

Reorganisation and Strengthening of the Indian Public Audit System – Reforms Overdue

T Selvaraju*

Abstract

The objective of this study is to ascertain whether the Comptroller and Auditor General of India (the Supreme Audit Institution of India) functions as per its given mandate, and whether it requires any reorganisation and further strengthening. There is conflict of interest in keeping the accounts for States and auditing them by CAG, with potential scope to adversely impact the quality of both accounting and auditing. Further, ever since 1976, CAG continues to perform entitlement functions for employees of a majority of States, without any statutory authority, thus incurring irregular expenditure. With the present level of audit coverage, all the auditable units by CAG could not be covered in a way that can provide an assurance as to the completeness and timeliness of audit. The susceptibility of public finance to the political regime, the meagre rate of expenditure (about Rs. 32 for checking of financial transactions worth Rs. 1,00,000), and significant recovery of public money at the instance of audit provide adequate justification for strengthening of audit with more human resources. Thus, reorganisation of the institution of CAG to make it an exclusive audit institution, along with strengthening it (with adequate human resources) would better serve the objective of its creation.

Keywords: Reorganisation of IAAD, Conflict of interest, Ultra-vires action of CAG, Compliance audit, Strengthening of audit

Publication Date: 27 November 2022

* T Selvaraju is a retired Senior Deputy Accountant General from IA&AS

1. Introduction

Public Audit in India is carried out by the Comptroller and Auditor General of India (CAG), who heads the Indian Audit and Accounts Department (IAAD). The CAG audits all Union and State/Union Territory government offices and Central and State public sector enterprises, government autonomous bodies, and organisations significantly financed by the governments. The CAG submits their Audit Reports to the Parliament or the State/UT Legislature, depending on the entities covered in the report.

The CAG also prepares, audits, and presents Finance and Appropriation Accounts of State governments to the respective State legislatures, besides certifying the Finance and Appropriation Accounts of the Union government.

Apart from the above audit and accounting functions, entitlement functions for many State governments are also carried out by IAAD. Entitlement functions refer to maintenance of General Provident Fund accounts of government employees, authorisation of final closure of GPF accounts and pension payments on their retirement and maintenance of service sheets and issue of pay slips of some Gazetted employees. The CAG is the sole institution with the mandate and powers to audit governments in India. They are to discharge their duties as per the Constitution of India and the CAG (Duties, Powers and Conditions of Service) Act, 1971. In this study, we aim to ascertain (i) whether the CAG functions in accordance with its given authorities and mandate, and (ii) whether there is any need for reorganisation of IAAD and Public Audit practices in India.

2. History of IAAD

A brief history of the institutions of the CAG and IAAD is given below, for proper appreciation of legislative intentions and Constitutional expectations from them:

2.1 Pre-Constitution position

A post of 'Accountant General' was created by the East India Company. This position, with added function of audit, was continued as the Accountant General to Government of India (1858), Auditor General of India (1860), Comptroller General of Accounts (1866), Comptroller and Auditor General (1884), Auditor General in India (1919) and Auditor General of India (1935) under a series of Indian Councils Acts / Government of India Acts.

As per the Government of India Act (1935):

- The Auditor General of India (AGI) should perform such duties and exercise such powers in relation to the accounts of the Federation and of the Provinces, as may be prescribed (Section 166),
- The Federation's and the Provinces' accounts should be kept in such a form as may be prescribed by the AGI, with approval of the Governor General (Section 168), and

- The Audit Reports of AGI should be submitted to the Governor General of India or the Governor of the Province, who should cause them to be placed in the Federal Legislature or the Provincial Legislature, as the case may be (Section 169).

The AGI's functions were further regulated by Ordinances, orders, bye-laws, rules or regulations made by the Governor-General, under the powers conferred upon him by the Act. The Government of India (Audit and Accounts) Order, 1936, issued under the Act, entrusted the work of keeping the accounts of the Dominion and the Provinces, other than that of Defence and Railways of the Dominion, to the AGI. The Order, however, gave powers to the Governor General/the Governor to relieve the AGI from the responsibility of keeping the accounts of any service or department and of any class or character.

Thus, while audit was made an inherent function of AGI, the accounting function was entrusted to them only as a temporary arrangement; it could be withdrawn, by executive orders, at any time.

