CHAPTER IV

TRANSACTION AUDIT OBSERVATIONS

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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

4.1 Loss making Public Sector Undertakings – reasons for losses

As on 31 March 2012, there were 116 Public Sector Undertakings (PSUs), of which 96 were working. The total investment by the State Government in these PSUs as on the above date was ₹5837.49 crore (equity ₹4422.85 crore and long term loans ₹1414.64 crore). Of the 34 loss incurring working PSUs, 17 PSUs had been incurring losses continuously for five years or more and the entire equity capital (₹1002.63 crore) was eroded by their accumulated loss of ₹3219.27 crore.

Out of the above mentioned 17 PSUs, 12 PSUs had a paid up capital of ₹10 crore or more. We identified four geographically distributed PSUs viz, Kerala State Warehousing Corporation, Kerala State Handloom Development Corporation Limited, Kerala State Cashew Development Corporation Limited and Autokast Limited, and conducted an analysis of their activities for the period from April 2006 to March 2012[1] under the broad categories of functioning of Board of Directors, Operational issues and Government support to ascertain the reasons for such huge and recurring losses. The deficiencies noticed in these aspects are discussed in succeeding paragraphs.

We found that all the four selected PSUs had deficiencies in Operational and Marketing activities and except Kerala State Handloom Development Corporation Limited, all three had issues in the functioning of Board of Directors. The areas where deficiencies were noticed in the selected PSUs is discussed below:

4.1.1 Kerala State Warehousing Corporation

Kerala State Warehousing Corporation (Corporation) is engaged in acquisition, construction and running of warehouses in the State for the storage of agricultural and notified commodities. The Corporation, with its Head Office at Ernakulam has nine Regional offices, three Zonal offices and operates 59 warehouses with 1.98 lakh MT warehousing capacity as on 31 March 2012. The Corporation had been continuously incurring operating losses during the last five years ***(Annexure 20).*** The Corporation incurred a loss of 36 paise for every rupee of operating income earned. We observed that this was due to the absence of an effective Board of Directors, high operating cost and poor revenue generation as discussed below:

[1] **Due to delay in finalisation of Annual Accounts of the PSUs, some of the analysis was limited to the period up to 2010-11.**

Functioning of Board of Directors

As per Section 20 (1) of the Warehousing Corporations Act, 1962 (Act), the general superintendence and management of the affairs of a state warehousing corporation shall vest in a Board of Directors comprising 10 directors[2] and Managing Director appointed by the State Government under intimation to Central Warehousing Corporation (CWC). We, however, found that there were several deficiencies in the functioning of the Board of Directors as detailed below:

Lack of interest by the Directors

As per the Section 20 (4) of the Act, the Board of Directors shall act on business principles having regard to public interest and shall be guided by such instructions on questions of policy as may be given to them by the State Government or the Central Warehousing Corporation. We, however, noticed that during the five year period ending on 31 March 2012, directors' absenteeism was as high as 44 *per cent*[3]**.** Three Directors did not attend even a single meeting during their tenure[4]. This indicated lack of interest of the directors in the affairs of the Corporation and the Board of Directors did not take cognizance of the major problems of operational inefficiencies and continued losses.

The Corporation stated (August 2012) that the absenteeism of directors was not intentional. Further, on the advice of the Board, the Corporation was trying to close down the continuous loss making hired warehouses. The high absenteeism, however, defeated the very purpose of appointment of the directors and adversely affected the performance of the Corporation as well as decision making process and corporate governance.

Ineffective Audit Committee

Audit Committee was formed in July 2008, but no meetings were conducted during the year 2011-12. As a result, several important issues such as ineffective internal audit system, delay in finalisation of accounts etc. were not discussed. The Corporation accepted that due to certain changes occurred in the constitution of the Board, the sub committees had to be reconstituted and hence the Audit Committee could not be convened. This, however, shows lack of effective corporate governance.

