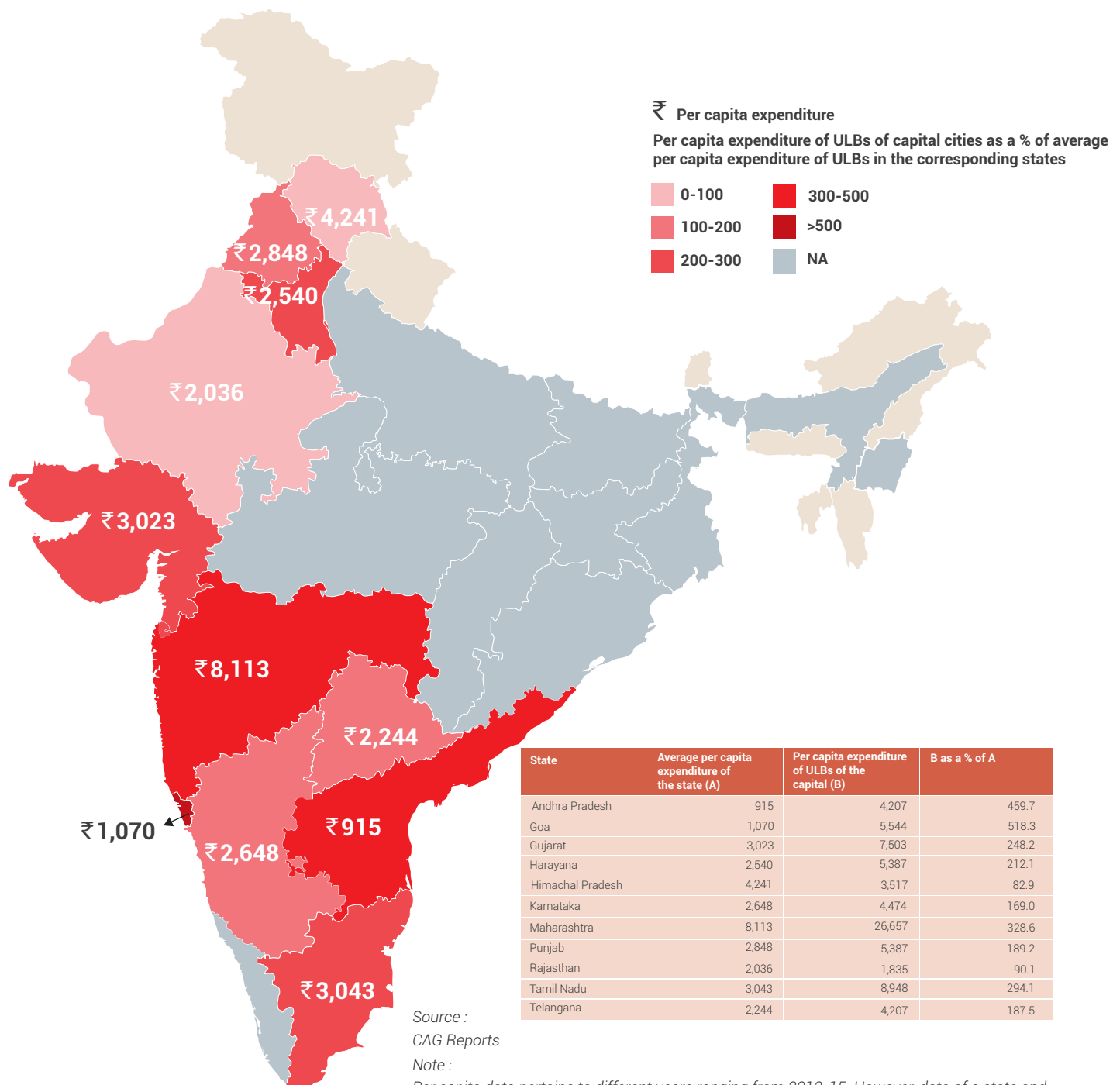
This indicates lower per capita spend across smaller cities, resulting in poorer quality of life in such cities.

Recommendation:

The focus, currently concentrated only to large cities, must also shift to the smaller cities and towns in order to bridge the gap in per capita spend, by -

- improving collections of own revenues of the ULBs in smaller cities and towns
- devolving buoyant sources of revenue such as stamp duties and entertainment taxes should be devolved to ULBs, and
- increasing grants devolved to smaller cities and towns to meet the infrastructure needs.

Per capita expenditure of ULBs of capital cities versus average per capita expenditure of all ULBs in the corresponding states



INSIGHT #3

Significant delay in preparation of Accounts and Audit of ULBs across states, inability to ascertain accurate financial position and performance of ULBs

Impact:

Constraining the ability of state governments to hold ULBs accountable and of ULBs themselves to take informed decisions or raise funds from the capital markets.

Recommendation:

To clear the pendency in accounts and audit, States should actively consider empanelling Chartered Accountants. Karnataka, Bihar, Chhattisgarh, Gujarat, Odisha and Rajasthan are among the states that have empanelled Chartered Accountants to clear the backlog in audit and accounts.

State	Total No of ULBs	Pendency in audit*	Pendency by year	Pendency in preparation of Accounts	Pendency by year
Andhra Pradesh	110	NA	NA	25	From 2016
Gujarat	187	339	2010-11 (5), 2011-12 (167), 2012-13 (167)	159	NA
Karnataka	275	173	NA	132	From 2015-16
Maharashtra	265	139	2012-13 (23), 2013-14 (116)	NA	NA
Tamil Nadu	664	122	2013-14 (122)	707	2012-13 (3), 2013-14 (52), 2014-15 (652)
Telangana	68	41	NA	NA	NA
Uttar Pradesh	630	NA	2008-09 (38), 2009-10 (67), 2010-11 (82)	187	NA
West Bengal	130	NA	NA	658	From 2012-13 (as on 31.03.2014)

Source –CAG Reports

Note: 1. Data on pendency in audit/account preparation is available only for states mentioned above.