2.2 Expectation of the Constitution Assembly

The concerns of the Constituent Assembly were mainly about Audit function of CAG of India (adopted on 30 May, 1949 in lieu of AGI), as may be noted from the following speeches during discussions held therein.

(i) Dr B Pattabhi Sitaramayya:

“...no matter how perfect the Constitutions may be, no matter how numerous may be checks and balances and safeguards for the right conduct of business of the future, it is money that counts, and we have to deal with about 370 crores at the Centre and as much money in the Provinces, and if all this money is not spent aright, and if the people deliver cheap gibes at men like me who count rupees, annas and pies, and to who, every rupee means 16 annas and every anna means 12 pies, then there is no government at all worth mentioning, it is anarchy, it is chaos. It is loot. It is dacoity. And who is to control this? Is it to be man who is appointed by the Ministry that should control this? No. The Comptroller and Auditor General must be as supreme and independent as the Judges of the Supreme Court... perhaps even more so. He is not merely an Accountant-General, but he represents a judicial authority with a judicial frame of mind, and his acts must be acts of justice between what he considers to be right and what is actually done by the executive. At times he is called upon to criticise the executive and to expose it even to contempt. He should not therefore, come under the ire of the government or of any party or of the treasury or of the Finance Department. ...” (Constituent Assembly Debates, Volume XI, November 25, 1949).

(ii) Dr. Rajendra Prasad, the President of the Constituent Assembly:

“... Another independent authority is the CAG who will watch our finances and see to it that no part of the revenues of India or of any of the States is used for purposes and on items without due authority and whose duty it will be otherwise to keep out accounts in order, when we consider that our governments will have to deal with hundreds of crores, it becomes clear how important and vital this department will be.” (Constituent Assembly Debates, Volume XI, November 26, 1949).

(iii) Shri R.K. Sidhva:

“... The Auditor-General should be always independent of either the legislature of (or) the executive. He is the watch-dog of our finance... his position must be made so strong that he cannot be influenced by anyone, howsoever great they may be” (Constituent Assembly Debates, Volume VIII, May 30, 1949).

(iv) Dr Ambedkar:

“... I am of opinion that this dignitary or officer (CAG) is probably the most important officer in the Constitution of India. He is the one man who is going to see that the expenses voted by Parliament are not exceeded, or varied from what has been laid down by Parliament in what is called the Appropriation Act.” (Constituent Assembly Debates, Volume VIII, May 30, 1949).

The founding fathers of the Constitution included suitable service conditions of CAG for ensuring its functioning independent of the Parliament and Executive; however, they left the CAGs duties and powers to be decided by the Parliament to come, and only enabled the CAG to continue to perform such duties and exercise such powers as were conferred on or exercisable by the AGI immediately before the commencement of the Constitution (Article 149¹).

2.3 Post-Constitution position

As per Article 149 of the Constitution, the CAG continued the duties which they had been doing prior to the adoption of the Constitution.

- In 1953, an Act prescribing / modifying service conditions of the CAG was enacted (Comptroller and Auditor General of India (Conditions of Service) Act, 1953).
- A comprehensive enactment covering duties and conditions of service of CAG was made only in 1971 – the Comptroller and Auditor General’s (Duties, Powers and Conditions of Service) Act, 1971 -- repealing the 1953 Act and ceasing the Government of India (Audit and Accounts) Order, 1936.

- After the enactment of the CAG (Duties, Powers and Conditions of Service) Act, 1971 (hereinafter referred to as 'CAG Act'), CAG shall perform the duties only as per the that Act and other Constitutional provisions.

The CAG Act empowered the CAG to audit expenditure and receipts of Union/State/UT governments, government autonomous bodies, etc., (Sections 13 to 20) and to compile, prepare and submit annual accounts of the Union, States and Union Territories having Legislative Assembly (Sections 10 to 12). As per the provisos of Sections 10 and 11 of the Act, the President or the Governor, as the case may be, may relieve CAG from compilation and preparation of accounts of the Union and States/UT.

In 1976, the Audit and Accounting functions in respect of Union government were separated, and – by a suitable amendment of the CAG Act – the CAG was relieved of the responsibility of compiling and keeping of accounts of various Departments/Ministries of Union Government (except in respect of accounts relating to their own Department (IAAD), and with respect to pensions in lieu of resumed jagirs, lands, etc.) A separate Indian Civil Accounts Service (ICAS) was established (1st March, 1976) with Controller General of Accounts (CGA) as the head, for compilation and preparation of Accounts of the Union Government.

