Chapter IV

4. TRANSACTION AUDIT OBSERVATIONS

Important audit findings emerging from test check of transactions made by the State Government Companies/Corporations have been included in this Chapter.

Government Companies

The Kerala Minerals and Metals Limited

4.1 Wasteful expenditure due to lack of due professional care

Failure to ensure source of finance, assess market situation and lack of due professional care resulted in issue of purchase orders for machinery/ erection, its subsequent cancellation and wasteful expenditure of Rs. 58.57 crore.

The Company is engaged in the production and sale of Titanium Dioxide Pigment (TDP). As envisaged in the corporate plan for expansion and modernisation (June 2003), the Company took up (2004-2007) implementation of expansion scheme for enhancement in production capacity for TDP from twenty two thousand MT to one lakh MT per annum in three phases (eight projects). The estimated cost of the projects was Rs. 760 crore, proposed for funding from own resources. This was based on the projection that Company had equity and reserve fund of Rs. 327 crore, fixed deposit of Rs. 187 crore and was making profit since 1999-2000, which was expected to continue in future also. The technical consultancy for carrying out the expansion project was entrusted (January 2004) to MECON, Ranchi, on total responsibility basis, which included preparation of Detailed Project Report (DPR) also.

Audit observed (January 2009) that the Company, even before the submission of DPR, which was essential for taking any investment decisions, issued (January 2005-July 2006) orders for machinery/ erection valuing Rs. 431.19 crore. According to the DPR submitted (June 2006) by MECON the estimated cost of the project on completion was projected at Rs. 1,115 crore against the originally estimated cost of Rs. 760 crore, an escalation of 47 *per cent*.

In view of enormous escalation in cost, the Board of Directors constituted (July 2006) a sub-committee to review the project and to submit recommendations. The sub-committee recommended (December 2006) to implement the expansion scheme after re-considering the financial situation, profit expectations and growth, debt servicing, stagnancy in the market situation, development, vigilance and legal implications.

The Board of Directors after considering the recommendations decided (February 2007) to abandon four projects involving capital cost of Rs. 500 crore (Mineral Separation Plant-Rs. 120 crore, Synthetic Rutile Plant-Rs. 250 crore, Oxygen Plant-Rs. 90 crore and Desalination Plant- Rs. 40 crore) subject to Government approval. The Government of Kerala accorded (January 2008) approval for the abandonment of these projects considering the fiscal position of the Company. The Board of Directors decided (March 2008) to abandon the remaining four projects also, involving a capital cost of Rs. 260 crore subject to Government approval which was awaited (September 2009). However, the cancellation of purchase orders did not take place so far (September 2009).

As a result of abandonment of the project, the purchase orders for machinery/ erection valuing Rs. 431.19 crore issued (January 2005 to July 2006) became unnecessary and amount of Rs. 58.57 crore (including consultancy fee of Rs. 18.62 crore) towards Desalination Plant, Oxygen Plant, Dredge and Wet Contraction Plant etc., incurred became wasteful expenditure.

Management stated (January 2009) that despite increase in production of TDP (2001-2008) the profitability had decreased drastically due to decrease in customs duty, appreciation of Rupee against US Dollar, lack of market demand etc., and expansion in production capacity of TDP to one lakh MT per annum was not desirable without expansion of supplies of raw material (ilmenite, synthetic rutile etc) and utilities (oxygen, nitrogen etc.).

Audit observed that the Management had taken up (2003) implementation of the expansion project involving investment of Rs. 760 crore by taking into consideration the reserve fund and equity and fixed deposit of Rs. 514 crore and anticipated profits in future years, while ignoring the fact that the Company was selling TDP at reduced prices from 2001-02 itself due to stiff competition from Multi National Companies (MNCs). The market share of the Company in 2003-04 was only 46.80 *per cent* for local demand and 29.30 *per cent* for domestic demand, due to poor quality of the product as compared to that of MNCs. The profit of Rs. 111.48 crore in 1999-2000, had declined to Rs. 49.65 crore in 2003-04, and to Rs. 17.82 crore in 2005-06 due to unfavourable market situation, when the company issued (January 2005-July 2006) purchase orders for machinery / erection valuing Rs. 431.19 crore. Moreover, the decisions were not taken based on the DPR or any other investment plan. However, the decision to abandon the project was based on the receipt of DPR (during June 2006).

Audit concludes that it is a case of deficient planning. The Company was overambitious in estimating its capabilities to ensure source of finance for the project, but ignored to assess the market situation and failed to exercise due professional care resulting in issue of purchase orders for machinery/ erection. Thus, payment of advance of Rs. 58.57 crore for purchase orders became wasteful, due to subsequent abandonment of projects and the amount otherwise available for meeting working capital requirements, had eroded due to wasteful investment. The Company had also invited future liability towards consequential losses due to cancellation of purchase orders and litigation. The Company should ensure the viability before embarking upon such major expansion projects in future.

Management stated (April 2009) that the finance for the expansion project was to be sourced from internal generation and external borrowings. As the profitability was down, the expansion schemes earlier envisaged in the corporate plan were found to be unfeasible and therefore, abandoned, with the approval of the Government. The reply is not acceptable as deficient planning without ensuring source of funding coupled with hasty decision to place purchase orders for machinery resulted in wasteful expenditure of Rs. 58.57 crore on abandonment of the projects.

The matter was reported to Government in March 2009; their reply was awaited (September 2009).

4.2 Avoidable Expenditure

Failure to purchase balancing equipments for the production of Synthetic Routile at an appropriate time resulted in cash loss of Rs. 18.55 crore on purchase of Synthetic Routile from outside sources and interest loss of Rs. 56.16 lakh on idle investment in digesters.

The Company had (2003-04) an installed capacity of 30,000 MT per annum (July 2003) for the production of Synthetic Routile (SR) also known as beneficiated ilmenite which is the input for production of TDP. At the same time, the synthetic routile plant had six Rotary Globe Digesters (Digesters) and four balancing equipments (Calciners, Roasters etc) rendering two digesters excess. The wasteful expenditure of Rs. 2.62 crore on these two redundant digesters was commented in the Report of the Comptroller and Auditor General of India (Commercial) for 2003-04 (Paragraph 2.1.30).

In July 2003 the Company also had an approved project proposal for increasing the annual production capacity for SR from 30,000 to 55,000 MT by installing two more digesters, one calciner and one roaster and other related equipments, with a capital outlay of Rs. 40 crore. The work order for supply/installation of two digesters was placed (May 2004) at a contract price of Rs. 1.60 crore with period of completion as February 2005. Despite knowing that, the digesters would not be operational without other balancing equipments such as calciner, roaster etc., the Company did not initiate action to purchase balancing equipments (July 2003-May 2004).

In February 2005, because of serious problems in disposal of waste, the proposal for increasing the capacity for SR production from 30,000 to 55,000

MT was dropped. According to the Management (June 2007) in the absence of adequate capacity for production of SR, the Company would have to purchase SR from outside sources incurring additional expenditure of Rs. 10,000 per MT. The Company had already created surplus capacity for digesters for 20,000 MT, which would ensure annual savings of about Rs. 16.87 crore, provided balancing equipments (Calciner, Roaster etc.) involving an amount of Rs. 27.98 crore were purchased/ installed.

The two digesters received (March 2005) were commissioned (November 2007, January 2008) at the cost of Rs. 3.65 crore of which Rs. 3.12 crore was paid as of March 2006. However these digesters could not be put to use for want of balancing equipments.

After the commissioning (January 2008) of two more digesters, the Company had eight digesters resulting in excess capacity, which could not be fully utilised for want of balancing equipments. In the absence of matching capacity, the Company had to purchase 20,043 MT of SR at prices higher than the variable cost of SR produced by the Company, during the two years 2006-2008 resulting in avoidable expenditure of Rs. 18.55 crore.

Thus, the defective and deficient planning in assessing the capacity for SRs envisaging savings and failure to safeguard the financial interest of the Company resulted in cash loss of Rs. 18.55 crore on purchase (2006-2008) of 20,043 MT of SR from outside sources at higher prices. Further an investment of Rs. 3.12 crore on the two digesters had also remained (April 2006 - March 2008) idle which resulted in loss of interest of Rs. 56.16 lakh (calculated @ 9 *per cent* per annum).

The matter was reported to Government/ Management in May 2009; their reply was awaited (September 2009).

