Public Expenditure Accountability of The Indian Railways

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Introduction

In a largely government controlled economy, the Indian Railways (IR) has been used as a tool of dispatch towards government objectives. A separate budget owing to historical circumstances is just one of the features that mark the close bondage between the government and its chief logistics agency. The basic attitude of running IR is that of a bureaucracy. A welfare outlook have burdened IR with many liabilities. Populist measures leading to an irrational fare structure with a heavy cross subsidy of the passenger sector by freight has corroded its viability as a profit making entity. Its share in the goods transport sector has steadily slipped behind road. An unwieldy workforce means that a greater part of its finances are being diverted towards staff costs and pensions. This is seriously compromising IR's ability to invest in capital goods like tracks and rolling stock leading to an alarming safety issue and the inability to keep abreast with global technology standards.

It is to its credit that IR, unlike its counterparts even in many developed countries, has been able to maintain an operating profit and has been sourcing funds for investments through internal resources. Even so, there is not enough funding. Part of this shortfall has been met by the government's budgetary support. The share of budgetary inputs in the investment plans has been varying, with IR having to look for other strategies like market borrowings through the Indian Railways Financial Corporation (IRFC) and schemes like Build Operate Lease Transfer (BOLT) and Own Your Wagon (OYW). Table 1 shows IR's sources of funds for the 5 year plans.

Table 1: Pattern of Financing Railways Plan Investment

Plan	Budgetary support from GOI		Internal resources		Market borrowings through IRFC		BOLT/OYW		Total	CAGR percentage per annum
	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage		
I (51-56)	142	33.6	280	66.4	0	0.0	0	0.0	422	
II (56-61)	576	55.2	467	44.8	0	0.0	0	0.0	1143	22.1
III (61-66)	1140	67.7	545	32.3	0	0.0	0	0.0	1785	9.3
IV (69-74)	1031	72.2	397	27.8	0	0.0	0	0.0	1528	-3.1
V (74-78)	1141	74.8	384	25.2	0	0.0	0	0.0	1625	1.6
VI (80-85)	3802	57.7	2783	42.3	0	0.0	0	0.0	6685	22.4
VII (85-90)	6940	41.9	7089	42.8	2520	15.2	0	0.0	16649	20.0
VIII (92-97)	7311	22.6	18830	58.3	5565	17.2	596	1.8	32400	10.0
IX (97-02)	15472	33.3	16352	35.2	13523	29.1	1058	2.3	46502	7.5
1997-8	1992	24.2	3452	41.9	2236	27.1	559	6.8	8332	
1998-9	2185	24.7	3455	39.0	2941	33.2	276	3.1	8953	7.5
1999-0	2588	28.6	3550	39.2	2785	30.7	134	1.5	9155	2.3
2000-1	3269	34.8	3229	34.4	2818	30.0	79	0.8	9494	3.7
2001-2	5438	50.1	2666	24.6	2743	25.3	10	0.1	10956	15.4
2002-3	5390	43.7	3940	32.0	3000	24.3	0	0.0	12430	13.5

Source: 1) Status paper, 1998,

2) Business line, Feb 27th, 2002.

Figures for 2001-2 are revised budget estimates

Figures for 2002-3 are budget estimates

2001-2, 2002-3 figures include the SRSF contributions.

As on March 2001, the total fund inflow into IR and available for use has been Rs 99542 crores. Out of this Rs 32661 crores have come in through budgetary support, Rs 30679 crores have come in from internal resources which include the Railway Capital Fund, Depreciation Reserve Fund and the Development Fund, Rs 21707 crores from the IRFC route and the rest in the form of reserves, deposits and current liabilities. Out of this money, Rs 35554 crores have been invested in buildings and track, Rs 34016 crores in rolling stock and Rs 11516 crores have been used towards procurement of plant and equipments. The rest of the money has been spent on land, investments, deposits with the central government and in current assets.

There is also the question of whether the potential of IR is fully leveraged for maximal revenues and judicious expenses, to generate optimal internal resources. The revenue, expenses and investments constitute the public expenditure of IR. Being in the public domain as a key infrastructure providing organisation, IR is accountable towards public expenditure. This paper focuses on certain key issues concerning Public Expenditure Accountability in IR.

This paper firstly looks at how the government exercises influence on the functioning of IR. The internal finance management of IR is the focus of the next portion. At the end, an effort is made to chalk out possible future remedies to the ills facing IR, wherein the route of corporatisation is evaluated.

1.0 Railway Government Interface.

While considering the IR government interface, it is necessary to understand certain roles and define some terms. IR is under the Ministry of Railways, which is referred to as the central government in the Indian Railways Act. The word government in this paper refers to the Government of India (GoI) which consists of all the other government agencies (including the Finance Ministry) other than IR. The Railway Minister (who heads the Ministry of Railways) acts as a link between the GoI and IR. The Railway Board heads the executive arm of IR and is also the secretariat to advise the Railway Minister on all matters concerning railway management.

This section begins with an examination of the Indian Railways Act, 1989. This is followed by an analysis of the financial interface of IR and GoI. The special railway budget is considered next followed by an overview of the different issues related with political interference in the working of IR. IR's interactions with state government's forms the last part of this section.

1.1 The Indian Railways Act - 1989.

The Indian Railways Act enacted by Parliament vests the central Government (Ministry of Railways) with powers over the functioning of IR. There are chapters dealing with railway administrations, Commissioners of Railway Safety, construction and maintenance of works, opening of railways, fixation of rates, carriage of passengers and goods etc. The act provides for operational independence of IR. There are only few instances when there is need for direct interaction with Parliament. They are related to safety, and exemptions and amendments with respect to the Act. The Chief Commissioner of Railway Safety is required to lay down an annual report of the activities of the Commissioners of Railway Safety before Parliament. Exemptions from the rules or inclusion of new rules into the Act also require the approval of Parliament. The separate Railway budget (discussed later), that is presented annually in the Parliament, is more a matter of convention and is not required by the Act.

1.2 Financial Interface between GoI and IR

The financial interface between GoI and IR has three dimensions: budgetary support, IRFC and dividends. The budgetary support is a direct fund input by the GoI into IR for plan investments. The borrowings of IRFC warrant mention in this section as they involve an indirect funding support to IR - The GoI eventually guarantees all IRFC borrowings. The dividend is a 'return' on investment that IR pays annually to GoI.