Similarly, CAG was relieved of preparation of Accounts of State of Goa and UT of Puducherry, in 1978 and 1989 respectively, and subsequently of the NCT of Delhi, and the work was entrusted to the relevant governments.

These accounts of the Union Government, Goa, Delhi, and Puducherry are, however, examined by the CAG as part of their constitutional and statutory audit function, and Audit certificate are issued by them to that effect before their submission to the Parliament/Legislature.

3. Conflict of interest in auditing the Accounts of State

As per the CAG Act, CAG continues to prepare the Accounts of 28 States through field offices viz., the office of the Accountant General/Principal Accountant General (Accounts & Entitlement) in these States. The audit of these accounts is conducted by another wing of IAAD viz., the office of the Accountant General/Principal Accountant General (Audit).

Accounting and Auditing of the accounts so prepared by same authority is not in consonance with global best practice. It constitutes conflict of interest, and is also against one of the basic principles of natural justice viz., one cannot be a judge of his own case. The Auditing Standards prescribed by CAG himself contemplates that the Supreme Audit Institution (CAG) should avoid conflict of interest between the auditor and the entity under audit (Auditing Standards 2002 of CAG, para 3.2(k)).

CAG, however, justifies the arrangement of accounting and auditing by him for the States, in his audit certificate appended with the Accounts concerned, as follows:

“... I am responsible for preparation and submission of Annual Accounts to the State Legislature. My responsibility for the preparation of Accounts is

discharged through the office of the Accountant General/Principal Accountant General (Accounts & Entitlement), (State name). The audit of these accounts is independently conducted through the office of the Accountant General/Principal Accountant General (Audit), (State name) in accordance with the requirements of Articles 149 and 151 of the Constitution of India and the Comptroller & Auditor General's (Duties, Powers and Conditions of Service) Act, 1971, for expressing an opinion on these accounts based on the results of such audit. These offices are independent organizations with distinct cadres, separate reporting lines and management structure.”

The CAG's statement that the two offices viz., AG (A&E) and AG (Audit) are independent with distinct cadres and separate reporting lines is not fully true in essence and practice.

- The cadres up to the level of Accounts Officers/Senior Accounts Officers and Audit Officers/Senior Audit Officers in the two offices respectively are only distinct and non-transferable between the two offices.
- However, the higher posts (Deputy Accountant General/Senior Deputy Accountant General and the Accountant General/Principal Accountant General) held by IAAS officers in the two offices (A&E and Audit) are transferrable; for instance, AG (A&E) today may be posted as AG (Audit) tomorrow.

Under these circumstances, one cannot expect the Audit Officer of Audit Office to be truly independent while examining the accounts for certification, as at any time DAG (Accounts)/AG of A&E may become their superiors in the Audit office.

The next level officers at CAG's office, to whom the State Accountants General are reporting, are also transferable from Accounts wing to Audit wing and vice-versa. Under the circumstances, the adverse impact of the inter-transferability of IAAS officers doing accounting and auditing functions, as also of a possible 'feeling of belonging of the same department', on fairness in discharging their assigned duties cannot be ruled out.

Now, in the entire world, only CAG of India is holding unique position of performing both accounting (for States) and audit functions (CAG's speech during the celebration of first Audit Diwas on 16.11.2021, Press Release of CAG, cag.gov.in). No other national auditor is performing accounting function.

Way forward

Accounting and auditing might have been left to the same agency in view of convention; in fact it was presumably inevitable, as there were no alternatives at the time of enactment of the CAG Act. But it is evident, as may be noted from the provisos to Sections 10 and 11 of the CAG Act itself, that the accounting function has been entrusted to CAG only as an interim arrangement and the President or the Governors are empowered to relieve the CAG from compiling and preparation of Accounts.

With respect to the Union government, the conflict of interest was addressed in the mid-1970's, by establishing a separate institution for preparation of Union accounts – the CGA. Since this reasoning and justifications equally applies for the States, it is not clear why the arrangement of accounting and auditing of States' Accounts by the same entity is allowed to continue for several decades.