4.3 Payment of inadmissible overtime wages

Erroneous calculation of hourly rate of overtime wages resulted in payment of inadmissible overtime wages to the extent of Rs. 2.92 crore.

The Company has two plants, Mineral Separation Plant and Titanium Dioxide Pigment (TDP) unit. The Company has been paying overtime wages to workers engaged in the TDP unit other than office staff for duty in excess of nine hours a day or forty eight hours a week in line with the provisions of Factories Act, 1948. Overtime wage was payable at double the ordinary rate of wages.

The Company paid (April 2006 to March 2009) overtime wages amounting to Rs. 12.27 crore to workers employed in manufacturing process.

Audit noticed (March 2009) that for working out the hourly rate of wages in a month, the Company had reckoned 180 hours (24 days X 7.5 hours) as the standard whereas as per the Factories Act, the effective hours per month was 240 hours (30 days X 8 hours) even though there was no specific provision for this in the wage settlement with the workers. As a result of this erroneous calculation of hourly wage, the company had paid excess overtime wages of Rs. 2.92 crore to workers employed in the TDP unit during April 2006 to March 2009.

Thus, erroneous calculation of hourly rate of overtime wages resulted in excess payment of overtime wages amounting to Rs. 2.92 crore.

Government stated (July 2009) that, on being pointed out by Audit, the Company modified the method of calculation of overtime wages reckoning monthly working time as 240 hours. The Company, however, had to restore the earlier method owing to objections of trade unions.

It is suggested that the Company shall, in the absence of any wage settlement agreement to the contrary, comply with the relevant provisions of the Factories Act on payment of overtime wages in order to obviate inadmissible over time wages.

Kerala Agro Machinery Corporation Limited

4.4 Committed loss due to short-collection of sales tax

Decision to collect sales tax at concessional rate on inter-state sales, contrary to the provisions of Kerala Value Added Tax Act, 2003 and Government clarification thereon, resulted in a committed liability of Rs. 3.72 crore.

The Company, engaged in the manufacture and sale of agricultural implements was allowed (August 1991) to levy Central Sales Tax (Kerala) at a concessional rate of two *per cent* against the general rate of four *per cent* in respect of inter- state sale of power tillers under Section 8(5) of the Central Sales Tax Act, 1956 (CST Act). In April 2005, Kerala Value Added Tax Act, 2003 (KVAT Act) was introduced by the Government of Kerala by repealing the CST Act and rescinding all the existing concessions given under Section 8(5) of the CST Act.

The Company, however, continued to collect CST on power tillers at concessional rate of 2 *per cent* during 2005-2008 against the general rate of four *per cent* during 2005-2007 and at three *per cent* during 2007-08 on the presumption that the concessions would be reinstated by the Government as the monthly sales tax returns continued to be accepted by the Sales Tax Department without any objection. Sales tax returns are finally accepted by the

Sales Tax Department only at the time of completion of assessment at a later date. Amount of Sales tax short collected on inter-state sale of power tillers in the period 2005-08 aggregating to Rs. 203.71 crore was Rs. 3.28 crore.

According to Section 31(5) of KVAT Act, delayed payment of differential tax between the general and pre-KVAT Act rates attracts simple interest at 12 *per cent* per annum. After a lapse of thirty months (April 2005 - September 2007) the Company requested (October 2007) the Government to restore the concessional rate of two *per cent* on inter-state sale of power tillers with retrospective effect from April 2005. The request was not accepted (April 2008) by the Government on the ground that all earlier notifications issued under section 8(5) of the CST Act, had been rescinded consequent upon notification of the KVAT Act.

Thus, the decision of the Company to continue to charge concessional rate of sales tax despite knowing that it was in violation of the provisions of KVAT Act resulted in a committed loss of Rs. 3.72 crore (including simple interest of Rs. 43.65 lakh) to the Company (during the three years 2005-08). As the concession in CST stood withdrawn from April 2005, the Company should have started collecting CST at normal rate with immediate effect.

The Government, in interim reply, stated (May 2009) that the State Taxes department had informed that individual exemptions are not contemplated in the VAT scenario and there is no provision in the KVAT Act for reduction of CST with retrospective effect. Accordingly the Taxes department rightly rejected the request of the Company. Although the Company has requested for waiver of the liability, the fact remains that these sales were already concluded and that the differential tax is irrecoverable from the customers. Thus, the Company will have to bear the liability for payment of sales tax short collected plus interest thereon of Rs. 3.72 crore.

Bekal Resorts Development Corporation Limited

4.5 Avoidable loss of interest on lease rent and undue favour to licensees

Decision to waive interest on defaulted lease rent resulted in a loss of income of Rs. 4.20 crore and undue favour to licensees.

The Company entered (February 2004 and December 2005) into agreements with five[1] private parties for the allotment of resort sites, developed in 164.40 acres of land on lease basis, at rates agreed upon on tender basis. The licence period was initially for two years from the date of agreement, within which period, each licensee was to develop resorts of five stars or above status in the sites provided and lease deeds were to be executed on completion of

[1] Escapade Resorts Private Limited, Air Travel Enterprises India Limited, Khanna Hotels (Pvt.) Ltd., Holiday Group of Companies and Bharath Hotels Limited.

construction of resorts and commencement of commercial operation. The licensees had to pay a licence fee of Rs. 1 lakh each as advance before the end of April of every year and lease rent from the date of expiry of two years. It was the duty of the licensees to obtain all Statutory and legal clearances from the local/municipal/Government agencies for the construction of the buildings.

One[2] resort site was surrendered (March 2008) as coastal regulation zone clearance could not be obtained from the Government, rendering investment of Rs. 3.32 crore on 33.39 acres unfruitful. Resort could not be constructed in another site[3] due to the failure of the Company in providing a railway gate and peripheral road, though, licence agreement was executed as early as in December 2005, resulting in idle investment of Rs. 3.42 crore on 45.94 acres and consequent loss of income by way of rent amounting to Rs. 35.27 lakh per annum since December 2007.

In the case of remaining three sites[4], though the licence agreements were executed as early as in February-May 2004, the licensees did not take proper action to construct the resorts and commence commercial operation within two years, due to their failure in obtaining the Statutory clearances. The Company decided (October 2007) to give moratorium for payment of lease rent for two years, on condition that accrued rent during moratorium period shall be paid in four half yearly instalments, with interest at PLR rate, commencing from the completion of moratorium period (February - May 2008). Two parties[5] remitted (February / June 2008) the first instalment of lease rent and all the three parties[6] requested to extend the licence period upto December 2008.

Accordingly, the Company decided (September 2008) to give moratorium for payment of lease rent for a period of three years after the expiry of licence period and the accumulated licence fee (Rs. 3.08 crore) was allowed to be spread over during the remaining lease period of 25 years commencing from February / May 2009. The Company also decided to waive the interest (Rs. 4.20 crore) on defaulted lease rent, computed at 7.5 *per cent* for the first three years and ten *per cent* thereafter. Necessary supplementary agreements were also signed (December 2008) with two parties[7].

The decision of the Company to waive the interest on defaulted lease rent due to failure of licensees in getting clearances from designated agencies, without the request of the licensees and purchase of unsuitable land for resorts in two locations resulted in avoidable loss of interest income of Rs. 4.20 crore and undue favour to licensees. Further, wasteful / idle investment of Rs. 6.74 crore on 79.33 acres of land resulted in loss of income from lease rent of Rs. 35.27 lakh per annum.

[2] Escapade Resorts Private Limited.
[3] Air Travel Enterprises India Limited.
[4] Bharath Hotels Limited, Khanna Hotels (Pvt.) Limited, Holiday Group of Companies.
[5] Khanna Hotels (Pvt.) Ltd and Holiday Group of Companies.
[6] Khanna Hotels (Pvt.) Ltd., Bharath Hotels Limited and Holiday Group of Companies.
[7] Khanna Hotels (Pvt.) Ltd. and Bharath Hotels Limited.

The Management/ Government stated (May, July 2009), that the three licensees had not complied with the basic lease agreement provisions on construction of resorts, remittance of licence fee and lease rent and the Company had taken rigorous steps to collect the arrears. It also stated that the defaulting parties represented that the delay in completing the construction was due to delay in getting statutory clearances from Government of India and requested for extension of licence period and time for payment of lease rent. Therefore, the Company decided to extend lease period and give moratorium for payment of lease rent, waiver of interest on defaulted lease rent etc.