1.2.1 Plan Funds

From the fifth plan onwards till 1997, it would appear that the government has been trying to reduce the share of budgetary support to IR (Table 1). This could be interpreted as a positive sign (notwithstanding the increasing share of expensive

market borrowings to meet revenue requirements) since at the least it was making IR have to think about improving fiscal discipline. The last few years (Table 1) have seen a reversal in the trend. Budgetary support has swelled to a high of 50%. In absolute terms, budgetary support has crossed Rs 5000 crores, with around Rs 3000 crores being borrowed from the marketplace. This indicates a possible fallback to the previous regime of easy use of public money

One reason for the GoI to support IR is the considerable amount it has to spend on its social obligations. These involve both operations and capital investments. The government explicitly subsidises investments in a few select projects on an annual basis. Table 2 compares the extent of these subsidies on investments with the total budgetary support.

Table 2: Subsidy on capital investment

Years	Subsidy on Investments	Budgetary support by GoI
1997-8	320	1992
1998-9	602	2185
1999-0	685	2588
2000-1	812	3269

Source: Annual Reports and Accounts, 1997-8, 1998-9, 1999-0,2000-1

1.2.2 IRFC

The Indian Railways Finance Corporation was incorporated in 1986 to partly finance the plan outlay of IR by raising funds from the market [Year Book 2000-1]. From 1987-8 onwards, IRFC had started borrowing from the market through tax free bonds having a coupon rate of 9%. Later, taxable bonds were introduced with a coupon rate of around 15%. The funds are used to procure Railway assets such as wagons, coaches and locomotives. They are then leased out to IR for operation at a lease rental of 18%. Table 3 gives an idea of lease payments to the IRFC and the borrowings through the IRFC route.

Table 3: Borrowings through IRFC and lease payments to IRFC

Year	IRFC Borrowings	IRFC Lease Payments
1999-0	2785	2553
2000-1	2818	2823
2001-2	2743	3250
2002-3	3000	3434

Source : 1) Business Line, February 27th , 2002

2) Annual Reports and Accounts, 2000-2001

At present, IRFC is the principal agent for procurement of rolling stock by IR. As of 2000-1, the combined asset value of IRFC stood at Rs 21,707 crores. This is more than the total rolling stock assets of IR obtained through other sources which are valued at Rs 12,309 crores.

IRFC enjoys a high rating in the credit market and posted a profit of Rs 238 crores in 2000-1. In 2002-3, Rs 3000 crores are proposed to be sourced through IRFC. Effectively, this money is being borrowed with the guarantee of the GoI. The IRFC based transaction raises the questions as to whether it might be less expensive on the public exchequer to give the money as budgetary support when the government incurs a 12% interest liability on its finances.

1.2.3 Dividends

A parliamentary committee called the Railway Convention Committee determines IR's rate of dividend payment. The dividend payable by IR during 2002-3 is 7% of the accumulated capital-at-charge provided by GoI. This amounts to Rs 2679 crores that need to be paid as dividend by IR. The average rate of interest on government borrowings being around 12%, the lending by GoI to IR is subsidised. This subsidy could be justified by the social and economic benefits available due to running IR. In the past, the dividend rate of IR has been more than GoI's borrowing rate (Table 4).

Table 4: Comparison of dividend rate with GoI's interest on borrowings

Year	Average RoI on GoI borrowings	Dividend Rate Payable by IR	Dividend Paid (Rs crores)	Total Capital at Charge (Rs crores)	Dividend as a Percentage of the Total Capital at Charge
1950-1	3.16	4	32.5	827	3.9
1960-1	3.57	4	55.9	1,520.9	3.7
1970-1	4.53	5.75	164.6	3,330.3	4.9
1980-1	6.1	5.75	325.4	6,096.3	5.3
1990-1	10	6.5	938.1	16,125.8	5.8
1999-0	12	7	1889.8	39,772.1	4.8

Dividend paid is not the same as the dividend payable due to deferred dividends.

Source: Second Report on Rate of Dividend for 2001-2 and other ancillary matters, Railway Convention Committee (1999), Lok Sabha Secretariat, New Delhi, 2001.

There is provision for deferments of dividend payable, depending on the financial circumstances of IR. During 2001-2, the amount deferred out of the dividend was Rs 1000 crores. This deferred dividend is not liable to interest payments. There is also provision for a moratorium on payment of dividend on investments in new lines during the period of construction and for the first 5 years after it is opened to traffic [Annual Reports and Accounts, 2000-1]. The high amount of deferred dividend payment is a sign of the financial crisis facing IR.

1.3 A Separate Railway Budget?

The present format of a separate Railway budget is a carry over from the British regime. The separation was effected in 1924, on the recommendation of the Acworth committee. The Acworth committee also heralded comprehensive state control over the railway system in India. The recommendations and the cause for a separate budget might have been relevant then. In the light of present circumstances, it is necessary to evaluate the rationale to persist with this tradition. The period preceding the Acworth committee (1900-1925) was one of rapid growth [www.irfca.org]. From 39603 route kilometers in 1900, it had gone up to 61232 kilometers in 1925 (these figures include areas outside present India) [Johnson, 1963]. Railway operations were

in the hands of numerous operators. There was a pressing need for standardisation and regulation to ensure sustained growth. Importantly, IR was among the biggest public investment activities taking place in India at that time

In the present times the situation has changed. In terms of route kilometers, it has increased marginally from 54376 kilometers in 1947 to 63028 kilometers in 2000 [Annual Report and Accounts, 2000-1]. . It is now necessary for IR to upgrade its resources and maintain its assets. Investment on IR no longer occupy a position of budgetary preponderance as in the pre independence period. While the government expenditure on railways as a percentage of total public investment stood at 53.7% and 58.3% respectively in the period 1860-1918 and 1919-1946 [Roy, 2000], according to the 8 th plan, it stood at 6.1% [Expert Group Report, 2001].

To put unnecessary limelight on IR by Parliamentary discussion might hamper its operational freedom. Political pressures affect the spending pattern presented in the budget. The fare structure is another area that is heavily subsidised owing to the political incorrectness of hiking the fare. Appeasement packages like the creation of new zones or the commissioning of new trains might affect the commercial viability of IR. It is important now to work on the sidelines. Reduced prominence is essential to effect the painful surgical alterations necessitated by decades unhealthy practices. Doing away with the separate railway budget will help shear off the perceived political glamour associated with IR. This is probably an essential step to instill a sense of professionalism in IR.

