

**THE KARNATAKA LOCAL FUND AUTHORITIES FISCAL RESPONSIBILITY
ACT, 2003**

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STATEMENT OF OBJECTS AND REASONS

Act No: 41 of 2003- The framework for budgeting, accounting and auditing for the State Government are specifically provided in various Code and Manuals framed by Government under Article 283 of the Constitution of India. The budget of the State is prepared by the Government and is put to vote before both the Houses of Legislature. Once the budget is passed by both the houses of Legislature, as laid down in the Constitution of India, the expenditure is met out of the Consolidated Fund as per the budget, duly passed by the Legislature. The deviations from the budget, as voted by the Legislature, can only be made as laid down in Karnataka Financial Code and is brought to the notice of Legislature in due course.

The Comptroller and Auditor General performs the audit and account functions for the State Government. Report of the Comptroller and Auditor General is submitted to the Governor who causes them to be laid before the Legislature of the State. These reports are referred to the Public Accounts Committee and the report of the Committee along with the report of the Comptroller and Auditor General is put on the table of the House.

With such a framework, the State Government, to ensure fiscal stability and sustainability, introduced the Karnataka Fiscal Responsibility Act, 2002, which mandates the State Government to have a Medium Term Fiscal Plan (MTFP), a rolling document for four years specifying targets for prescribed parameters. The Act also specifies fiscal management principles to be followed by the State Government. In furtherance to Medium Term Fiscal Plan, the State Government decided to disintegrate the MTFP on departmental lines and prepare Departmental Medium Term Fiscal Plan for each department along with the MTFP for the entire State.

It is now felt that a similar framework for budgeting, accounting and auditing should be there for the Local Fund Authorities (LFA). There is a need for an Act which,

- (1) mandates a Medium Term Fiscal Plan for the Local Fund Authorities.
- (2) lays down principles for financial management.
- (3) ensures transparency in Fiscal Management at the local level.
- (4) ensures proper procedure for preparation, submission and audit of accounts.
- (5) ensures proper scrutiny and adherence to the audit reports.
- (6) lays down measures to enforce compliance to the provisions of the Act. Hence the Bill.

[LA Bill No. 22 OF 2003]
(Entries 5 and 32 of List-II of Seventh Schedule to the Constitution of India)

I

Amending Act 41 of 2021.- It is considered necessary to amend the Karnataka Local Fund Authorities Fiscal Responsibility Act, 2003 (Karnataka Act 41 of 2003) to make the Rural Development and Panchayat Raj Department in respect of panchayat Raj institutions and Urban Development Department in respect of Urban Local Bodies as Competent Authority instead of the State Accounts Department to oversee the compliance of the Act and to notify the mechanism of submitting periodical review reports.

Hence, the Bill.

[L.A. Bill No. 32 of 2021, File No. Samvyashae 33 Shasana 2021]

[Entry 5 and 32 of List II of the Seventh Schedule to the Constitution of India.]

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KARNATAKA ACT NO 41 OF 2003

(First published in the Karnataka Gazette Extra-ordinary on the sixth day of September, 2003)

THE KARNATAKA LOCAL FUND AUTHORITIES FISCAL RESPONSIBILITY ACT, 2003

(Received the assent of the Governor on the fifth day of September, 2003)

(As amended by Act 41 of 2021)

An Act to provide for the responsibility of Local Fund Authorities to ensure best practice of financial management of local funds and to enhance the scope for improving social and physical infrastructure and human development by achieving sufficient revenue surplus, ensuring prudent management of public fiscal operations of the Local Funds and use of a medium term fiscal frame work, and for matters connected therewith or incidental thereto.

Whereas it is expedient to provide for the responsibility of Local Fund Authorities to ensure fiscal stability and sustainability and to enhance scope for improving social and physical infrastructure and human development by achieving sufficient revenue surplus, performance enhancement, citizen participation and transparency while removing impediments to the effective conduct of fiscal policy and enabling prudent financial management through appropriate modern systems and with greater transparency in fiscal operations of the Local Funds with the use of a medium-term fiscal frame work, and for matters connected therewith or incidental thereto.

Be it enacted by the Karnataka State Legislature in the fifty-fourth year of the Republic of the India as follows:-

1. Short title, extent and commencement.- (1) This Act may be called the Karnataka Local Fund Authorities Fiscal Responsibility Act, 2003.