2. *Audit by the state audit department.

- The NITI Aayog's three year Action Agenda recommends that the introduction of **standardized, time-bound, audited balance sheets** across 4,041 ULBs would help **improve financial management** as well as spur further reforms in the area of Municipal Finance.
- Publishing of Audited Financial Statements is one of the mandatory conditions for availing performance grants as per recommendations of 14th Finance Commission as well as a mandatory reform under AMRUT.

INSIGHT #4

Over 33,198 unanswered audit observations from CAG Audits across 16 states, relating to several thousand crores in financial terms; no implications for open audit observations

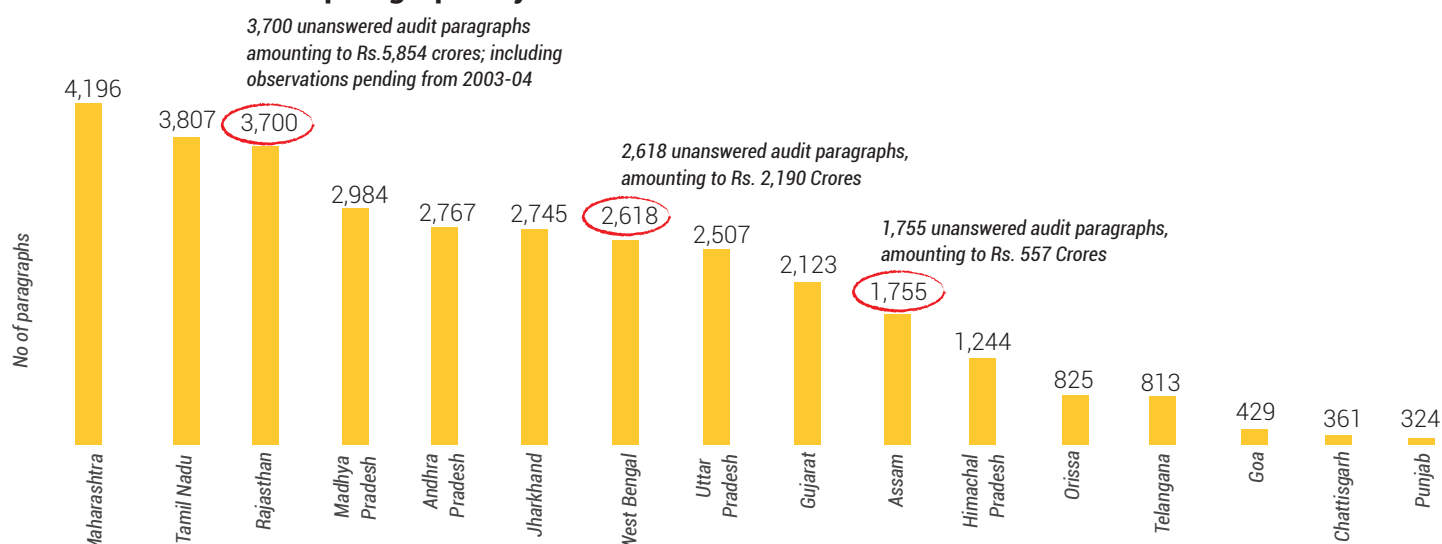
Impact:

Open audit observations are a sign of weak internal controls and poor financial hygiene in ULBs, exposing them to frauds and losses.

Recommendation:

Time-bound, transparent responses to CAG audit observations to be mandated in Municipal Corporation Acts, central and state grants to be tied to performance in audits and responses to audit observations.

Unanswered audit paragraphs by state



Source: CAG reports

INSIGHT #5:

Significant backlog in CAG audits of local bodies undermining quality of TG&S by CAG

Impact:

CAG audits are the last line of defence around internal controls in ULBs. Delays in CAG audit reflects lackadaisical approach to the audit process.

Recommendation:

Fix accountability for submission of financial records of ULBs on time to CAG; make transparent time table of CAG audits and reasons for delays in CAG audits.

Year for which latest CAG report is available	No of States	States
2016	4	Andhra Pradesh, Assam, Karnataka, Telangana
2015	9	Chhattisgarh, Himachal Pradesh, Maharashtra, Punjab, Rajasthan, Tamil Nadu, Madhya Pradesh, Bihar, Kerala
2014	2	Manipur, West Bengal
2013	2	Gujarat, Haryana
2012	1	Goa
2011	2	Uttar Pradesh, Jharkhand
2010	1	Odisha

Source: CAG reports



JANAAGRAHA CENTRE FOR CITIZENSHIP & DEMOCRACY

Janaagraha Centre for Citizenship and Democracy is a Bengaluru based not-for-profit having the mission of transforming quality of life in India's cities and towns. It defines quality of life as comprising quality of citizenship and quality of infrastructure and services. It works with citizens to catalyse active citizenship in neighbourhoods and works with governments to institute city-system reforms to city governance in India. Janaagraha's City-Systems framework comprises four components: Urban Planning and Design, Urban Capacities and Resources, Empowered and Legitimate Political Representation and Transparency, Accountability and Participation. Municipal Finance is an integral part of the Urban Capacities and Resources city-system component.

Acknowledgement : We would like to acknowledge the contributions made by Bharathy Jayprakash and Kartika Nair in the preparation of this brief.