However, the decision of the Company to waive the interest (Rs. 4.20 crore), *suo moto*, resulting in undue favour being given to licensees was uncalled for.

Kerala Police Housing and Construction Corporation Limited

4.6 Avoidable loss of interest

Failure of the management in evaluating fund requirements resulted in avoidable loss of interest of Rs. 1.10 crore due to depositing funds in call deposits account.

The Company was having sums ranging from Rs. 33.78 crore to Rs. 41.44 crore in call deposits with State Bank of Travancore during 2007-08, earning interest at 4.5 *per cent* per annum. The amounts deposited in call deposits were the withdrawals from Treasury Personal Deposit (TP) Account intended for keeping funds received towards Central/ State Sponsored Schemes for modernisation of police forces. The minimum monthly balance maintained in call deposits during the year 2007-08 was as given below:

Month	Amount (Rs. in crore)
April 2007	33.78
May 2007	33.83
June 2007	38.33
July 2007	36.78
August 2007	38.71
September 2007	37.93
October 2007	40.66
November 2007	40.16
December 2007	44.64
January 2008	44.39
February 2008	43.39
March 2008	41.14

While the Company was withdrawing funds ranging from Rupees five crore to Rupees six crore from TP account every month, for depositing in call deposits, day to day expenses were met through transfers from call deposit account, of sums ranging from Rs. 0.76 crore to Rs. 5.75 crore, every month to current account with State Bank of Travancore.

Audit observed (March 2009) that the minimum balance held in call deposit account during 2007-08 was Rs. 33.78 crore and had the Company deposited at least Rs. 33 crore in fixed deposits for 180 days with bank fetching minimum interest rate of 6.75 *per cent* per annum, the Company would have earned additional income of Rs. 1.10 crore (after adjusting Rs. 1.13 crore actually received as interest on call deposits) during the year.

The reply of the Management (November 2008) endorsed by the Government (April 2009) stated that funds received from Government of India in respect of Centrally Sponsored Schemes are deposited in call deposits, as Clause 17 (xii) of the Articles of Association of the Company authorises to operate only call deposits and current accounts as the funds deposited by various agencies will be required for payment of work bills of various schemes executed. The Board of Directors has already directed the Managing Director to keep the unutilised funds in fixed deposits for a period ranging from 30 days to one year. However, as suggested by Audit, necessary amendments in the Articles of Association will be made later. The reply is not convincing as the Management failed to evaluate the actual fund requirements periodically and deposit the surplus funds in fixed deposits fetching higher rate of interest by amending the Articles of Association following the procedure as per section 31 of the Companies Act, 1956 as Memorandum of Association (clause III B (ii) permitted the investment of surplus funds in any manner other than in shares and stock). Thus, the Company had to forego an income of Rs. 1.10 crore. The Company should take immediate steps to amend its Articles of Association so as to safeguard its financial interests.

Indian Institute of Information Technology and Management-Kerala

4.7 Loss due to want of mandatory approval for technical courses

Failure to obtain mandatory approval for conduct of technical courses and absence of independent own campus arising from non-provision of necessary land by the State Government resulted in uneconomic working and loss of Rs. 5.69 crore.

The Company was formed (September 2000) with the objective of conducting various educational and training programmes in Information Technology (IT) and Management and to give consultancy services to Government of Kerala in its drive for computerisation. It started a post graduate diploma course in IT beginning June 2001 session with 60 seats for B.Tech / BE and MCA graduates at a fee of Rs. 0.75 lakh without obtaining the mandatory recognition from the All India Council for Technical Education (AICTE) to conduct such courses. The Company at this stage was not having its own campus and other infrastructure in stipulated minimum of eight to ten hectares of land to run an educational institution as per the provisions of the AICTE Act, 1987. The Government of Kerala allotted (2003) ten acres (4.07 hectares) of land to the Company at Thiruvananthapuram to build its campus but withdrew the allotment in 2003. The Company meanwhile upgraded (2005) the diploma courses into post-graduate diploma courses [MS (IT)] at a fee of Rs. 1.50 lakh. This was again without obtaining the mandatory approval of AICTE and creating basic educational infrastructure facilities.

The Company was served (March 2007) a show cause notice from AICTE for conducting technical education programmes without their prior approval. AICTE directed (June 2008) the Company to close down the technical courses conducted by it citing unsatisfactory reply to show cause notice and submit a fresh proposal for approval. But, the Company neither terminated the courses, nor applied for fresh sanction to conduct the courses leading AICTE to categorise (2006-07) the Company in the list of unapproved institutions conducting technical courses. AICTE also advised students not to take admission in the courses conducted by the Company, as it had consequences in terms of their eligibility for employment, higher studies etc.

As against the planned student strength of 60, the number of students joining the institution in the first year (2001-02) were 49, which increased to 65 in 2003-04 and started declining from 2004-05 (60) and to a mere 12 in 2008-10. There were ten faculty members taking classes for 12 students as of March 2008 whereas the Company had been incurring huge expenditure on pay and allowances, electricity, rent, entrance test and other educational expenses etc.

According to the Memorandum and Articles of Association, the Company was envisaged to be run on no profit-no loss basis. As the income by way of fees collected from the students was not sufficient to run the institution, the Company was incurring continuous losses since inception (2001) and its accumulated losses stood at Rs. 5.69 crore as on 31 March 2008.

This failure of the Company to obtain mandatory AICTE approval for its technical courses due to non-fulfillment of criterion and absence of independent own campus arising from non-provision of necessary land by the State Government resulted in uneconomic working and a loss of Rs. 5.69 crore.

The Management stated (January 2009) that the contribution of the Company could not be gauged merely by looking at the expenditure in relation to student fee received. There has been added emphasis on research activities and development efforts to social sector. This contention of the Management is not convincing as the fact remains that there was an adverse impact on the eligibility / acceptability of technical / professional education imparted to students in the absence of any recognition/approval from AICTE. The action of the Company to start courses without mandatory approval was in disregard of the extant law / regulations. Further the Company did not follow prudent financial management practices to run the institution on a no profit-no loss basis as per Memorandum of Association.

Government replied (June 2009) that the substantial portion of the expenditure incurred has gone towards creation of basic infrastructure and also intimated that 0.96 acres of land has been allotted, appointed an architect and the work would be tendered soon. Necessary action has also been taken for obtaining affiliation / approval of a University / AICTE.

Audit suggests that the Company should start technical education courses only after obtaining due permission from controlling bodies to avoid conflict of interest. In the instant case, the responsibility should be fixed for violation of mandatory provisions and consequent loss.

Kerala Transport Development Finance Corporation Limited

4.8 Undue favour to Shriram Investments

Avoidable loss and undue favour to Shriram Investments Limited, a marketing agency, by allowing them to enter into agreement with loanees and to collect security deposits of Rs. 6.42 crore.

The Company formed with the main object of financing Kerala State Road Transport Corporation and to assist other transport undertakings started (October 2001), a direct lending scheme to transport operators in Kerala viz., Small Road Transport Operators (SRTO) loans scheme, as proposed by Shriram Investments Limited (SIL), Chennai, engaged in arranging finance for heavy commercial vehicles. According to the agreement (October 2001) with SIL, the Company was to finance 100 *per cent* of invoice price of chassis of vehicles and 75 *per cent* of body building cost of new vehicles and 50 *per cent* of assessed value of used / second hand vehicles with 25 *per cent* margin money, based on the select list of borrowers prepared by SIL.

The loans in respect of new/ used vehicles were to be repaid in sixty / forty eight, Equated Monthly Instalments (EMI) commencing from the end of second month of sanction of loan. The rate of interest at the time of sanction of loan remained unchanged throughout. SIL was entering into agreements with the loanees and collecting instalments from borrowers. The Company's security for loans was the corporate guarantee by SIL, personal guarantee of individual transport operator, personal guarantee by the Directors of SIL and all the vehicles financed by the Company should be hypothecated in favour of the Company and the fact noted/ exhibited on the vehicles.

According to the agreement (Clause 9), SIL was entitled to collect service charge not exceeding three *per cent* and ten to twenty *per cent* of loan amount as security deposit from the borrowers. In order to make transactions between the borrower and SIL transparent, SIL requested (October 2003) the Company to enhance the rate of interest on loans from 12.5 *per cent* to 14.5 *per cent* with effect from November 2003. This difference of 2 *per cent* was proposed to be treated as service charges and passed on to SIL, after the remittance of loans in full by SIL. The agreement with SIL was modified accordingly (October 2003).