1.4 Issues of Political Interference

1.4.1 Project Related Issues.

The year's break up of investment during 2002-3 is given below in Table 5.

Table 5: Break up of Investment in 2002-3

Head	**Investment**	
	Amounts (Rs. cr.)	Percentage
New lines(construction)	890.67	8.0
Gauge conversion	862.21	7.8
Doubling	610.03	5.5
Traffic facilities	226.21	2.0
Computerisation	139	1.2
Rolling stock	919.19	8.3
Track renewals	3516.5	31.6
Road safety	450	4.0
Bridge works	209	1.9
Signaling and telecommunication	727.05	6.5
Electrification projects	239.17	2.2
Workshops including production units	215.8	1.9
Passenger amenities	200	1.8
Others	1915.92	17.2

Source : Railway Budget, 2002-3

Some of the heads like 'New Lines' are demand based. Demands are received from state governments, Members of Parliament, Ministries of GoI and so on [White Paper, 1998]. The process of project approval is an area of potential political influence. Some projects have obtained clearance even without the feasibility survey being completed or before the Railway board had completed its scrutiny. As on 1998-9, 37 such projects were included in the Railway budgets

This year, track renewals, new lines and gauge conversions are the major heads of investment. While track renewals are important from the point of safety (most of these investments are being met from the Special Safety Reserve Fund), the prioritisation of new tracks and gauge conversion have been questioned in the past. Changes in the center have usually been accompanied by shifts in policy as well. At one time, the focus would be on electrification while later, it would shift to gauge conversion. Table 6 emphasises the point [Expert Group Report, 2001]. This points to

an inconsistency in decision making. Political expediency and individual whims seem dominant on commercial and operation based requirements.

Table 6: Changing focus of IR in its investment decision.

Category	**Total Outlay (Rs Crore)**		**Percentage**	
	1990-1	2000-1	1990-1	2000-1
New lines	356	790	29.8	30.2
Gauge conversion	121	623	10.1	23.9
Doubling	327	646	27.4	24.7
Electrification	235	325	19.7	12.4
Traffic facilities	154	227	12.9	8.7
Total	1193	2611	100.0	100.0

Source: Expert Group Report, 2001

Even in individual projects, there have been cases of patchy investments without adequate follow up. Examples include the Salem Karur line. It was cleared in April 1997. The project was estimated at Rs 229 crores. Rs 43 crores were spent till March 2002 with Rs 15 crores provided in 2002-3. A project of this profile could be completed in three to five years. [Sunday Express, August 11, 2002]. Another example is the Jammu – Udhampur line. Such projects have witnessed spurts of investments followed by periods of lull. Returns on investment are poorly accounted for in these cases. There is a need to ensure that projects are executed according to the predetermined investment patterns.

Another issue concerning project investments is that of inadequate follow up funding after sanction. Projects can be mooted and sanctioned due to a variety of reasons, but it is necessary to follow up with sustained funding towards completion. A failure to do so would lead to a spiraling rise in project costs combined with a mounting backlog of pending projects. Examples include the Munger-Monghyr Ganga Bridge project and the Angamaly Sabarimala railway project, [CMIE CapEx, Feb 2002] where the project

is kept barely alive by inputs of token sums. This is an attitude problem that needs to be addressed. The issue is also one of taking constituencies for a ride by announcing and approving projects never intended for scheduled completion.

In August 2002, the Prime Minister has given the green signal for the National Rail Vikas Yojana. It is envisioned that Rs 15000 crores will be spent within a predetermined time frame of five years for the completion of important projects including the strengthening of the golden quadrilateral, port connectivity and mega bridge construction. This seems to be an implicit mechanism by which part of the budgetary support is getting committed for specific purposes. Such declarations also help reduce the effects of other political vagaries as the IR management is armed with the authority of the Prime Minister's office to focus on certain areas.

1.4.2 Pricing

The issue of passenger fare pricing is a politically sensitive issue. Hardly any government musters the courage to raise passenger fares, especially in the lower classes, to realistic figures. Like petroleum pricing, it probably requires a crisis of sorts to rationalise the fares. In an effort to cover operating expenses, IR has resorted to debilitating cross subsidies. This is both between different passenger classes as well as in subsidising passenger by freight. In a monopolised framework, there is no one to pull the rug from under this imbalanced scheme except for the response from the goods transport users. IR has been steadily losing its share in goods transport to road. The Railway share has fallen from 89% in 1950-1 to 40% in 1995-6 [Status Paper, 1998].

If it can be argued that fare hikes are detrimental to the travelling citizenry, then it is equally if not more harmful to the financial well being of the nation as a whole to

support such dangerously skewed pricing policies. In fact, it is possible that one of the results of below cost transportation being available to a large number of people is the unmanageable crowding of urban centers With the right economies not reflected in migration patterns, naturally untenable agglomerations might be forcibly occurring.

There is a pressing need for management directed towards arriving at a more rational and flexible pricing mechanism in IR. If, due to the ephemeral nature of political power combined with other extraneous pressures, the government is unable to provide the required direction, it only rallies in support of a more independent and professional management of IR.

1.4.2 New Railway Zones

A zonal headquarters is like a holding company of five or six divisions, where a kind of balanced and viable operating position is attempted to give optimum financial and traffic results. The announcements for the formation of new zones and divisions raises the issue of trying to balance local needs versus the operational considerations of IR. Smaller administrative regions of IR will mean that the connectivity and service needs of the local population might find better reflection in the decisions of the railway administration. On the other hand, small zones might end up as uneconomical and unviable tatters.

Political influence on IR is understood in the July 2002 demarcation of new zones and divisions. The zones' formation is largely viewed more as an appeasement of state based demands rather than the operational consideration of IR. The issue of the boundaries of the divisions of the newly formed South Western (SW) Railways based in Hubli brought out this aspect. The Guntakal division was initially part of the South Central (SC) Railway, which is based in Secunderabad. Although the headquarters of

Guntakal division is in Andhra Pradesh, most of its area lay in Karnataka. With respect to the operations of the SW Railways, including most part of the Guntakal division would help in maintaining the contiguity. But state based political compulsions however forced Guntakal to remain with the Andhra based SC Railways. There has been some restructuring of the boundaries of the Guntakal division transferring some areas to the SW Railways but overall, there still remains a compromise in terms of operational suitability. The state factor being more important than operational considerations is also exemplified by the creation of the Bilaspur based South East Central Railway. This zone wasn't part of the first list of new zones marked out for creation by the then railway minister, Ram Vilas Paswan. The fact that the Bilaspur based railway zone got created seems very obviously linked to the formation of the state of Chattisgarh.