(2) It extends to such Local Fund Authorities as may be notified by the State Government from time to time.

(3) It shall come into force on such date as the State Government may, by notification, appoint.

2. Definitions.- In this Act, unless the context otherwise requires,-

- (a) "local fund" means the revenue administered by bodies which by any law or rule having the force of law are under the control of State Government whether in regard to the proceeding generally or to specific matters such as sanctioning of their budget, sanction to the creation or filling up of post or particular appointments or encashment of leave, pension or similar matters;
- (b) "local fund authority" means any body which administers the local fund;
- (c) "accounting standard" means such accounting standards in respect of local fund authorities, as may be prescribed;
- (d) "annual budget" means the budget placed before the concerned local fund authority as per the relevant Acts or the rules made thereunder;
- (e) "budget variance" means the difference between the budgeted amount and the actuals for the financial year;
- (f) "Controlling Authority" means any officer appointed as controlling authority by the State Government for the purpose of this Act and different controlling authorities may be appointed in respect of different local fund

authorities;

- (g) "Current Year" means the year preceding the year for which budget and Medium Term Fiscal Plan (MTFP) are being presented;
- (h) "fiscal indicators" means such measures as may be prescribed, for evaluation of fiscal position of local fund authority;
- (i) "Previous Year" means the year preceding the current year.

3. Medium Term Fiscal Plan.- (1) There shall be prepared in each financial year a Medium Term Fiscal Plan along with the annual budget in respect of every local fund authority and shall be submitted for approval of the concerned authority.

(2) The medium Term Fiscal Plan shall set forth a four-year rolling target for the fiscal indicators with specification of underlying assumptions.

(3) In particular and without prejudice to the provisions contained in sub-section (2), the Medium Term Fiscal Plan shall include an assessment of sustainability relating to:-

- (7) the balance between revenue receipts and revenue expenditures; and
- (8) the use of capital receipts including borrowings for generating productive assets.

(4) The Medium Term Fiscal Plan shall, *inter alia*, contain,-

- (a) the medium term fiscal objectives of the local fund authority;
- (b) the mission, objectives and goals of the local fund authority;
- (c) an evaluation of the performance of the fiscal indicators in the previous year vis-à-vis the targets set out earlier, and the likely performance in the current year as per revised estimates;
- (d) a statement on recent trends and future prospects for growth and development affecting fiscal position of the local fund authority;
- (e) the strategic priorities of the local fund authority in the fiscal area for the ensuing financial year;
- (f) the policies of the local fund authority for the ensuing financial year relating to expenditure, borrowings and other liabilities, lending and investments. and all such activities which have potential budgetary implications and the key fiscal measures and targets pertaining to each of these;
- (g) an evaluation as to how the current policies of the local fund authority are in conformity with the financial management principles set out in section 4 and the fiscal objectives set out in the Medium Term Fiscal Plan;
- (h) a clear linkage of the physical and financial targets;
- (i) the key performance areas and corresponding performance indicators in as much quantitative detail as possible.

(5) The Medium Term Fiscal Plan shall be the source document for the preparation of the annual budget and shall address the prime needs of the citizens as relevant to the specific local fund authority such as water supply, construction of road, education, public health, solid waste management and the like.

(6) The Medium Term Fiscal Plan shall have a functional focus and provide for backend modalities such as fund based accounting system (FBAS), computerisation and a realistic and transparent budgeting process.

(7) The Medium Term Fiscal Plan shall be in such form as may be prescribed.

4. Financial management principles.- Every local fund authority will be guided by the following financial management principles, namely:-