As a specialised organisation for compilation/preparation of accounts has already been established at the Union level, rather than entrusting the accounting work to each State, it would be easier and better to have a common separate specialised organisation for all State accounts. So, accounting work all States also may be entrusted to CGA. CGA may establish separate State level offices (Accountant General with ICAS officers) under their control. State Audit office may be redesignated as Auditor General with retitling of Comptroller and Auditor General of India as Chief Auditor General of India (CAG), exclusively for audit.

4 *Ultra vires* action of CAG

Article 149 of the Constitution permitted CAG to continue with the same duties and powers only till an Act of Parliament is made in this regard. Once an Act is enacted by the Parliament, the CAG shall perform only those duties and exercise those powers conferred on them by/under that Act and other provisions of the Constitution.

In the CAG Act, there is no provision for doing Entitlement functions for the employees of the Union and State governments. CAG has dispensed with maintaining of GPF accounts of employees of Union government (except those in IAAD) and employees of eight² States; however, CAG continues to perform Entitlement functions of maintenance of individual GPF accounts of employees (which may not be construed as essential for compilation and preparation of accounts) and authorisation of their final payments, authorisation of pension to them and gazetted entitlement functions for 20, 19, and 9 States respectively (Performance Report of CAG for 2019-20).

The continuance of Entitlement function for the employees of the States by CAG even after 1971 lacks statutory authority, and, as such, is *ultra vires* the Constitution. Consequently, the engagement of officers and staff for entitlement function for the States by CAG is not legally valid.

It is pertinent to note that the CAG Act itself specifically required the CAG to audit, *inter alia*, all expenditures from the Consolidated Fund of Union, and to ascertain whether the moneys shown in the accounts as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged, and whether the expenditure conforms to the authority which governs it (Section 13 of CAG's Act). In the absence of statutory backing for performance of the entitlement function by the CAG, the expenditures thereon since 1971 were not legally available – that is, those expenditures are irregular.

The CAG should immediately initiate action to hand over the entitlement functions to the States concerned, explaining the relevant Constitutional and legal provisions, and engage the resultant human resources for the mandated functions.

5. Importance of CAG's audit and need for its strengthening

5.1 Vulnerability of public finance

The size and complex nature of government functioning make public money susceptible for misuse at the hands of unscrupulous persons, despite various checks and balances within the system.

- The financial activity of the government starts with getting the approval of Parliament/Legislature for both collection of revenue and spending the collected money for governance and for implementation of various developmental and welfare schemes.
- The money approved by the Parliament/Legislature for expenditure would be allocated by the government to all the offices, from the apex level to subordinate and field level, for spending.
- The officer, having the delegated financial power, would accord sanction for incurring expenditure and then the Drawing and Disbursing Officer (DDO) of the office would draw the money from the Consolidated fund, where all government moneys are kept, and disburse them to the person concerned.

A corrupt government servant may, individually or in collusion with others, indulge in all sorts of deviations from the prescribed procedure, to divert the public money. Media reports on possession of huge money – in cash, bank accounts, and other properties like land and buildings, bullions, shares, etc. – with some public/government servants, disproportionate to their known sources of income are the proof for the flaws in the system. An internal audit may not have the required specialisation, or may not be allowed to detect and report such irregularities if involved persons are higher officers and in power. Only an external, specialised, independent, and statutorily empowered audit may bring out those irregularities.

Appropriately considering the vulnerability of public money, complexity of its administration, and the importance of money in governance and growth of the country, the founding fathers of the Constitution have established an independent Institution of CAG with constitutional protection as watchdog of public finance.

Thus, the CAG has a key role in ensuring the financial accountability of all those dealing with the management of public money. In the words of T.N. Chaturvedi, former CAG,

“... The Auditor General should have a strong psychological or subjective feeling of accountability which must manifest itself in the organisation and working of his office. The imaginative and purposive functioning of his office and the faith it inspires in the public mind will reinforce and also provide the continuing rationale of his office.

... As guardian of public accountability the Auditor General should hold himself out as a model institution fully conscious of his own responsibility to the people at large. He should evolve adequate internal control mechanism to ensure this wider accountability of his organisation. It is possible that some convention here or a regulation there may presently seem to restrict the character, scope and

direction of audit, but once the institution carries conviction with the people that it is both conscious of and competent to discharge its responsibilities, public opinion will, may be imperceptibly, compel the authorities to change them in public interest.