Frequent change of Chief Executive Officer

During the period from November 2009 to March 2012, the Managing Director of the Corporation was changed five times, with tenure varying from one month to 12 months**.** Such frequent changes of the Chief Executive Officer also hampered the smooth functioning of the Corporation. The Management apprised (August 2012) that the appointment of a full time Managing Director was under active consideration of the Government.

Operational Inefficiencies

The Corporation rents out storage space in two ways; normal warehousing basis (based on quantity) and reservation basis (area/quantity based), including bulk

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[2] Five directors each nominated by the Central Warehousing Corporation and Government of Kerala.
[3] (Required attendance – Actual attendance/Required attendance)* 100: (209-117/209)*100 = 44 %.
[4] From July 2006 to December 2010, November 2008 to July 2010 and December 2006 to December 2007.

reservation scheme for two PSUs. We found the following weak areas in its operational activities:

High cost of operations

Since the expenses remained higher than the operational income, we analysed the expenses and found that employee cost was the single largest item constituting about 78 *per cent* of the total expenditure. We also found that the revenue earned was insufficient to meet even the employee cost. For example, for every rupee of revenue earned, the Corporation incurred (2010-11) ₹1.03 towards manpower. Considering all other costs, the Corporation spent ₹1.36 to generate an income of one rupee ***(Annexure 21).*** The reasons for high employee cost were as discussed below:

Administrative set up

Administrative staff

The Corporation has a three tier administrative set up consisting of Head office, three Zonal offices and nine Regional offices, with a total man power of 110, to manage the affairs of 59 warehouses. The warehouses have an additional manpower of 286 raising the total staff strength to 396. Out of the total establishment expenditure, about 1/3rd was on the administrative staff in the Head office, Zonal offices and Regional offices.

The Corporation replied that the three tier administrative set up was with a view to manage the business effectively. The fact remained that the Corporation did not analyse the high administrative cost and present administrative set up did not improve the performance of the Corporation.

Staff in warehouses

The Corporation employs its own staff in the warehouses for carrying out various related activities like receipt and issue of commodities, maintenance of books/records, fumigation and other godown keeping activities and overall supervision. Out of 59 warehouses, only 14 warehouses were able to generate sufficient revenue to meet even the employee cost ***(Annexure 22*****)**. The Corporation replied that the staff pattern and strength were fixed after taking into account the works related to its activities. The Corporation should reassess the staff requirement scientifically and rationalise deployment of the existing staff.

Small and unviable size of the warehouses

We found that the size of the warehouses of the Corporation ranged from 770 MTs to 11000 MTs. Considering the potential revenue and staff cost as per norms, the warehouses with a capacity of 10000 MTs (at 90 *per cent* capacity utilisation) alone could achieve breakeven. Considering this, 55 out of 59 warehouses of the Corporation were uneconomic in size ***(Annexure 23)***. The Corporation acknowledged that a number of warehouses were small in size as they were functioning in rural areas to cater to the needs of the rural population.

Comparison with Central Warehousing Corporation

To understand the high cost of operations, we compared the Corporation with CWC operations in Kerala. We found that the average size of the warehouse of the Corporation was much smaller i.e. only 1/3rd of the size of the CWC warehouse; but the employee strength was four times higher with a heavy administration structure as shown below:

Sl. No	Item	CWC	Corporation	Audit comment
1	Warehouses	13	59	Uneconomic size
2	Storage capacity	1.54 lakh MT	1.98 lakh MT	
3	Average size	11,846 MT	3,355 MT	
4	Administration Offices	1 no	12 nos (3 tier)	Excess manpower
5	Office Staff	15	110	
6	Warehouse Staff	59	286	
7	Total staff	74	396	
8	Capacity-Employee ratio	2081:1	500:1	
9	Employee cost for 2010-11	₹4.20 crore	₹11.82 crore	High employee cost
10	Employee cost/MT	₹273	₹597	

It was replied that the high variance in operating cost was because of the concentration of CWC in highly potential areas while the Corporation caters to the needs of rural beneficiaries. But the fact remains that for improving the performance of the Corporation, the capacity-employee ratio needs to be improved.