The Company disbursed loans amounting to Rs. 125.77 crore (Rs. 55.90 crore during October 2001-October 2003 and Rs. 69.87 crore during November 2003- April 2006). SIL received a commission of Rs. 2.34 crore during November 2003-April 2006 and also collected security deposit as per agreement terms amounting to Rs. 5.59 crore (October 2001-October 2003).

Audit noticed that despite deciding to stop the collection of 20 *per cent* of the loan amount as security deposit from borrowers and limit the service charges to 2 *per cent* only (with effect from November 2003) by increasing the rate of interest and collecting the same in instalments from borrowers, the Company failed to ensure that, SIL was not collecting security deposit from borrowers because of lack of monitoring of loan agreements with ultimate borrowers. Further, SIL changed the moratorium period from 60 days to 30 days without the knowledge and approval of the Company. The agreements entered between the Company and the loanees were also not made available to Audit. Two cases where complaints were registered with the Company only were susceptible to verification in audit, as the Company had given full freedom to SIL for dealing with the loanees. The Company also had issued (April 2005) a power of attorney relaxing the provisions of original agreement condition allowing SIL to seize the vehicles of borrowers, collection of instalments and issue of receipts etc., on behalf of the Company. The tie-up with SIL was, however, discontinued in April 2006 and the reasons for the same were not available on record.

Thus, decision to permit SIL, to directly enter into agreements with loanees and deficient monitoring resulted in non-transparent deals and undue benefit of Rs. 2.21 crore to SIL for the entire loan period of 60 months in respect of 1,458 loanees for new vehicles sanctioned during 2001-2006. Potential interest income unauthorisedly received by SIL at the minimum interest rate of 7.5 *per cent* charged by the Company during the period for 60 months amounted to Rs. 0.83 crore in addition to Rs. 5.59 crore collected as security deposit during October 2001-April 2006. Audit observes that appointment of a private canvassing agency in a Government financing institution for promoting SRTO loan scheme was unjustified as it led to lack of transparency in dealings.

The Company had registered (December 2008) a complaint with the State police stating that as reported by the loanees, SIL, assumed themselves to be lenders of money and charged high rates of finance charges and are suspected to have changed the EMI amounts and requested to register a case against them.

Audit suggests that in future, when the Company embarks upon direct lending schemes to beneficiaries through marketing/ canvassing agents, it should be ensured that the provisions of the agreement with the agencies are strictly enforced so that, the agency should not profit out of the scheme due to the lack of proper monitoring by the Company.

The matter was reported to Government/ Management in June 2009; their reply was awaited (September 2009).

4.9 Wasteful expenditure on commission to Marketing Agents

Decision to appoint two unqualified and inexperienced marketing/ verification agents for promoting the loan schemes, resulted in wasteful expenditure on commission and verification charges amounting to Rs. 40.96 lakh.

The Company was formed with the main object of financing Kerala State Road Transport Corporation for purchase of vehicles and to assist other transport undertakings. Grant of personal housing finance and personal loan schemes are the sub-objectives of the Company. The Company launched (February 2005) a new housing scheme viz., AISWARYA Griha Housing Finance Scheme and decided (March 2005) to appoint Direct Marketing Agents (DMA) for promotion and canvassing genuine and needy customers for the housing scheme, in places where the Company was not having branches. Based on applications invited (March 2005), through advertisements, the Company short listed two firms viz. H- Worknet and Powerlink Services (P) Ltd., (Powerlink).

Both the firms, although did not possess the minimum desired experience of five years in marketing housing loans of Nationalised and other Commercial banks, were issued appointment letters (September 2005) which were prima facie managed by same persons and closely related to each other. As per the agreement entered (October, November 2005) with the DMAs for a period of three years, commission was payable at specified rates (half *per cent* to one *per cent*) on the loan canvassed in different slabs (Rs. 10 lakh to Rs. 50 lakh and above).

The Board of the Company authorised (August 2005) the Managing Director (MD) only to appoint the two firms as DMAs, for housing loan schemes, but the MD appointed (February 2006) the two firms as canvassing and verification agents of housing and other loans as well, with a commission of Rs. 500 per file for housing, vehicle and consumer durable loans etc., and Rs. 300 per file for personal loans exceeding the delegated authority/ powers. The DMAs were paid Rs. 40.96 lakh, as commission (Rs. 37.26 lakh) and as verification charges (Rs. 3.70 lakh) during the four years 2005-08 (up to November 2008).

Audit noticed (January 2009) that the Company had not fixed any monthly or region-wise target for DMAs and continued paying commission and verification charges without assessing the usefulness of their services. The Company should have been aware that using the DMAs for verification of loan applications would create conflict of interest as the verification process was the integral function of the Company. Thus, the Officers of the Company had failed in protecting the financial interest of the Company. Out of Rs. 75.32 crore loan disbursed (2005-09), Rs. 55.97 crore (74 *per cent*) in 45 cases was DMAs' share and out of this, 37 cases involving Rs. 49.56 crore were in Thiruvananthapuram district only, where, the head office of the Company was situated. The business generated by the two DMAs in other eleven districts of the State was only Rs. 6.41 lakh (11.45 *per cent*) defeating the very objective of appointing the DMAs, viz., expanding the customer base to districts where Company was not having branches.

It was also noticed that the directors of both the firms had availed (2006-07) housing loan of Rs. 90.39 lakh. In addition to the above, Powerlink Builders, with the same address of Powerlink Services also was granted (2007-08) housing loan of Rs. 2 crore. Aggregate amount of commission paid to the two DMAs on these three loans (Rs. 2.90 crore) amounted to Rs. 2.90 lakh.

Audit observes that the decision to appoint a marketing agency for canvassing loans by a Government Company by appointing two firms was not a transparent step. The DMAs selected were unqualified and inexperienced firms having partners/ directors closely related to each other. Permitting, these DMAs to canvass and verify the documents of borrowers, to do business at places where Company, itself had its head office, without any strong business objective resulted in conflict of interest as well as wasteful expenditure of Rs. 40.96 lakh by way of commission and verification charges. On being pointed out by Audit (January 2009) the Government issued directions (February 2009), to stop payment of commission to DMAs in places where the Company had branches, and the direction was implemented with immediate effect.

The Government stated (July 2009) that the appointment of marketing and verification agents was as per Board resolution and there was no default in repayment of loan given to directors of DMA firms though the directors/ partners of two firms appointed as marketing/ verification agents are related persons. The reply of the Government is not convincing as the final Board decision on 23 March 2005 was to appoint the two firms as Direct Marketing Agents alone and the audit contention of appointment of one and the same firm as marketing agent as well as verification agent was against the financial interest of the Company has not been contested. Thus the Officers of the Company failed to protect the financial interest of the Company and major share of business canvassed by the two firms was from the place where the head office of the Company is situated giving them undue advantage by abdicating their own responsibility.

Audit suggests that the Management / Government should take immediate steps to fix the responsibility for this act and direct to recover the undue benefits passed on to the DMAs and should appoint DMA firms after due diligence.

4.10 Undue benefit

Decision to refund rent for the period of 18 months during which Reliance Retail Limited occupied the premises, resulted in undue benefit of Rs. 15.92 lakh.

The Company decided (October 2005) to allot shops and office space on lease and invited tenders (July 2006). Reliance Retail Limited (RRL) which submitted their bid (August 2006) for an area of 4411.60 square feet for a lease rent of Rs. 1.11 lakh per month, was allotted (August 2006) the space for 3 years from 7 December 2006 to 6 December 2009. RRL also remitted the security deposit of Rs. 1.11 crore.

Government of Kerala, meanwhile, directed (December 2007) the Company to revoke the agreement with RRL and it consequently terminated the agreement (June 2008). However, RRL requested (January 2008) the Company either to allow them to operate with the approval of Government of Kerala or to refund the entire security deposit along with entire rent paid. The Company returned the security deposit of Rs. 1.11 crore along with rent of Rs. 15.92 lakh (net amount after adjusting TDS deducted by RRL) for the period from January 2007 to June 2008 while neither the directives of State Government nor the lease agreement contained provision for refund of rent collected for the period of occupation in case of premature termination of the agreement by the lessor.

This decision of the Company to refund the rent for the period of 18 months during which RRL occupied the premises did not follow the principle of *quid pro quo* and caused it a loss of Rs. 15.92 lakh.