A zonal railway that calls for restructuring would be the Northeastern Railway headquartered at Gorakhpur. Originally, it was largely a meter gauge railway with routes intertwining many broad gauge segments of the Northern Railway. With increasing gauge conversion in the Northeastern Railway, it would be more appropriate to have one common zonal administration to fully exploit the multiplicity of broad gauge routes from operational and commercial considerations.

1.4.3 Concessions to Certain Constituencies

Apart from subsidised passenger fares, IR is burdened with numerous concessional fare patterns and free pass schemes. Government stipulated concessions in fare are extended to various categories of society such as recipients of gallantry and National sports awards, participants in national and state sports tournaments, teachers honoured with national awards, Shram awardees, war widows, patients suffering from serious diseases, handicapped persons and so on.

[www.southernrailway.org/pass_info]. Although the government has a prerogative to decide whom it should provide subsidised transportation to, it is unfair to expect IR to bear the burden of those decisions. It would be more accountable if a separate estimate is made of the concessions provided for by IR, with a straightforward reimbursement being made by the government. Apart from the above categories, IR provides tariff concessions to military traffic, postal traffic, transportation of seeds, foodgrain, milk etc. and traffic to the North East region.

The net social service obligation borne by IR in 2000-1 is assessed at Rs 3283 crores [Year Book 2000-1]. This excludes the staff welfare cost of Rs 1143 crores. This loss amounted to 9.31% of the total earnings and 9.64% of the total expenses of IR.

Many previous investments of IR in the form of branch lines have turned out to be loss making. A suitable option to exit from these ventures will ensure IR's ability to function as a flexible, commercial operation. Any such line, if necessary to be maintained for social reasons can be paid for directly by the government and operated by IR.

IR also provides free passes to its employees with generous travel provisions. This being more an internal management issue, it is discussed in the next section.

Seasonal passes are heavily subsidised. At present, the monthly season ticket holders pay for 10 to 19 single journeys as against 50 single journeys normally undertaken in a month. The fares of second class monthly season tickets are fixed equivalent to the fares for 15 single journeys by second class (ordinary) uniformly for all distances. First class season tickets are charged at 4 times the second class season ticket fares. For the first class (value wise), this works out to a much higher subsidy. Quarterly season tickets are charged at 2.7 times the monthly season ticket fares [Railway Budget

Speech, 2002-3]. These facilities are used by around 65% of the passengers in suburban routes and 35% of the traffic in non suburban routes (for distances upto 150 km) [Year Book, 2000-1]. Being a sensitive political issue, IR finds it difficult to reflect reality into the amounts being charged. Subsidised transport leads to demand distortions causing, overcrowding.

By loading IR with these government mooted subsidies, the operating viability of IR as a commercial entity is put under strain. IR then goes to the government to compensate for the losses on account of socially motivated reduced tariffs. The whole business of doling out largesse is eventually out of the pocket of the public exchequer. Better accounting and pin pointed subsidy payment by the government will help to make sure that the excuse of concessions is not used to cover operating deficiencies.

1.5 State Governments

IR derives its right of way from the central government. IR is not obliged to pay any tax to state governments for transportation across states. Hence, in terms of liabilities by IR, there is no interaction between individual states and IR. Of late however, there has begun an initiative aimed at making states participate in the investment activities of IR. The present Railway Budget reveals that a MOU has been signed with the government of Jharkhand in which the government of Jharkhand has agreed to bear 2/3rd of the share in the cost of projects in that state for expeditious completion.

State participation in the execution of railway projects is also expected in Haryana and Karnataka. The case of the Konkan Railways is another example of a successful joint venture between the states of Maharashtra, Goa, Karnataka, Kerala and IR. State participation is also expected to gain a fillip with the recently announced formula (based on the state's own contribution and demographic characteristics) to determine

the distribution of a part of IR's plan investment finances. This is discussed further in the next section.

2.0 Financial Management of IR

This portion of the paper seeks to address issues regarding the internal functioning of IR, about how IR generates its revenues and justifies its expenses and investments. There are obviously places where improvements can be called for and an effort is made to make some relevant suggestions for improved usage of the finances of this public asset.

2.1 The Situation

Table 7 give an idea of how the Railway rupee was earned and how it was spent. The figures are for 2000-01.

Table 7: Earnings and Expenses of IR

Earnings		Expenses	
Head	Percentage	Head	Percentage
Passenger	29	Staff	35
Goods	64	DRF	6
Other Coach	2	Pension	14
Sundry Other	2	Lease	9
Misc.	3	Misc.	36
Total	100	Total	100

Source : Railway Budget 2002-3

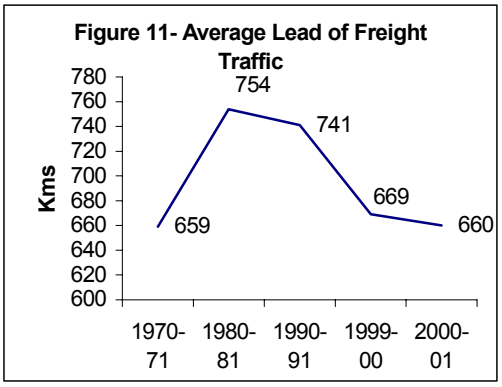
The revenue heads indicate that 64% of the Railway earnings came from the goods sector. In 2000-1, it stood at Rs 23,305 crores. Passenger earnings on the other hand were 10,515 crores. This highlights the revenue generating potential of the freight transport sector and the need to focus attention on goods if IR is to fashion itself to be a commercially viable organisation. The passenger sector at 29% is also big, but in the present pricing scenario it can be thought to be underleveraged.

Among expenses, staff remuneration and pensions are the two dominant heads where controls can be exercised. IR is overstaffed and the fifth pay commission award pushed up staff costs including pension up to 60% of the total expenses. In this situation, it is important to push towards a leaner workforce and greater productivity.