- (a) ensuring transparency at all stages of policy making and implementation;
- (b) introducing performance linked budget policies;
- (c) providing for effective and sustained fiscal monitoring systems;
- (d) introducing robust financial management principles;
- (e) maintaining local fund authority's debt at prudent levels;
- (f) managing guarantees and other contingent liabilities prudently, with particular reference to the quality and level of such liabilities;
- (g) ensuring that policy decisions of the local fund authority have due regard to their current financial position and the financial implications on future generations;
- (h) adopting accrual system of accounting for payables and receivables;
- (i) ensuring that borrowings are used for productive purposes and accumulation of capital assets, and are not applied to finance current expenditure;
- (j) ensuring a reasonable degree of predictability in the flow of funds;
- (k) pursuing tax policies with due regard to economic efficiency and compliance costs;
- (l) pursuing fiscal policies with due regard to cost recovery and equity;
- (m) pursuing expenditure policies that would provide impetus for economic growth, poverty reduction and improvement in human welfare;
- (n) ensuring that physical assets of the local fund authority are properly maintained;
- (o) disclosing sufficient information to allow the public to scrutinize the conduct of fiscal policy and the state of local fund authority finances;
- (p) ensuring that local fund authority uses resources in ways that give best value for money, and also ensure that public assets are put to best possible use;
- (q) managing expenditure consistent with the level of revenue generated;
- (r) formulating budget in a realistic and objective manner with due regard to the general economic outlook and revenue prospects, and minimize deviations during the course of the year;
- (s) ensuring collection of dues and taxes in an expeditious manner;
- (t) ensuring discharge of current liabilities in a timely manner;
- (u) adopting appropriate techniques for measuring the cost of the services provided by the local fund authority.

5. Measures for fiscal transparency.- (1) The local fund authority shall take suitable measures to ensure greater transparency in its fiscal operation in public interest and minimize as far as practicable, secrecy in the preparation of the annual budget. For this purpose every local fund authority shall ensure that there are at least two meetings every year at the time of budget preparation and finalization with such citizen forums as may be prescribed.

(2) Provision shall be made for meetings at such intervals and with citizen forums as may be prescribed to review the operations and finances of the local fund authority.

(3) In particular, and without prejudice to the generality of the foregoing provisions, local fund authority shall, at the time of presentation of the annual budget, disclose in a statement in such form as may be prescribed –

- (a) significant changes in the accounting standards, policies and practices affecting or likely to affect the computation of fiscal indicators;
- (b) as far as practicable, and consistent with protection of public interest, the contingent liabilities created by way of guarantees and the actual liabilities arising out of execution of works by external agencies where liability for repayment is on the local fund authority.

(4) The State Government shall ensure that such contingent liabilities are communicated to the concerned local fund authority so that it shall make sufficient provision in its budget.

6. Measure to enforce compliance to this Act.- (1) ¹[The Rural Development and Panchayat Raj Department in respect of Panchayat Raj institutions and Urban Development Department in respect of Urban Local Bodies]¹ shall enforce compliance with the provisions of this Act and the rules made thereunder.

(2) ¹[The Rural Development and Panchayat Raj Department in respect of Panchayat Raj institutions and Urban Development Department in respect of Urban Local Bodies]¹ may oversee the compliance and a suitable mechanism may be notified by the State Government regarding the submission of periodical review reports.

(3) The State Government shall ensure that the local fund authority comply with provisions of the relevant Act and the rules relating to budget and the budget prepared is in accordance with the Medium Term Fiscal Plan already approved and variations, if any, are explained.

(4) The local fund authority shall prepare a budget variance report and submit it to the Controlling Authority within such time and in such form as may be prescribed.

(5) The local fund authority shall prepare receipts and payments account, income and expenditure account and a balance sheet as may be prescribed.

(6) Audit of accounts of the local fund authority shall be conducted by the auditor appointed under the relevant Acts and the rules and orders issued thereunder which is the authority and the report shall be submitted to the concerned authorities within the time stipulated.

(7) The Controlling Authorities shall be responsible to ensure strict follow up action on the audit reports by the local fund authority and slackness, if any, noticed in this behalf shall be reported to the State Government for appropriate action against local fund authority in default.

(8) The State Government may, by notification, constitute a Local Fund Audit Overseeing Authority comprising of such officers and having such powers as may be specified in the notification. The Local Fund Audit Overseeing Authority shall submit to the State Government periodical report on compliance to audit reports by the local fund authority, as may be prescribed.

(9) The State Government may withhold release of funds to any local fund authority which fails to furnish accounts to the concerned authority within six months from the end of the financial year.

(10) The local fund authority shall introduce and strengthen appropriate internal audit measures and a sustainable computerisation programme using appropriate technology.

1. Substituted by Act 41 of 2021 w.e.f. 12.10.2021.

2. Publication of financial document and annual report.- (1) Every local fund authority shall publish the MTFP, the annual budget, annual accounts and the annual report together with the certified annual accounts in such manner as may be prescribed.