This may see irksome at times; the opposite and greater danger is the general feeling that the institution is just scratching the surface and that it is doing too little, and too late, in enforcing the accountability of audited institutions. Such a feeling, if allowed to persist, may erode the very credibility of the institution of Auditor General. Substantial and substantive approach, and not a peripheral one which tries to skirt round difficult issues, will help to maintain the institutional ethos and autonomous of the institution.”

- (T. N. Chaturvedi, Role of the Auditor General in Public Accountability, Government Auditing, Ashish Publishing House, New Delhi, 1987, pages 22-23).

5.2 Present level of audit coverage

Three types of audits are conducted by CAG viz., Financial audit, Compliance audit, and Performance audit.

- Financial audit is mainly certification of accounts
- Compliance audit is examining the regularity (compliance of rules) and propriety (observance of the general principles, governing sound financial management and the conduct of public officials) of financial transactions (Regulations 44 and 45 of Regulations on Audit and Accounts, 2020)
- Performance audit is an appraisal type to inform the stakeholders about the quality of management of public finance, and to assist the executive with better management practice for implementation of policy objectives economically, efficiently and effectively.

The mandate for Performance Audit is derived by authority given to CAG in Section 23 of CAG's Act to decide the scope of audit (Performance Auditing Guidelines, 2004, para 1.40) and conduct of Performance audit was formally accepted by the Government of India in June 2006 (Letter No. F 6(5)-B (R)/99, dated 13th June 2006 Ministry of Finance, Government of India, Brochure on CAG's (DPC) Act, 1971, page 35, cag.gov.in). Thus, the Financial and Compliance audits are the core audit functions of CAG.

The Compliance audit is being conducted based on DDOs (auditable Units). A reasonable periodic coverage of audit of every unit (annual / at least once in cycle of 5 years, based on the risk analysis) and checking of samples of transactions in the units audited (as may be decided by CAG, under Section 24 of CAG's Act) is vital, as each unit is headed by different individuals with adequate power for sanctioning and drawing of public money for spending.

Further, CAG is the sole independent auditor of the government; if a unit remains unaudited for a long period, it would prove 'audit is too late', even if it could trace all the records of transactions for

all audit trails after a gap of many years. Significant non-coverage of compliance audit for long periods would further embolden unscrupulous elements, as the deterrent effect of audit gets thinned.

As per the information in the Performance Reports of CAG for the years 2011-12 to 2019-20, the number of units audited each year during the above period were in the range of 42,192 to 57,985, with available human resources of 44,241 to 46,936. The total number of units auditable in the country by CAG is not disclosed. The data of total number of DDOs in the Union and State/UT governments is also not available in the public domain.

As per the available information with respect to Telangana State government, the number of DDOs in that State was 45,385 (the date to which this pertains is not available), excluding other commercial undertakings, autonomous bodies, etc., of the State which are also auditable by CAG (www.treasury.telangana.gov.in/ddolist.php).

This position would clearly prove that at the present level of compliance audit, all the auditable units could not be covered by CAG in a reasonable periodic cycle. This strongly suggests that the audit coverage by CAG is not complete.

5.3 Expenditure for audit

All the receipts and expenditure of the governments are to be audited by CAG. The expenditure for conduct of CAG audit (Rs. 1538.96 crore) in 2011-12 was only 0.036% of total receipts and expenditure (Rs. 42,96,047 crore) of Union and all State/UT governments (Performance Audit Report of CAG for 2011-12).

Similar data for 2018-19 was not given by CAG in the Performance Report for that year. However, from the available information, expenditure on audit function for the year 2018-19 works out to approximately Rs. 3,300 crores³, which is only 0.032% of total receipts and expenditure (Rs. 101,65,794 crore) of Union and all State/UT governments. Thus, the expenditure incurred for audit of financial transaction value of every one lakh rupees was a mere Rs. 36 in 2011-12, which further reduced to Rs. 32 in 2018-19.

There are no clear benchmarks or standards available for cost of government audit. However, considering the high risk in view of complexity of government transactions, the expenditure on audit seems to be on the lower side.