2.2 Revenues

2.2.1 Goods

IR has projected an operating ratio of 94.4% [Railway Budget, 2002-3] for the year 2002-03 and stood at 98.3% for the previous year. This is a dismal figure which provides a very narrow margin which can be used for much needed capital investments. One way to improve this ratio is by boosting the revenues of IR. As mentioned in the previous section, goods transportation should take a priority in the policy of IR. Although overall, there is a growth in the net haulage, IR have been declining as a transporter of choice in the Indian economy. The share of IR against Road is reducing. The average lead is gradually reducing (fig 11) thus indicating that loaded freight is running shorter distances which translates to lesser revenues. At present, IR is depending to a large extent on its captive customers, the Public Sector Enterprises [Year Book 2000-1].



Source: Year Book, 2000-1.

With the disinvestment of many leading PSUs, professional ethics are becoming the norm. The changing face of the Indian economy is also leading to less transportation of bulk goods and a greater value accorded to consumer items. This would mean taking a commercial approach and to ensure IR' viability with respect to road. A few steps IR can take are:

- Providing a *Customer Oriented* outlook to its business operations. Rather than a supply side oriented bureaucratic mentality that presently prevails, it is necessary to maintain customer loyalty by ensuring prompt and reliable service according to the customer's needs. This includes ready availability of wagons and the attraction of piecemeal loads rather than the insistence of rakeloads.
- *Technological Innovations* should be implemented making it possible to run high speed and high capacity freight. This will also help provide for a dedicated *Land Bridge* connecting the East and West coasts. This can present India as an attractive maritime trading country. The effort would entail providing for commodity specific transport vehicles suited to the needs of the customer.

- *Flexible Pricing* mechanisms should be implemented to ensure the most efficient and profitable utilisation of money and resources.
- *Innovative* marketing schemes like the Roll On Roll Off (RORO) can be used to capture road based markets. *Containerisation* can also be promoted. Overall, a focus should be put on the goods segment with the numerous advantages of rail transport properly exploited and marketed.

2.2.2 Passenger

For the last couple of decades, the passenger segment has constituted a 25-30% [Year Book, 2000-1] share of the overall earnings. This is in spite of the priority that has been accorded to the passenger segment in terms of operations. Passenger trains are moved at high speeds and are usually given precedence over the mobility of goods. As the commercial motive increases, passenger earnings will have to justify this preference. If IR are to be able to offer continued and effective transportation, it is necessary to correct gross imbalances in the fare structure and service quality in the passenger sector. Table 8 gives an idea of the imbalances occurring in the fare structure [Year Book 2000-1]. In this table, sleeper class is included in second class figures. The figures are for 2000-2

Table 8: Distribution of PKM and Revenue Earned among the Different Classes

Class	PKM		Revenue	
	Distances	Percentages	Amount (Rs Crores)	Percentages
Upper Class	26315	5.8	2295.2	22.0
Second Class M/E	222568	48.7	5525.8	52.9
Second Class Ordinary	119267	26.1	1571.0	15.0
Suburban	88872	19.4	1091.1	10.4
All Class	457022	100.0	10483.2	100.0

Source: Year Book 2000-1

The figures give an idea of the extent of across the class subsidising that takes place in IR. While the upper class travel constitutes 6% of the share of the distance traveled in passenger kms, it contributes 22% of IR's revenues.

Certain policies which IR can implement to enhance the potential of passenger earnings are given below:

- *Commuters* are a big source of passenger earnings. It is important that steps and mechanisms are undertaken to turn around loss making commuter railways into viable entities. Suburban sector losses are estimated to be Rs 659 crores.
- Since most of the revenue is from better trains and the *Higher Classes*, there is a necessity to exploit the potential for profitability. Good marketing and better quality services along with attractive pricing mechanisms will help capture clientele from alternate road and air options.

  The issue of overpriced higher classes was in the focus due to the price cuts announced by the Airline industry in certain routes. As a consequence, air travel cost less than certain classes in the Rajadhani express. This had forced IR to go into a mid budget rethink of its pricing policy. If effected, the passenger fare cuts will be an unprecedented event. In any case, IR may need to realise that the upper class market might be elastic. Reducing the fares might eventually lead to a higher revenue realisation.
- IR has a very good connectivity touching many important important *Tourist Destinations*. Efforts at marketing them along with special trains for comfortable connectivity will help IR tap into the international tourism market. Increasing the number of theme trains and widening the ambit of the clientele can help rejuvenate its brand image.
- A novel way for IR to boost its revenues through the passenger segment is to exploit the potential of the value of its infrastructure. Trains and Railway stations are a ready *Marketing Platform*. There have been efforts in the past aimed at catching the eyeballs of the multitudes of passengers using the rail system. It is necessary to ensure that the potential for the use of Railway resources as a vehicle for other activities is not left underutilised. The efforts

of IR Catering and Tourism Corporation (IRCTC) can be combined with private enterprise to market and sell the concept of using the Railway premises for profitable activities by interested parties.

- There are 17000 hectares of *Vacant Railway Land*. This is a huge unused asset. IR seem to be making steps towards exploiting this resource as indicated by the proposed Land Development Authority.
- Theme based entertainment/business centers can be developed on the considerable *Real Estate* that IR owns in and around urban areas. The Belapur railway station near Mumbai is only one example of such ventures being possible. This will help IR associate with modern urban lifestyles to bring it closer to its customers

2.3 Subsidies

Rather than involve itself in social debates concerning the right or wrong of policies, IR ought to focus attention on its main job of being a premier logistics agency. Any pricing subsidy that the government feels fit should be surgically implemented with IR being suitably compensated for such external burdens. This well defined accounting practice is essential not only to boost the productivity of IR but to kindle an attitudinal change in the way the Railway looks at its business. There should be less potential excuses to cower behind and more accountability for efficient action or the lack of it.

This perspective needs to be applied on the generous free and subsidised travel provisions that IR provides to its employees and pensioners. According to the Rakesh Mohan Committee report, this perquisite would have cost IR around Rs 500 crores at that time. The Railway point of view is that it is a part of the service condition of the railway employees and denying or taxing it would amount to tampering with their terms of service. Other departments and sectors have also provided such freebies such as the free telephones availed by BSNL employees. The free pass scheme might

also be positively viewed with regard to maintaining good relations with the staff. It will be important to keep in mind the volumes of travel and the costs that the free pass scheme results in. IR needs to have a rethink on this issue with probably a reduction in the number of free passes claimable by employees. Box 1 looks at the free pass and privilege travel order (PTO) issue and tries to get a rough estimate of the magnitude of passenger kilometers and revenue forgone by IR on this account.