Management stated (June 2009) that the agreement had not envisaged anything in such a peculiar condition. This showed that the agreement was not properly drafted by envisaging all the possibilities.

The matter was reported to Government in April 2009; their reply was awaited (September 2009).

Kerala Forest Development Corporation Limited

4.11 Wasteful expenditure on wattle plantations

Decision of the Company to raise wattle plantation without conducting suitability study resulted in wasteful expenditure of Rs. 1.14 crore.

The Company engaged in raising of all species of forest plantations for the development of timber based industries in the State, wrote off (2007-08) the entire expenditure incurred on wattle plantations amounting to Rs. 1.14 crore. The wattle plants were raised (1994-98) in 312.60 hectares at Silent Valley in Munnar, which were expected to give an yield of 3150 MT after eight years (2002-07) fetching expected revenue of Rs. 42.51 lakh.

The felling of wattle did not take place due to non-availability of grown-up plants in the area. As per the report (October 2007) of the Manager, Silent Valley Sub-unit, the survival rate of the plants ranged from a meager 4 *per cent* to 50 *per cent.* The reported height of the plants was only 2 to 3 metres and Girth at Breast Height (GBH) 10 to 19 centimeters and hence they could not be commercially exploited. The growth of the plants was retarded since high altitude place was not suitable for the growth of the plant.

Audit noticed that the Eucalyptus plantation raised in 1978 in same plots of land had failed and as a substitute of Eucalyptus, the Company identified wattle as an ideal species for planting in high elevated areas with the favourable planting experience of other departments/States. The Company without proper studies regarding the suitability of the land for raising wattle plantations went for mass planting of wattle from 1994 to 1998; which eventually failed. Even the meager anticipated revenue of Rs. 42.51 lakh could not be realised due to total failure of the plantations.

Thus, the decision (1994-98) of the Company to raise wattle plantation without conducting any suitability study was a case of defective planning which resulted in wasteful expenditure of Rs. 1.14 crore.

The Management/ Government stated (June, July 2009) that such a massive under-performance of the species and resultant failure in terms of expected yields was never anticipated. The fact remained that deficient planning and failure to conduct suitability study by the Management prior to plantation resulted in wasteful expenditure to the Company.

Audit recommends that the Company should undertake proper feasibility study and cost benefit analysis before undertaking such activities.

Travancore Titanium Products Limited

4.12 Avoidable payment of demurrage charges

Delay in initiating action to obtain EPCG licence resulted in payment of avoidable demurrage charges amounting to Rs. 37.62 lakh.

The Company is engaged in the manufacture and sale (both domestic and export) of Anatase grade[♦] titanium dioxide pigment. Government of Kerala accorded (May 2005) sanction for the Company's project to implement pollution control measures in two phases along with Company's expansion and modernisation plans. The project cost of Phase I[≈] was pegged at Rs. 225.80 crore and MECON (a GoI Company) was engaged as the project management consultant.

Chematur Ecoplanning Oy, Finland and their associates, AVI Europe Limited, UK (AVI) were contracted (February 2006) for the supply of technical know-how and import of proprietary equipments for Phase I of the project. As per the Export Promotion Capital Goods (EPCG) scheme envisaged in the Foreign Trade Policy 2004-09, Company was eligible for concessional import duty rate of 5 *per cent* on these imported items as against the normal import duty of 34.47 *per cent*. To avail this concessional rate of duty, an application in self declaration form had to be submitted to the Regional Licensing Authority (RLA) along with specified documents and the RLA shall issue the licence within 3 days.

AVI despatched (2 April 2007) first consignment of the order which reached Cochin Port on 13 May 2007. The Company, however, did not take delivery of the equipments within the free delivery period i.e., by 23 May 2007 since it had applied (1 June 2007) for EPCG licence only after arrival of goods. The consignment was finally cleared (2 July 2007) after obtaining (27 June 2007) EPCG licence. Owing to delay in clearing the consignment, the Company had to pay (July 2007) demurrage charges of Rs. 37.62 lakh imposed by the Cochin Port Trust.

Audit observed that the Company had initiated (June 2007) action for obtaining EPCG licence only after the receipt of equipments at Cochin Port (13 May 2007) even though AVI had notified the despatch of equipments in April 2007 itself.

[♦] It is a mineral form of Titanium dioxide which has low density and is used in the manufacture of paper, plastic, interior paint, etc., as pigment.

[≈] Involving construction of Acid Recovery Plant, Copperas Recovery Plant and Neutralisation Plant with water recovery module.

Thus, defective planning and monitoring and delay in initiating action to obtain EPCG licence resulted in payment of avoidable demurrage charges of Rs. 37.62 lakh.

Management reply (July 2009) as endorsed by Government stated that at the time of import the Company was in deep financial trouble because of the rise in cost of titanium dioxide due to increase in price of major inputs, sulphur and fuel. By 2007 export price was matching with the domestic price and availing EPCG Scheme was beneficial to the Company. But the fact remained that the Management was well aware of the difficult financial position of the Company and action was not taken in time to obtain the EPCG licence, so that demurrage charges could have been avoided.

Malabar Cements Limited

4.13 Avoidable expenditure due to lack of transparency

Changes made in contract conditions after the opening of tender/quotation resulted in lack of transparency in conditions advertised and avoidable extra expenditure of Rs. 16.97 lakh.

In response to tenders invited (June 2007) for supply of limestone with moisture content of three to eight *per cent* with pro-rata reduction in quantity for excessive moisture content, Venkateswara Cements Limited (VC) quoted (August 2007), the lowest rate of Rs. 580.25 per MT, which was reduced (September 2007) to Rs. 570 per MT (including transportation charges-Rs. 389 per MT and loading charges-Rs. 20 per MT). Based on the request of VC at the time of negotiation (September 2007), prior to the issue of order (September 2007), the contract was split up (September 2007) into two viz., one for supply of limestone by VC and another for loading and transportation by Raja Transport (RT) and the accepted maximum level of moisture content was increased from three *per cent* to six *per cent*. This resulted in changes in tender conditions after the opening of tender and lack of transparency as all the tenderers did not get equal opportunity to quote their lowest rates as it was a composite contract for supply of limestone at Company's factory at Walayar.

The contract was for supply of 3,60,000 MT of limestone for two years (September 2007 to September 2009) at 15,000 MT per month. The Company amended (November 2007) the stipulation for the level of moisture content in limestone from six *per cent* to three *per cent* in the order and if the moisture content exceeded this level, pro-rata reduction in the basic value of material and loading charges only (excluding transportation charges) was to be made. The amendment, however, was not extended to transportation cost, even though, that was a major component (68 *per cent*) of the composite rate of Rs. 570 per MT quoted / agreed upon.

VC supplied (November 2007 to October 2008) 61,262 MT of limestone through RT with moisture content varying between 8.27 to 12.29 *per cent*. While proportionate reduction was made from payment for basic material cost as per amended conditions, no recovery / reduction could be effected from transportation cost in the absence of stipulation / enabling provision in the contract, even though transportation cost accounted for 68 *per cent* of total cost.

The Government in reply stated (July 2009) that tenders were framed with a general understanding of the situation. However, based on offers and situation, suitable changes need to be made in order to ensure continuous supply of essential raw materials. The reply is not acceptable since tender conditions were modified after opening of tender resulting in lack of transparency in tender conditions published in news papers i.e., other tenderers were not given equal opportunity to quote fresh rates.

Thus, the changes made in the conditions of the contract after opening of tender exhibited lack of transparency in working of the Company and the Company bore the avoidable extra expenditure of Rs. 16.97 lakh due to transportation of excess moisture laden limestone.

Statutory Corporations

Kerala State Electricity Board

4.14 Avoidable committed liability

Failure to maintain security deposit account of individual consumers resulted in non-payment of interest on security deposit and consequent committed additional liability of Rs. 38.19 crore.

The Board by virtue of the provisions of Electricity Act, 2003 and Kerala Electricity Supply Code 2005, was empowered to collect security deposit equivalent to two/ three months electricity bill from consumers having monthly/ bimonthly billing cycle during the period of agreement in force. At the same time, the Board had to pay interest on these security deposits at bank rates prevailing as on 1 April of the financial year commencing from April 2005, by way of deduction from consumer's electricity bills commencing from first quarter of financial year 2005-06, every year. In case of default / delay in payment of interest, the interest payable was to be at double the normal rate. The Board fixed (November 2005) the rate of interest as 6 *per cent* for the period 2005-2008.