5.4 Quantum of recovery at the instance of audit

Any standards or an ideal level of expenditure on government audit is not set. However as per the statement of CAG, every rupee spent on audit resulted in realisation of Rs 10.93 to governments at the instance of audit during 2005-06, excluding the value of assurance provided, system improvement, and deterrent value. (Performance Report of IAAD for 2005-06).

Similar information for the years 2011-12 to 2019-20 were not available; however, the recoveries towards under-assessment of tax and specific loss to the exchequer made at the instance of audit during the above period were in the range of Rs 3000 crore to Rs 6,917 crore (Performance Reports

of CAG for 2011-12 to 2019-20). This may serve as an indicator of the gaps in the financial management system, besides proving any expenditure on audit would fetch more returns.

The vulnerability of public finance (para 5.1 above), the present lesser level of audit coverage (para 5.2 above), meagre expenditure on audit (para 5.3 above) and the prospects for recovering/saving of more public money by effective and more audit (para 5.4 above) give scope and justification for coverage of all the auditable units in periodic intervals based on risk factors. Strengthening of audit with more human-power to cover all auditable units and for effective audit is essential to fully serve the purpose of audit.

6. Conclusion

This article has identified a number of necessary reforms in the public accounts and auditing system in India.

Accounting and auditing of accounts by the same entity is a conflict of interest, with scope to adversely impact the quality of both accounting and auditing. The good sense of separating accounting and audit functions for the Union government prevailed in 1976. It is yet to be extended for States' Accounts.

The CAG continues to do the entitlement function for considerable number of States, without any statutory backing and thus incurring irregular expenditure to that extent. While doing such unauthorised work, the CAG is allowing a significant shortage in the mandated audit function. The significant non-coverage of audit may pose a potential risk of making the institution of CAG irrelevant, defeating the very objective of creating a supreme audit institution.

Thus, there is an urgent need for reorganisation of IAAD/CAG's functions to make it an exclusive institution for audit, for ensuring the financial accountability of all persons dealing with public finance.

References

1. Brochure on Comptroller and Auditor General's (Duties, Powers and Conditions of service), Act 1971 (web-site - cag.gov.in)
2. Combined Accounts of Union and State finance for 2018-19 - https://cag.gov.in/uploads/combined_accounts/Union-State-Finances-Glance2018-19-0607800c98e0012-60664951.pdf
3. Comptroller and Auditor General's (DPC) Act, 1971 (web-site - cag.gov.in)
4. Constituent Assembly proceedings
5. Constitution of India
6. Controller General of Accounts (web-site - cga.gov.in)
7. Government of India Act, 1935
8. Government of India (Audit and Accounts) Order, 1936
9. Performance Reports for CAG for the years 2011-12, 2018-19 and 2019-20 (cag.gov.in)
10. Regulations on Audit and Accounts, CAG, 2020 (web-site - cag.gov.in)
11. R. K. Chandrasekharan, Comptroller and Auditor General of India, Analytical History, 1947-1989, Volume I (web-site - cag.gov.in)
12. T. N. Chaturvedi, Role of the Auditor General in Public Accountability, Government Auditing, Ashish Publishing House, New Delhi, 1987, pages 22-23

Notes

¹ Article 149 of the Constitution - the CAG shall perform such duties and exercise such powers in relation to the accounts of the Union and of the States and of any authority or body as may be prescribed by or under any law made by Parliament and, until provision in that behalf is so made, shall perform such duties and exercise such powers in relation to the accounts of the Union and of the States as were conferred on or exercisable by the Auditor General of India immediately before the commencement of this Constitution in relation to the Dominion of India and of the Provinces respectively.

² Rajasthan, Mizoram, Arunachal Pradesh, Jammu & Kashmir, Bihar (now including Jharkhand), Punjab and Sikkim

³ (Total expenditure of Rs 4778.13 crore including expenditure on Training Institutes, UN Audit, etc., - (minus) Expenditure of Rs 1477.92 crore on Accounts). Adopting the data in Union and State Finances at-a-Glance 2018-19, (total of revenue receipts Rs. 44,25,317 crore and revenue and capital expenditure - Rs 57,40,477 crore of Union and all States) (para 2.1.1 - https://cag.gov.in/uploads/combined_accounts/Union-State-Finances-Glance2018-19-0607800c98e0012-60664951.pdf)