2.4 Investments

This section deals with the investment issue from the point of view of the Railway management. There was a pending backlog of Rs 36000 crores in project investments [White Paper, 1998]. Out of this, Rs 25000 crores were for nonviable projects. The projects need to be reviewed regarding requirement and accorded priority in terms of commercial viability.

Unable to meet the costs for its investments, IR is forced to borrow every year from the government either directly in the form of budgetary support or indirectly in the form of market loans from the IRFC under government guarantees. This means that IR is accountable to the public in how it decides on its investments. These investments amounting to around Rs 10000 crores for the present year have a distribution pattern as shown in Table 5.

According to the 2002 status paper, there is going to be a transparent scheme to allocate IR's investment funds:

- The IRFC funds generated from the market are used for meeting most of the rolling stock requirements of IR.

- The internal allocations to the Depreciation, Development and Capital funds are being used for replenishment, upgradation and infrastructure projects respectively.
- Out of the budgetary support, 70% is earmarked for infrastructure projects.
- The remaining 30% of the budgetary support is to be used other than for infrastructure projects.
- 70% of the infrastructure funds (or 49% of the budgetary support) are to be used for projects in the North East, Metropolitan Transportation Projects, Mega Bridges and for states with a 2/3 contribution to the projects.
- 30% of the infrastructure funds (or 21% of the total) are to be distributed based on a formula that accords 15% weightage to the area of the state, 15% weightage to the population of the state and a 70% weightage to the throwforward of the project (throwforward indicates the amount required to complete the project).

This formula is questionable as the throwforward is not necessarily the most crucial factor which should determine the priority of a project. More meaningful transparency can be arrived at by according weightage to the *ratio of the expected returns from the project to the throwforward of the project*.

IR ought to keep track of the significant sums being invested in projects. In this the first stage is the evaluation. At the outset it is necessary to determine the priorities of investment. Once specific projects are identified, a fair appraisal should be made of the financial viability of projects. In the past, certain projects have been pushed forward by either underestimating costs or overestimating returns. The White paper on projects mentions the poor quality of surveys as a result of the pressure of numbers. Survey reports are generally considered defecient to form a satisfactory basis of investment decisions. If necessary, the services of outside consultants/appraisers should be employed for a fair estimate. The number of projects

should be chosen considering present and future resource limitations. Finally, cleared projects should be meticulously followed up to ensure progress according to plan and the final returns compared with estimated returns with responsibility affixed in case of gross inconsistencies. Such rigorous and careful accounting is necessary to ensure that there is no casual attitude towards public money.

Systems to lock in funds to viable projects are essential. The Special Railway Safety Fund (SRSF) and the Prime Minister's National Rail Vikas Yojana are a step in this direction.

2.5 SRSF

The SRSF of Rs 17000 crores is an important investment input for the Railway in the coming few years Its purpose is to facilitate faster modernisation of overaged assets like bridges, tracks, signalling equipment and rolling stock. This investment specification is implemented on the basis of the report of the Justice Khanna committee, constituted after a spate of accidents in the late 90s. It is estimated that over 10975 km (BG) are due for renewal along with 874 Broad Gauge (BG) coaches and 585 EMUs [Status Paper, 2002]. The SRSF involves a government input of Rs 12000 crores and Railway generation (through a special safety levy) of Rs 5000 crores over a period of six yeaRs The necessity of this huge investment indicates the laxity with which IR had been dealing with asset depreciation. The Depreciation Reserve Fund (DRF) is not sufficient to meet IR requirements' and its value as a share of the revenues has been declining. The method of depreciation calculation is based on an outdated British era scheme that needs to be revamped. It is a sorry state of affairs that a vital area like safety has been allowed to accumulate backlogs necessitating the emergency influx of funds now.

2.6 Overstaffing and Cost Reduction

From Table 7 it is clear to note that staff costs occupy a 50% presence in the expenses of IR. A RITES survey has indicated that Railway over staffing could be to the extent of 25%. This is coupled with a low employee to accentuate the problems of a large workforce [Expert Group Report, 2001]. The reduction in staff has been occurring at a very slow pace of 0.07% in 1999-0 and 2% in 2000-1 [Annual Report and Accounts, 2000-1]. Much needs to be done at a faster pace to ensure any meaningful rightsizing. The VRS route is one option. Another innovative idea would be to consider the large and capable workforce of IR as an asset that can be retrained and outsourced to other agencies. This would at the least ensure a good productivity till the numbers reduce sufficiently. In order to reduce direct staff liabilities, non critical and routine jobs can be contracted out in the future to provide a greater accountability and control over the functioning of IR.

Excessive overstaffing can also lead to technical compromises. A case here is of the track maintenance machinery that was purchased at considerable cost. The capabilities of this machinery were left underutilised due to the existence of a large number of employees who did the job manually. This led to wastage of resources and also compromise on the quality and speed of work that might have been possible. A huge permanent workforce restricts IR, reducing the number of options it can exercise and thus affecting its ability to flexibly react to changes in the operating environment.

3.0 Towards Corporatisation.

Corporatisation is a word used here only as a broad indicative direction which to move towards. It might involve procedural restructuring or involve large-scale overhaul of the entire operational and decision making framework. Either way, it is clear that the

status quo is not tenable. This section effects focus on certain issues which might figure in a roadmap for change.

3.1 Financial Issues

One of the most important results that should accompany any change in IR is greater financial accountability. In the present set up, there are too many easy routes the Railway can take. These are in the form of budgetary support, government guaranteed market loans, captive freight markets and so on. Government mooted subsidies and socially oriented schemes should not be railway sponsored with a clear separation of IR role as a transportation solution provider and the government's social obligations.

Functioning as a corporation would entail having to pay taxes and probably something like a license fee for obtaining right of way. It should be noted that from experience, many corporatised PSUs are not yet truly free from the clutches of the government. It should be ensured that Corporatisation is not an end in itself but should indicate a process by which IR will move towards responsibility for its financial health.

3.2 Pensions

This year, the appropriation to the pension fund has been Rs 5990 crores and accounted for over 15% of the expenses [Railway Budget, 2002-3]. With the way pension liabilities have been increasing, the pension bill is all set to overtake the wage bill in coming years Normally IR appropriates the required pension amount from the revenues in the form of operating expenses. There has been no long term planning to take care of pension liabilities. A notional pension fund of around 10% returns would amount to 2/3rds of IR's capital worth. A sign of the changing mentality is that the

recent recruits of the government are contributing towards a pension fund. It is expected that this attitude will apply to IR as well.