The security deposits eligible for interest held by the Board at the beginning of April 2005, April 2006 and April 2007 were Rs. 478.44 crore, Rs. 545.46 crore and Rs. 624.08 crore respectively on which the aggregate interest payable at six *per cent* amounted to Rs. 98.87 crore had they been credited on due dates. The Board however, gave a credit of Rs. 60.68 crore only to consumers during the three years (2005-2008) resulting in short payment of interest of Rs. 38.19 crore.

Since the non-payment of interest on security deposit attracted interest at double the normal rate (12 *per cent*), the Board had to pay Rs. 76.38 crore as against Rs. 38.19 crore payable as per the requirements of Kerala State Electricity Supply Code 2005. Audit observed that, non-payment of interest on security deposit to all consumers in time, as per Statutory requirements was due to incomplete maintenance of security deposit accounts of individual consumers during the period prior to 1 April 2005. The Board has treated the opening balance of security deposit of those consumers whose accounts are not maintained as Re.1 on which interest was not paid.

This failure to maintain security deposit accounts of individual consumers and consequent delay in credit of interest on security deposit resulted in avoidable liability of Rs. 38.19 crore for the Board.

Audit suggests that the Board should undertake vigorous time bound exercise to streamline its financial and consumer records so that these types of unwarranted liabilities can be avoided as this deficiency is going to lead to further future liabilities on this account.

The matter was reported to Government/ Management in June 2009; their reply was awaited (September 2009).

4.15 Undue benefit to the contractor

Failure to negotiate with the contractor to reduce the rates for galvanization of line materials, while extending the delivery period for the convenience of the contractor, resulted in extra expenditure and undue benefit to the contractor amounting to Rs. 95.53 lakh.

The Board invited (December 2007) tenders for galvanizing 4165 MT of line materials (V Cross Arms-3575 MT and Stay rods-590 MT) with a probable amount of contract of Rs. 6.31 crore. Out of two offers received (December 2007), the offer of The Metal Industries Limited, Shoranur (a State PSU) was rejected for lack of experience while the other offer of Alsteel Industrials, Kollam, which had quoted a price of Rs. 18.18 per kg (excluding transportation) was selected and the pre-qualification committee recommended (April 2008), the offer for sanction by the Board, subject to ensuring the reasonableness of the rates with reference to IEEMA[1] circulars.

[1] Indian Electrical & Electronics Manufacturers' Association.

The Board further negotiated the price to Rs. 18 per kg (excluding transportation) and a work order for galvanizing 4165 MT of line materials (Cross Arms-2707 MT and Stay rods-1458 MT) was issued (May 2008) and an agreement concluded (June 2008). As per agreement entire quantity was to be supplied by December 2008. The contractor delayed supply and requested (February 2009) extension of time up to March 2009, which was duly approved by the Board, without any financial commitment on both the sides. The contractor completed the supply of 4,158.576 MT of galvanized material during December 2008 - April 2009.

Audit noticed that at the time of inviting (December 2007) tenders, the price of zinc was reckoned as Rs. 1.74 lakh per MT and was witnessing a declining trend since January 2008. The price of zinc was Rs. 1.18 lakh/MT at the time of negotiation (March 2008) and Rs. 0.69 lakh/MT (November 2008) when first lot was supplied (December 2008) by the contractor. The contractor did not complete supply of galvanized material as per schedule (December 2008) and extension was granted (March 2009) to the contractor, the price of zinc had further declined to Rs. 0.68 lakh per MT. Out of the total cost of galvanization, the cost of zinc was 42 *per cent*. Despite decline in zinc prices by 32 *per cent* to 60 *per cent* during December 2007 to November 2008, no attempt was made to re-negotiate the price by the Board even when there was an opportunity while extending the delivery period to the convenience of contractor.

Thus, failure of the Board to negotiate the rates for galvanization of line material while extending the delivery period for the convenience of the contractor was an opportunity foregone which resulted in an extra expenditure and undue benefit to the contractor amounting to Rs. 95.53 lakh.

Audit suggests that the delivery time extension should be made by competent authority in the same way as a new purchase decision is dealt with to protect the financial interest of the Board.

The matter was reported to Government / Management in June 2009; their reply was awaited (September 2009).

4.16 Opportunity to recover money ignored

Kerala State Electricity Board, a PSU did not either seize the opportunity to recover its money or pursue the matters to their logical end, as a result, recovery of money amounting to Rs. 7.63 crore remains doubtful.

A review of unsettled paras from Inspection Reports (IRs) pertaining to period up to 2003-04 showed that there were 42 paras in respect of Kerala State Electricity Board (Board) involving a recovery of Rs. 7.63 crore. As per the extant instructions contained in Article 63 of Kerala Financial Code Vol: I, Board was required to take remedial action within one month after receipt of Inspection Reports from Audit. However, no effective action had been taken to take the matters to their logical end, i.e., to recover money from the concerned parties. As a result, the Board has so far lost the opportunity to recover its money which could have augmented the finances.

The paras mainly pertain to recovery on account of short assessment of current charges, penal charges and non-recovery of consumers' contribution amounts etc.

Above cases, point out the failure of the Board to safeguard its financial interests. Audit observations and their repeated follow up by Audit, including bringing the pendency to the notice of the Power Department and Board management periodically; have not yielded the desired results in these cases.

The Board should initiate immediate steps to recover the money and complete the exercise in a time bound manner.

The matter was reported to Government / Management in June 2009; their reply was awaited (September 2009).

4.17 Lack of remedial action on audit observation

Kerala State Electricity Board, a PSU did not either take remedial action or pursue the matters to their logical end in respect of 48 IR paras, resulting in foregoing the opportunity to improve their functioning.

A review of unsettled paras from Inspection Reports pertaining to period up to 2003-04 showed that there were 48 paras in respect of Kerala State Electricity Board (Board) which pointed out deficiencies in the functioning of this PSU. As per the extant instructions contained in Article 63 of Kerala Financial Code Vol: I, Board was required to take remedial action within one month after receipt of Inspection Reports from Audit. However, no effective action had been taken to take the matters to their logical end, i.e., to take remedial action to address these deficiencies. As a result, the Board has so far lost the opportunity to improve its functioning in this regard.

The paras mainly pertain to delay in execution of major works and resultant excess expenditure, idling of equipments, short realisation of electrical connection charges, non-reconciliation of bank accounts, non-identification of defaulters, cost overrun and transmission and distribution loss etc.

Above cases point out the failure of the Board to address the specific deficiencies and ensure accountability of its staff. Audit observations and their repeated follow up by Audit, including bringing the pendency to the notice of their Administrative Department and Board management periodically, have not yielded the desired results in these cases.

The Board should initiate immediate steps to take remedial action on these paras and complete the exercise in a time bound manner.

The matter was reported to Government/ Management in June 2009; their reply was awaited (September 2009).

4.18 Undue benefit to a distribution licensee

Relaxation of existing rules / procedures and stipulation of Kerala State Electricity Regulatory Commission on giving two service connections at different voltage, resulted in revenue loss and undue benefit to Thrissur Municipal Corporation amounting to Rs. 75.05 lakh.

Thrissur Municipal Corporation (TMC) is a deemed distribution licensee under section 14 of Electricity Act, 2003, even though no agreement evidencing distribution licence existed between the TMC and the Kerala State Electricity Board. The licensee had (March 2007) a connected load of 20 MVA (2 x 10 MVA) in excess of the contracted demand of 8 MVA at 66 KV which was irregular as per stipulation of Kerala State Electricity Regulatory Commission (KSERC) in Supply Code 2005. Pending construction of own 110 KV Substation, to tide over the difficulty, TMC requested (March 2007) for an additional 11 KV supply from KSEB's 110 KV substation at Ollur.

The Board sanctioned (April 2007) a temporary connection of 11 MVA in HT IV tariff, which was higher than 66 KV grid tariff, from Board's own infrastructure as a special case. According to standing orders (1987), of the Board which provide that no additional load/ power allocation should be given to a defaulting consumer and concurrence of the KSERC is essential for giving supply to a consumer at two points at different voltage levels, TMC did not satisfy both the requirements when additional load was sanctioned (April 2007).