Low income generation

We also observed that along with the high cost of operations, low income generation aggravated the loss as explained below:

- During the year 2011-12, only 14 out of 59 warehouses had occupancy of 80 *per cent* or above. Average capacity utilisation of the warehouses was only 59 *per cent* and 68 *per cent* in 2008-09 and 2009-10 respectively and 62 *per cent* in 2010-11 and 2011-12. The Corporation, however, had not even worked out the breakeven level and taken any effective action to maximise the capacity utilisation of its warehouses.

  While accepting that the capacity of the warehouses was not being fully utilised, the Corporation clarified that the occupancy of warehouses was dependent on various factors like climatic conditions, market price of agricultural produce and procurement programmes of governments. However, continuous poor occupancy indicated lack of initiative of the Corporation to maximise its capacity utilisation and formulation of business plan.

- Though the occupancy of the warehouses was very low, the Corporation did not formulate any business plan, marketing strategy etc. to attract more business. We noticed that Kerala State Beverages (M&M) Corporation Ltd. and Kerala State Civil Supplies Corporation Ltd. occupied about 29 *per cent* of the total area under the Bulk Reservation Scheme and generated 45 *per cent* of the total income of the Corporation. But for the revenue from bulk reservation, the operations of 47 out of 59 warehouses would have ended up in loss for the year 2011-12 ***(Annexure 24)***. Further, the two PSUs used their own staff to manage stock in the Corporation's warehouses under the scheme. The staff of the Corporation deployed in these warehouses was idling.

The Corporation responded that storage space provided to two PSUs was to ensure guaranteed occupancy. Reduced rates extended to them were adversely affecting income of the Corporation. The fact however, remained that given the low return from such warehouses, the Corporation should have taken efforts to reduce the employee cost by suitable re-deployment of idle staff.

- Warehousing charges being the main source of revenue should have been fixed keeping in view the prevailing market rates and cost of operation. The Corporation, however, revised (January 2008) its rates only after a lapse of seven and half years. Thereafter, the rates were being revised on biennial basis. The Corporation apprised that the tariff was revised with effect from 01 April 2012. The rate revision, however, was not made scientifically, but arbitrarily enhanced by 20 *per cent.*
- The Corporation allotted 19459 sq.ft of warehouse space to various customers for functioning as office. We noticed that CWC levies 50 *per cent* higher rent for its warehouse area rented out as office space. The Corporation, however, did not have the practice of applying differential tariff for office space and warehouse space though an area of 19459 sq.ft was utilised for office purpose by the customers. Accepting our suggestion, the Corporation agreed to enhance the rates for office space.

Government Assistance

The Government of Kerala and CWC, together had invested (March 2011) ₹10.75 crore as equity in the Corporation. The Corporation, instead of providing a return on equity, incurred a loss of ₹1.56 for every rupee invested. During the last five years ending 31 March 2012, the assistance by Government and CWC amounted to ₹5 crore (equity ₹2.25 crore and grants ₹2.75 crore).

4.1.2 Kerala State Handloom Development Corporation Limited

The main objective of Kerala State Handloom Development Corporation Limited (Company) is developing the handloom industry in the State. The Company functions with a Corporate office at Kannur and three Regional offices at Kannur, Ernakulam and Thiruvananthapuram. It has 33 procurement centres, four processing units/dye houses and three regional stores.

The Company had been continuously incurring operating losses during the five year period ending 31 March 2011 ***(Annexure 25)***. We observed that high operating expenditure, insufficient margin, poor sales performance etc. were the major reasons for the continuous losses as discussed below:

Operational issues

The Company procures yarn mainly from National Handloom Development Corporation Ltd. which is issued at cost to the registered weavers for making different kinds of fabrics. These fabrics are purchased back at pre-determined prices i.e. cost plus wages and are marketed by the Company at prices fixed by adding 15 to 38 *per cent* towards margin, through showrooms and direct sales.