3.3 Customer Focus

In the times to come, IR will have to go and look for the customers instead of the present comfortable situation when the customer comes looking. The customer has to be identified and catered to. This would require the use of information systems to assist in the identification and management of customer oriented operations. This shift in operations from the supply side convenience to customer side end result orientation should become evident in the goods as well as the passenger sectors.

3.4 Focus on Core Competencies

In its present form, IR is a huge and nebulous entity. Apart from its main business of operating and maintaining Rail transportation, it has numerous other concerns attached. These range from manufacturing units and construction to other ancillary units like health care, education, catering and the like. For IR to move ahead as a premier logistics solution provider and passenger transporter, it is necessary to focus on its core competencies and spin off whatever is not essential. Steps like the formation of an autonomous CONCOR is a positive sign of the change from unified ownership to discrete focused entities. All sectors that do not require direct involvement can be contracted away. This would ensure that the attitude of the side units of IR will also gear up to professionalism. Here it can be noted that previous corporatisations like RITES for consultancy and IRCON for construction have been making profits since their inception [Status Paper, 1998].

3.5 Change in Administrative Structure and Attitude

The present administrative structure of IR suffers from numerous shortcomings. The closeness to the government which leads to unwanted political interference has already been mentioned earlier. Apart from this there are also the problems associated with a bureaucratised internal setup. Rampant departmentalism is a problem often mentioned in reports and analyses. This requires a shake up in the administrative structure and functioning of IR. One solution would be to create an independent management structure for IR to oversee operations and planning. A statutory Railway authority can be created for overall regulation and coordination of IR towards safeguarding the interests of the government.

IR sorely requires of a sea change in attitude. It would mean looking at the whole business of running a Railway as a commercial activity rather than as a national service. The innovative ideas implemented in the Konkan Railways after being pushed to the brink give an idea of how being motivated by commercial profit oriented motives can contribute to a vibrant operational outlook.

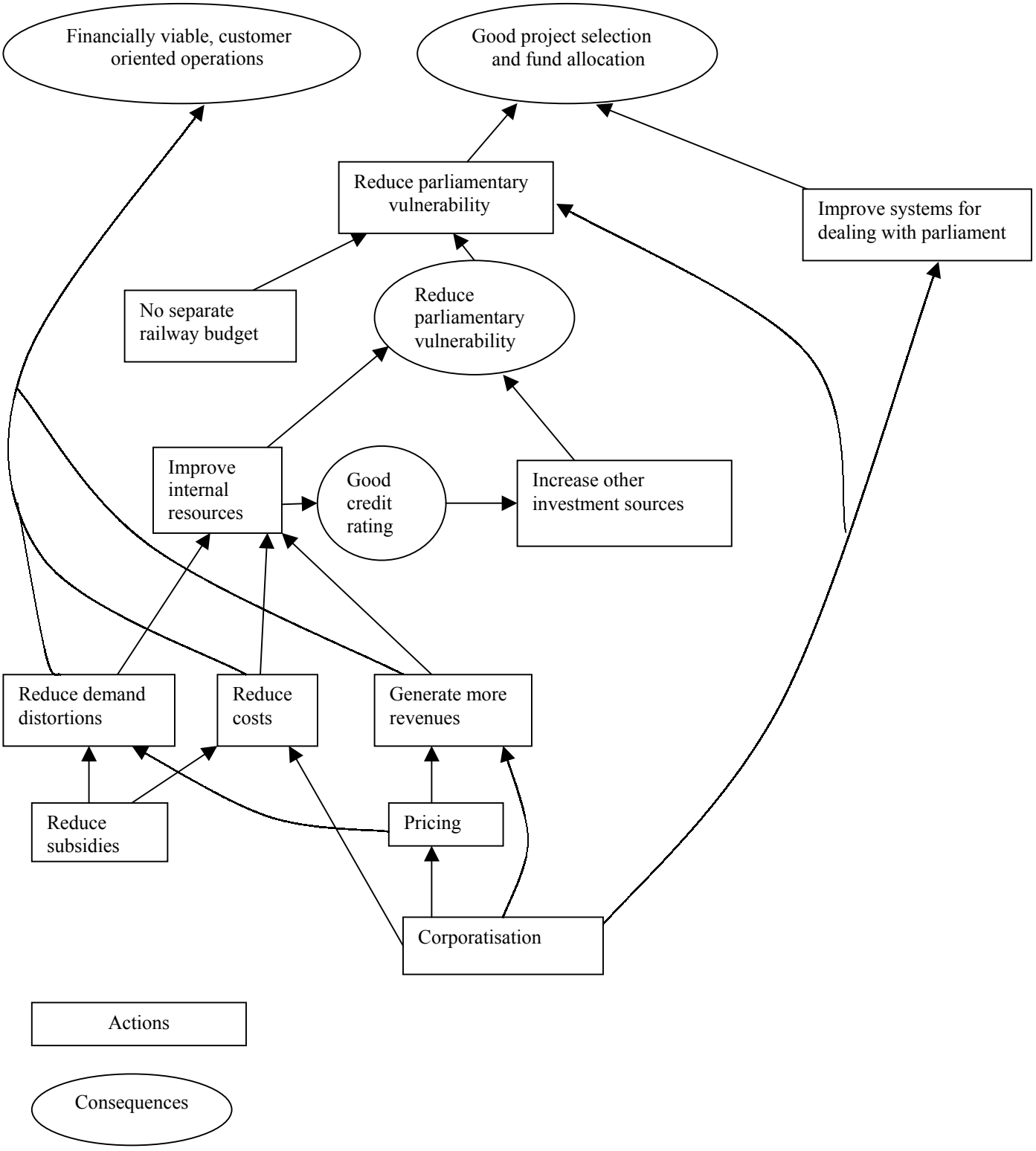
It should be remembered that the Railway system in India was originally created to cater to the commercial and administrative interests of the British. It grew initially as many privately owned Rail systems motivated by profits and government guarantees. The present IR is only 50 years old and has hardly matched the energy and growth witnessed in the years of rapid expansion in the early 1900s. The function of IR amounts largely to maintaining and running the British era framework. There has only been a minimum impetus and change largely in the form of additions and upgradations in technology. The need of the hour for the Railway system seems that it must be let free. If it survives, it should do so as a healthy and contributing entity.