Audit noticed that TMC owed Rs. 3.55 crore (April 2007) to the Board towards electricity tariff pertaining to the period January 1986-November 2002, including interest at concessional rate of three *per cent* per annum and also delayed the execution of HT agreement upto September 2007, resulting in delay of regular billing by five months (April-August 2007) and loss of interest to the Board amounting to Rs. 2.30 lakh. The additional load was shifted to TMC's substation in April 2008 and an amount of Rs. 2.88 crore was overdue from TMC towards defaulted payments as of January 2009.

The Board, however, based on the request (May 2007) from TMC, immediately, after giving (April 2007) connection, accorded (June 2007) sanction, for converting the tariff from 11 KV HT IV to 11 KV Grid 1 tariff, with a lesser rate. The revenue, thus, foregone by the Board by converting the connection to Grid 1 tariff (11 KV) for the period (April 2007–March 2008) amounted to Rs. 75.05 lakh.

Audit observed that by granting relaxation in existing rules, procedures and stipulation of KSERC, on giving two different service connections to TMC at different voltage, Board incurred loss of revenue and extended undue benefit to TMC amounting to Rs. 75.05 lakh during April 2007 to March 2008.

The matter was reported to Government / Management in June 2009; their reply was awaited (September 2009).

4.19 Avoidable extra expenditure

Avoidable extra expenditure of Rs. 1.07 crore due to purchase of Mild Steel Flats under single tender system.

The delegation of powers of Deputy Chief Engineer (Dy.CE), Civil Circle, Pallom of Kerala State Electricity Board (Board) for purchase of steel items from Government Companies, Steel Authority of India Limited (SAIL) and Visakhapatnam Steel Plant (VSP) was raised (December 2006 & May 2007) from Rs. 12 lakh to Rs. 50 lakh at a time, in order to meet urgent requirements to achieve targeted production of fabricated parts during May 2005-March 2008, with an overall ceiling of Rs. 2.50 crore. Later, based on the request of the Dy.CE sanction was given (May 2008) to purchase items not available with SAIL / VSP upto value of Rs. 50 lakh at a time with an overall limit of Rs. 5 crore from other suppliers during the years 2006-08 on condition that non-availability of items from SAIL and VSP must be ensured before purchase through open tenders.

The Dy.CE invited tenders for purchase of Mild Steel (MS) Flats (1091 MT) during 2005-2007 of different specifications by placing advertisements in local dailies having limited circulation in and around Kottayam district only contrary to the provisions of Kerala Government Stores Purchase Manual and Tender Regulations. The Board received offers for supply from only two firms viz., Binu and Company (BC) and Alsteel Industrials from the nearby district of Kollam, except in one case where one dealer (Pipe Distributors) from Kochi had responded.

Audit observed, as evidenced from records that the proprietor of BC was also the authorised signatory of Alsteel Industrials and as such there was only one offer / tender in all the cases. The Board while evaluating the offers ignored the market trend and did not verify availability and prevailing prices of other reliable sources such as SAIL / VSP. The offers of BC were invariably accepted in all cases.

The Board purchased 960.215 MT of MS flats of different specifications in 14 purchase orders, at rates ranging from Rs. 32,150 to Rs. 39,970 per MT from BC during the two years 2005-07 involving an expenditure of Rs. 3.82 crore. Audit compared these rates to the rates at which MS flats were purchased at prevailing market price by Kerala Small Industries Development Corporation Limited (SIDCO), a Government Company, acting as agency for procurement and supply of steel items to small entrepreneurs and found that the difference ranged between Rs. 2,150 per MT to Rs. 13,942 per MT in four types of MS flats during the same period.

The delegation of powers given to the Dy.CE by the Board for purchase of steel items were thus grossly misused by resorting to purchase of MS flats from a single private party without adhering to normal tender procedures for publicity and comparison of prevailing market price as per Kerala Government Stores Purchase Manual resulting in avoidable extra expenditure of Rs. 1.07 crore during the two years 2005-2007.

It is suggested that the delegation of financial powers given to different circles be reviewed and internal control procedure strengthened. The Board should also follow its tendering procedures scrupulously.

The matter was reported to Government/ Management in April 2009; their reply was awaited (September 2009).

4.20 Avoidable loss of revenue

Failure of KSEB to convert HT connection into more beneficial LT connection has resulted in avoidable revenue loss of Rs. 43.18 lakh.

The Board had in Kerala Financial Corporation (KFC) a High Tension (HT) power consumer with a maximum contracted demand of 150 KVA for Ernakulam Branch Office. Due to restructuring (March 2006) of KFC's space requirement it retained part of the building and leased out balance to four institutions[Ψ]. KFC submitted (December 2006) an application to KSEB for conversion of the single HT connection into separate Low Tension (LT) connection for each floor of the building after the scheme for conversion into LT was approved (April 2006) by the Electrical Inspectorate. KSEB received separate application for each floor with processing fee submitted by KFC in December 2006 and the contract demand as per the conversion schedule was

[Ψ] South Indian Bank on ground floor; Small Industries Development Bank of India on the second; Bajaj Allianz on the third and Geojit Financial Services Limited on the fourth, fifth and sixth floors.

fixed at 334 KW. Conversion into LT is, however, yet to take place (September 2009).

Audit observed that the energy charge applicable under LT VI C and VII A category was Rs. 8.40 and Rs. 8.05 per unit respectively, whereas energy charge under HT category was Rs. 6.66 per unit, yet KSEB did not take any steps for conversion of the HT connection into LT connection even after two years of application. As a result, the Board could not bill 1.90 million units of power consumed by KFC during April 2007 to June 2009 at the more beneficial LT tariff resulting in revenue loss of Rs. 43.18 lakh.

This failure of KSEB to convert HT connection into more beneficial LT connection due to inadequate and deficient monitoring of applications from electricity consumers led to non-safeguarding of financial interests of the organisation and resulted in avoidable revenue loss of Rs. 43.18 lakh to the Board.

Government replied (July 2009) that the delay in conversion to LT connection was due to delay in submission of necessary documents by KFC. The reply is not acceptable as KFC had submitted the application and processing fee as early as in December 2006 and any additional documents / information could have been called for by the Board.

It is suggested that the Board should strengthen its internal control mechanism to monitor consumer application / requests and make the response a time bound exercise.

4.21 Avoidable extra expenditure

Failure of the KSEB in analysing the extra cost involved in invoices of fuel resulted in extra expenditure of Rs. 27.88 lakh.

The Board entered into (January 1999) an agreement with Bharat Petroleum Corporation Limited (BPCL) for purchase of fuel[π] for its Kozhikode Diesel Power Project (KDPP), Nallalam, valid for a period of 15 years (up to 2013), at the rate applicable on the date of drawal. According to the agreement, the total operation facilities including receipt of the product at Nallalam, storage and transferring of the product from Nallalam tanks to buyer's service tanks was also the responsibility of the seller.

In order to avail the excise duty concession on fuel consumed for power generation, the storage facilities at Nallalam were declared (March 2000) as a bonded warehouse of BPCL. Consequent to withdrawal (September 2004) of

[π] Low Sulphur Heavy Stock (LSHS)/ High Speed Diesel (HSD)/ Low Sulphur Furnace Oil (LSFO) / Low Sulphur Waxy Residue (LSWR) exemption by Government of India for products drawn from bonded ware houses, KDPP resorted (December 2004) to sourcing the fuel directly from Kochi Refineries Limited (KRL) of BPCL at Kochi to avail the excise duty exemption.

The Government of India withdrew (July 2005) the excise duty exemption for fuel used for power generation but KDPP switched over in October 2008 to sourcing of fuel from storage tanks at Nallalam. At the same time KRL continued invoicing fuel supplies as if withdrawals were from KRL, Kochi.

Audit noticed that depot prices included basic price at Kochi including transportation cost to Nallalam, in which excise duty, education cess, sales tax (KVAT) and cess thereon amounting to Rs. 109.03 per MT had been included. The extra expenditure, thus, incurred on 25,571.903 MT fuel during the period from November 2008 to February 2009 amounted to Rs. 27.88 lakh.

This failure of the Board in analysing the extra cost involved in invoicing the fuel drawn from storage tanks at Nallalam at depot prices at Kochi which included transportation cost from Kochi to Nallalam and duties thereon and other levies etc., resulted in avoidable extra expenditure of Rs. 27.88 lakh (November 2008-February 2009).

Government stated (June 2009) that the present practice followed was as per the agreement. Considering the interest on advance payment on bulk stock stored in the tank, purchasing fuel at depot price at Kochi was beneficial to the Board. The reply will not hold good as the agreement required payment only on withdrawal basis and Management failed to opt for invoicing on withdrawal basis at Nallam, as was done prior to September 2004.