We identified the following areas of operational inefficiency:

High Operating Expenditure

We found that during the review period, to generate one rupee sale the Company had to spend ₹1.41 on an average ***(Annexure 26)***. The major elements forming part of the expenditure of the Company were material consumed, employee cost and wages and production incentive to weavers.

While accepting our contention, the Company stated (September 2012) that it was not in a position to reduce the high operating expenses.

Meagre monetary benefit to weavers

The basic objective of the Company is to develop handloom industry. We, however, found that the benefits accrued to weavers were negligible.

- Though there were 6500 weavers registered with the Company, only 1200 to 1580 weavers *(22 per cent)* were active during the review period, indicating poor achievement of its social objective.
- As on 31 March 2011, the Company had 297 staff to support the activities of the weavers and to carry out other operations. We observed that for every rupee of sale, the weavers on an average received only 25 paise as against 37 paise paid to the staff of the Company. Further, average annual monetary benefit received by a weaver during the period was only ₹0.25 lakh as compared to ₹1.58 lakh received by an employee.

While accepting that low earnings of the weaver was the main reason for downfall in weaver strength, the Company stated that the wage of the weavers was fixed based on the industrial standards. It was also clarified that a proposal for semi-automation of production was submitted to Government for increasing the productivity and the earning capacity of the weavers. The fact, however, remained that the Company could not achieve the social objective which was to uplift the living conditions of the traditional weavers in the State.

Poor sales performance

The sales of the Company through showrooms (56 showrooms and two mobile sales vans) accounted for 71 *per cent* (₹39.46 crore) of the total sales (₹55.35 crore) during the period from 2006-07 to 2010-11 and the balance was through seasonal exhibitions, agency showrooms and direct sales. We observed that despite the huge infrastructure for marketing, the Company took, on an average, 262 days[5] to sell its finished fabrics indicating poor marketing strategy. Further analysis revealed that:

- 82 *per cent* of showroom sales were during the rebate period[6] of 71 days per year on an average.
- The balance 18 *per cent* sales were achieved during the remaining period of 294 days for which the showrooms functioned throughout the year. As

[5] **Days in Inventory = 365 days/(Cost of sales/average inventory).**

[6] **Period during which Central and State Governments allow rebate for handloom products.**

a result, the margin achieved during the rebate period was wiped off by the expenses during the remaining period.

- The Company did not undertake adequate promotional activities and also did not fix any monthly/ annual sales target. As such the showroom staff did not have any pre-set goal to achieve and had no motivation which led to piling up of finished products. During the year 2010-11, the Company held an average monthly stock of ₹960.23 lakh against the average monthly sale of ₹84.72 lakh. Further, the selling and distribution expenses incurred by the Company were only 2.24 to 3.20 *per cent* of sales.

The Company stated that showroom-wise targets were given and closely monitored to improve the performance. During non-rebate period sales staff was used to canvas institutional orders. It was also stated that hectic efforts were being made to obtain bulk orders from Government departments. However, the Company has yet to get any favourable orders from the Government.

Insufficient margin-a pointer to increase sales and reduce cost of sales

The need for increasing sales and reducing cost was evident from the low sales margin which was insufficient to meet the operating expenses. We observed that, during the period from 2006-07 to 2010-11, the average margin[7] obtained by the Company was ₹323 lakh. This was not sufficient to meet even the salary and wages paid to the staff and administration and selling expenses amounting to ₹688 lakh. The Company concurred with the audit observation.

Government assistance

The Government of Kerala had invested (March 2010) ₹18.08 crore as equity in the Company. Against the above, the Government suffered a loss of ₹2.33 on every rupee of its investment. During the five year period, the Government disbursed an amount of ₹41.22 crore to the Company by way of equity (₹10.90 crore), loans (₹0.87 crore) and grants etc (₹29.45 crore[8]). Despite this, the Company continued to incur losses. This indicated failure of the Company to capitalise on the substantial financial assistance extended by Government.