(2) Every local fund authority shall, within six months from the end of the financial year submit a copy of its annual report together with the certified annual accounts to the State Government and the State Government shall cause the annual report together with the certified annual accounts to be laid, as soon as may be they are received, before each House of the State Legislature.

3. Power to make rules.- (1) The State Government may by notification and after previous publication, make rules for carrying out all or any of the purposes of this Act.

(2) Every rule made under this Act shall be laid as soon as may be after it is made, before each House of the State Legislature while it is in session for a total period of thirty days, which may be comprised in one session or in two or more successive sessions and if before the expiry of the session in which it is so laid or the session immediately following both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made, the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be, so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.

4. Protection of action taken in good faith.- No suit, prosecution or other legal proceedings shall lie against the State Government, any local fund authority or any officer or servant or any person acting under the direction of the State Government or local fund authority in respect of anything done or intended to be done in good faith under this Act or any rule or order made thereunder.

5. Application of other laws.- The provisions of this Act shall be in addition to the provisions of any other law for the time being in force, to the extent they are not inconsistent with the provisions of this Act and the provisions of this Act shall have effect notwithstanding anything contrary contained in any other law for the time being in force.

6. Removal of difficulties.- (1) If any difficulty arises in giving effect to the provisions of this Act, the State Government may by order, published in the official gazette, as the occasion may require, do anything which appears to it to be necessary to remove the difficulty;

Provided that no order shall be made after the expiry of a period of two years from the date of commencement of this Act.

The above translation of the ಕರ್ನಾಟಕ ಸ್ಥಳೀಯ ನಿಧಿ ಪ್ರಾಧಿಕಾರಗಳ ಆರ್ಥಿಕ ಹೊಣೆಗಾರಿಕೆ ಅಧಿನಿಯಮ, 2003 (2003 ರ ಕರ್ನಾಟಕ ಅಧಿನಿಯಮ ಸಂಖ್ಯೆ: 41) be published in the Official Gazette under clause (3) of Article 348 of the Constitution of India.

KARNATAKA ACT NO.41 OF 2021

(First Published in the Karnataka Gazette Extra-ordinary on the 12th day of October 2021)

**THE KARNATAKA LOCAL FUND AUTHORITIES FISCAL RESPONSIBILITY
(AMENDMENT) ACT, 2021**

(Received the assent of the Governor on the 11th day of October, 2021)

An Act to amend the Karnataka Local Fund Authorities Fiscal Responsibility Act, 2003.

Whereas it is expedient to amend the Karnataka Local Fund Authorities Fiscal Responsibility Act, 2003 (Karnataka Act 41 of 2003) for the purposes hereinafter appearing:

Be it enacted by the Karnataka State Legislature in the seventy second year of the republic of India as follows:-

1. Short title and Commencement.- (1) This Act may be called the Karnataka Local Fund Authorities Fiscal Responsibility (Amendment) Act, 2021.

(2) It shall come into force at once.

2. Amendment of section 6.- In the Karnataka Local Fund Authorities Fiscal Responsibility Act, 2003 (Karnataka Act 41 of 2003), in section 6,-

(1) in sub-section (1), for the words "The State Accounts Department", the words "The Rural Development and Panchayat Raj Department in respect of Panchayat Raj institutions and Urban Development Department in respect of Urban Local Bodies", shall be substituted; and

(2) in sub-section (2), for the words "The State Accounts Department may", the words "The Rural Development and Panchayat Raj Department in respect of Panchayat Raj institutions and Urban Development Department in respect of Urban Local Bodies shall", shall be substituted.

The above translation of ಕರ್ನಾಟಕ ಸ್ಥಳೀಯ ನಿಧಿ ಪ್ರಾಧಿಕಾರಗಳ ಆರ್ಥಿಕ ಹೊಣೆಗಾರಿಕೆ (ತಿದ್ದುಪಡಿ) ಅಧಿನಿಯಮ, 2021 (2021 ರ ಕರ್ನಾಟಕ ಅಧಿನಿಯಮ ಸಂಖ್ಯೆ: 41) be published in the official Gazette under clause (3) of Article 348 of the Constitution of India.

**THAAWARCHAND GEHLOT
GOVERNOR OF KARNATAKA**

By Order and in the name of
the Governor of Karnataka,

G.SRIDHAR
Secretary to Government
Department of Parliamentary
Affairs and Legislation