Summary

Figure 15 summarises the essence of this paper. Consumer oriented operations along with financial viability (sections 2.1, 2.2, 2.3), and good project selection and fund allocation towards projects (sections 1.4.1, 2.4) are the two main desirable objectives of public expenditure accountability. Reducing Parliamentary vulnerability is important to manage projects professionally. The separate railway budget is an impediment that can be done away with (section 1.3). But to begin with it is necessary to reduce the dependence on budgetary support which brings with it the baggage of political interference (section 1.4). This can be achieved by improving internal resources which will also improve the credit rating of IR allowing the tapping of market funds (Section 1.2.2). The three main ways to improving internal resources are by generating more revenues (section 2.2), reducing costs (section 2.6) and by reducing demand distortions (section 1.4.2). These three factors also directly contribute to the financial viability. In terms of actions, the reduction of social subsidies (sections 1.4.4, 2.3) and a more flexible and rational pricing mechanism are essential (sections 1.4.2, 2.2.1). In the broader sense, the path leading to corporatisation (section 3) can be seen as bringing about this transformation in IR. Corporatisation will also facilitate improved systems for IR's dealings with parliament hence reducing parliamentary vulnerability. These systems include more focused project selection and visibility through schemes like the Prime Ministers National Rail Yojana and the SRSF (section 2.5), rules for transparent allocation of investment funds (section 2.4) and a 'ring fenced' budgetary support to meet the expenditure on social obligations (for example, explicit capital subsidy – sections 1.2.1, 1.4.4).

Figure 15: Towards Improvement of Expenditure Accountability in the IR

A scheme of Linked Action



[To be put as Box 1]

Free Pass Scheme and Privilege Ticket Orders (PTOs):

We estimate below the annual subsidy in PKM and revenue due to the free pass scheme and the PTOs (travel provided at 1/3rd the price) that IR employees enjoy and the free passes available to the pensioners of IR.

The eligibility for free passes and PTOs, which is a part of the service condition has varied over the years. The present estimate of average eligibility for employees and pensioners is as follows. The class wise distribution of pensioners is based on the distribution of employees.

Employee group	A	B	C	D
Number of free passes	6	6	3	2
Class eligibility	AC II/AC I	AC II	AC III/AC II	Sleeper
Number of PTOs	4	4	4	4
PTO class eligibility	AC II/AC I	AC II	AC III/AC II	Sleeper
Number of employees	7,800	6,900	9,00,000	6,30,000
Number of free passes (pensioners)	3	3	1	1
Class eligibility (pensioners)	AC II/AC I	AC II	AC III/AC II	Sleeper
Number of pensioners	5,700	5,100	6,58,000	4,61,000

On the basis of discussions with IR personnel, the following assumptions are made on the usage pattern of free passes and PTOs. Each of the free passes can be availed by all the family members of the employee. The average family size of each emplyee class for employees and pensioners is also shown.

Employee group	A	B	C	D
Average family size for employees	4	4	4	4
Average number of free passes used	3	3	3	2
Class usage	ACII	ACII	80% AC III, 20% AC II	Sleeper
Lead	1000 km	1000 km	1000 km	1000 km
Average number of PTOs	2	2	2	2

used (50% of eligibility)				
PTO class usage	Sleeper	Sleeper	Sleeper	Sleeper
Lead assumed	500 km	500 km	500 km	500 km
Average family size for pensioners	1.5	1.5	1.5	1.5
Average number of free passes used (pensioners) (100% of eligibility)	3	3	1	1
Class usage (pensioners)	AC II	AC II	80% AC III, 20% AC II	Sleeper
Lead assumed	1000 km	1000 km	1000 km	1000 km
Total BPKM calculated	Class A	Class B	Class C	Class D
Employees' free pass scheme	0.09	0.08	10.80	5.04
Employees' PTO scheme	0.04	0.04	2.40	1.68
Pensioners' Free pass scheme	0.03	0.02	0.99	0.69

We have calculated the BPKM lost on account of subsidised travel on the basis of the above assumptions. An example of the calculations involved is given as the BPKM on account of Class A employees using the free pass. In this case it would be 7800*4*3*1000=0.09 BPKM, where 7800 is the number of employees, 4 is the average family size of the employee, 3 is the number of passes used by an employee on an average and 1000 km is the average lead of travel. In the case of calculations for the PTO usage, the travel figure is multiplied by 2/3 as it involves payment of one third of the ticket price.

Though these assumptions are not substantiated by any study, we believe they are very conservative. We are not considering similar subsidies in suburban travel. According to the expert committee report, 'there appear to be widespread abuse of the facility by beneficiaries. There is also the issue of overuse of travel allowances due to non-cancellation of a pass once used. Apart from the passes considered, there are also other schemes such as the students pass or the free travel for accompanying attendants and guardians. A study in this area is essential in the context of public expenditure accountability and would become a necessity if these privileges were to get taxed, as has been proposed by the GoI.

Subsidy in PKMs ***BPKM = Billion Passenger Kilometers***

The break up of the tally of employee and pensioner subsidised travel in BPKM is as follows :

	Class	PTO (500 km lead)	Free Pass (1000 km lead)	Total
Upper	AC II tier	0.00	2.57	2.57
	AC III tier	0.00	9.43	9.43
	Sleeper	4.16	5.73	9.89

Total	4.16	17.74	21.90

This gives a total of 21.9 BPKM. This works out to 5.9% of the total non suburban travel of 368.1 BPKM and 4.8% of the total travel of 457.0 BPKM (2000-1 figures).

Subsidy in Revenue

To calculate the revenue subsidy, we use the cost per PKM for the relevant lead for each class of travel and multiply by the BPKMs.

The cost (paise per PKM) the 2000-1 IR timetable is.

Mail/Express Sleeper Class (1000km lead) : 27.0
Mail/Express Sleeper Class (500km lead) : 32.2
Upper Class - AC III tier (1000km lead) : 78.3
Upper Class – AC II tier (1000km lead) : 125.3

The break up of the revenue lost (Rs Crore) is as follows:

Class		PTO (500km lead)	Free Pass (1000km lead)	Total
Upper	AC II tier	0.00	322.02	322.02
	AC III tier	0.00	738.36	738.36
Sleeper		133.95	154.71	288.66
Total		133.95	1188.69	1349.04

This gives a total potential revenue of Rs 1,349 crores, which equals 14.4% of the total non suburban passenger revenue of Rs 9,392 crores and 12.9% of the total revenue of Rs 10,483 crores (2000-1 figures).

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