Audit recommends that this deficient purchase procedure be amended so as to avoid further loss to the Board.

Kerala State Warehousing Corporation

4.22 Avoidable cash loss on procurement of urea

Injudicious decision to procure 1,850 MT urea without approval of Government and its subsequent sale at a cash loss of Rs. 20.72 lakh.

The State Government entrusted (November 2003-October 2004) to the Corporation the implementation of the Centrally Sponsored Scheme with twin objective for spraying of bio-pesticides on coconut trees against tree disease causing mite and supply of fertilizer kits to farmers containing Urea, Super Phosphate, Magnesium Sulphate etc., in nine districts of the State and sanctioned and released Rs. 9.40 crore for the purpose of spraying bio-pesticides alone.

The Corporation sprayed (November 2004-March 2006) bio-pesticides on 74.5 lakh coconut trees in nine districts, spending Rs. 8.48 crore and also purchased (February 2005) 1,850 MT of urea adequate for use on 25 lakh coconut trees by spending Rs. 91.75 lakh utilising funds received for spraying bio-pesticides. The utilisation certificates submitted (May 2006) by the Corporation for Rs. 9.40 crore were not accepted (August 2006) by the Agriculture Department for want of certificate accepting purchase of urea from subordinate offices as it was without the specific approval of the Government. The Corporation abandoned (November 2006) the fertilizer application scheme for want of further funds from the Government.

Despite knowing the fact that urea was purchased out of funds intended for spraying bio-pesticides, the Corporation did not seek prior specific approval of Government for deviation from the directions. The whole of urea purchased (February 2005) remained in the warehouses of the Corporation without issue to the farmers for twelve months (February 2005- January 2006), resulting in loss of weight and nutrient value. The Corporation's request (February 2006) for the disposal of urea was ultimately approved (November 2006) with a severe criticism by the Government. The available 1,790 MT of urea was sold (April 2007) at a reduced price of Rs. 71.03 lakh, resulting in a cash loss of Rs. 20.72 lakh.

Thus, the injudicious decision to purchase 1,850 MT urea by utilising funds received for spraying bio-pesticides for coconut trees, without specific approval of the Government and its subsequent sale at reduced prices resulted in a cash loss of Rs. 20.72 lakh.

The Management reply as endorsed by the Government stated (May 2009) that the Corporation decided to purchase 1,850 MT urea from advance given for spraying operations, without sanction either from the Government or Director of Agriculture. Even though, the Corporation was directed to remit back the cost of urea, the amount was yet (September 2009) to be refunded.

Kerala Financial Corporation

4.23 Avoidable payment of interest

Failure of the Corporation in remitting the prescribed amount of advance income tax despite having sufficient cash surplus resulted in avoidable payment of interest of Rs. 26.97 lakh.

As per Section 234 B and C of the Income Tax (IT) Act, 1961, a Corporate assessee has to pay 90 *per cent* of the tax in advance when the amount of tax payable exceeds five thousand rupees per annum. The advance tax is payable in four quarterly instalments between June and March months of the corresponding financial year. Failure to pay at least *90 per cent* of the tax in advance by March attracts interest at the rate of 12 *per cent* per annum (section 234 B ibid). Similarly for failure to pay instalments of advance tax by specified dates, interest is chargeable at the rate of one *per cent* per month (Section 234 C ibid).

Kerala Financial Corporation (KFC), a Statutory Corporation established under the State Financial Corporation Act, 1951 was liable to pay advance tax on its assessed income under the provisions (Section 8) of the Act ibid. KFC had an assessed income of Rs. 6.97 crore and Rs. 8.08 crore respectively during the financial years 2005-06 and 2006-07. Advance tax payable on the assessed income was Rs. 2.11 crore and Rs. 2.45 crore respectively against which the advance tax actually paid (March 2006 / December 2006/March 2007) by the Corporation was only Rs. 1.57 crore (2005-06) and Rs. 0.59 crore (2006-07). The Corporation had also defaulted in payment of quarterly instalments. As a result of short payment of advance tax and failure to pay instalments of advance tax, the IT Authorities imposed penal interest of Rs. 39.97 lakh (Rs. 14.42 lakh for 2005-06 and Rs. 25.55 lakh for 2006-07) on the Corporation and the penal interest was paid in October 2007 / 2008.

Audit noticed that the Corporation had failed in remitting advance tax after correct assessment of the taxable income despite notices by the IT Department. The Corporation in this period also had sufficient cash balance to defray the advance income tax.

The failure of the Corporation in remitting the prescribed amount of advance income tax despite having sufficient cash surplus resulted in avoidable payment of interest of Rs. 26.97 lakh[♠] besides non-compliance with tax laws.

It is recommended that the Management should ensure payment of the advance tax on due dates as well as filing of the Income Tax Return in time to avoid unintended liabilities.

The matter was reported to Government / Management in May 2009; their reply was awaited (September 2009).

General

4.24 Follow-up action on Audit Reports

Explanatory notes[♣] outstanding

4.24.1 The Audit Reports of the CAG represent the culmination of the process of scrutiny starting with initial inspection of accounts and records maintained in the various Government Companies and Statutory Corporations. It is,

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♠ Rs. 39.97 lakh as reduced by interest of Rs. 13.00 lakh (at the rate of 6 *per cent* per annum for 7 months) applicable to advance income tax (from April to October).

♣ Explanatory notes refer to the explanations furnished by Administrative Departments to the Legislature Secretariat, on reviews / paragraphs contained in Audit Reports placed before the Legislature.

therefore, necessary that they elicit appropriate and timely response from the executive**.** Finance Department, Government of Kerala issued (April 2005) instructions to all Administrative Departments to submit explanatory notes indicating a corrective / remedial action taken or proposed to be taken on paragraphs and reviews included in the Audit Reports within two months of their presentation to the Legislature, without waiting for any notice or call from the Committee on Public Undertakings (COPU).

The Audit Reports for the years up to 2007-08 have been presented to the State Legislature but ten departments did not furnish explanatory notes on 61 out of 94 paragraphs / reviews relating to the Audit Reports for the year 2004-05 to 2007-08 as of September 2009.

Compliance to Reports of Committee on Public Undertakings (COPU) outstanding.

4.24.2 As per the Handbook of Instructions for Speedy Settlement of Audit Objections issued by the State Government the replies to paragraphs are required to be furnished within two months from the presentation of the Reports by COPU to the State Legislature. Action Taken Notes (ATNs) to 398 paragraphs pertaining to 91 Reports of the COPU presented to the State Legislature between July 2000 and July 2009 had not been received as of September 2009 as shown below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where ATNs not received
1998-2000	2	13
2001	2	6
2001-2004	12	55
2004-2006	26	93
2006-2008	31	155
2008-2011	18	76
Total	**91**	**398**

Response to inspection reports, draft paragraphs and reviews

4.24.3 Audit observations made during audit and not settled on the spot are communicated to the heads of the PSUs and the concerned departments of the State Government through Inspection Reports (IRs). The heads of PSUs are required to furnish replies to the IRs through the respective heads of departments within a period of six weeks. IRs issued up to March 2009 pertaining to 91 PSUs disclosed that 3,377 paragraphs relating to 739 IRs remained outstanding at the end of September 2009. Of these, 211 IRs containing 1,406 paragraphs had not been replied to for one to five years. Department-wise break-up of IRs and paragraphs outstanding as on 30 September 2009 is given in ***Annexure 15***.

Similarly draft paragraphs and reviews on the working of PSUs are forwarded to the Principal Secretary / Secretary of the administrative department concerned demi-officially seeking confirmation of facts and figures and their comments thereon within a period of six weeks. It was, however, observed that 11 draft paragraphs and one draft review forwarded to various departments during March-June 2009 as detailed in ***Annexure 16*** had not been replied to so far (September 2009).

It is recommended that the Government should ensure that (a) procedure exists for action against the officials who fail to send replies to IRs / draft paragraphs / reviews and ATNs on recommendations of COPU as per the prescribed time schedule, (b) action is taken to recover loss / outstanding advances / overpayment in a time bound schedule, and (c) the system of responding to audit observations is revamped.

Thiruvananthapuram **(S.NAGALSAMY)**
The **Principal Accountant General (Civil and Commercial Audit), Kerala**

Countersigned

New Delhi **(VINOD RAI)**
The **Comptroller and Auditor General of India**