4.1.3 Autokast Limited

Autokast Limited (Company) was incorporated in 1984 with the objective of promoting, undertaking, financing, executing and developing ferrous and non ferrous castings to meet the requirements of industrial units in the State of Kerala or elsewhere. The Company had been continuously incurring operating losses during the five year period ending 31 March 2011. The major reasons for continued losses, in addition to frequent changes in the management, were insufficient value addition, mismatch in capacity, low labour productivity, excessive consumption of power and high rate of rejections as discussed below:

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[7] **Sales less (material consumed and manufacturing expenses).**
[8] **Grant (₹10.36 crore), Subsidy (₹2.24 crore), Rebate(₹11.52 crore), Marketing Incentive (₹5.33 crore).**

Tenure of Chief Executive

The tenure of service of the Chief Executive had to be long enough to enable continuity in decision making. We noticed that the Managing Director was changed four times with tenure ranging from seven months to 17 months having adverse effect on the decision making process. Meetings of the Board of Directors/Audit Committee were, however, conducted regularly.

Operational issues

The production process involves feeding of raw material consisting of Cold Rolled Continuously Annealed scrap, Pig Iron, MS Scrap etc, into the Induction Furnace for melting. Necessary additives are added for maintaining the properties of castings as required by the individual customers. The molten metal is then poured into the moulds and after cooling, the same is decored, fettled and machined to form the finished product as per the requirement of the customer.

Expenditure incurred by the Company to generate one rupee sales during the review period was as detailed below:

(in ₹)

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11	Average
Raw material consumed	0.46	0.46	0.48	0.27	0.41	0.41
Manufacturing expense	0.33	0.32	0.28	0.32	0.27	0.31
Employee cost	0.36	0.39	0.40	0.41	0.35	0.38
Other expenses	0.06	0.20	0.20	0.06	0.06	0.12
Total expenditure	1.21	1.37	1.35	1.07	1.10	1.22
Loss	**0.21**	**0.37**	**0.35**	**0.07**	**0.10**	**0.22**

As could be seen, to generate one rupee of sale, the Company had to incur an average total expenditure of ₹1.22. Major elements of expenditure were raw materials consumed, manufacturing expenses and employee cost. In this regard, we identified the following areas of operational inefficiency:

Mismatch in capacity

We noticed that the maximum quantity melted and moulded in a month during the year 2011-12 was 403 MT whereas the maximum fettling[9] in a month was only 325 MT including quantity out sourced indicating mismatch in capacity at different stages (***Annexure 27***). This led to under utilisation of the melting capacity in addition to excess consumption of power.

While accepting the existence of mismatch in its melting and fettling capacities, the Company stated (August 2012) that additional fettling facilities have been added and efforts were on to further minimise the mismatch in melting and fettling capacities.

Labour productivity

The major element of cost, other than raw material, was employee cost, which constituted nearly 35 to 41 *per cent* of sales revenue. To minimise the employee cost per MT, every effort should be made to maximise labour productivity.

[9] **Removal of protrusions, runners, risers etc from the decored castings.**

The actual productivity, however, varied from 0.45 MT to 0.62 MT during the five years ending 31 March 2011 as compared to the standard[10] labour productivity of 1.2 MT per month, resulting in under utilisation of manpower ***(Annexure 28)***. The actual labour cost per MT amounted to ₹23984 as against the standard cost of ₹10749.

The Company replied that low labour productivity was due to the high employee turnover and shift in the product mix from high weight items to low weight items.

Excess consumption of power

The actual consumption of power varied from 2200 units to 2800 units per MT for the last five years ending 31 March 2011 against the envisaged 1500 units in the project report. The excess consumption of power resulted in increase in average cost of production for the last five years by ₹4108 per MT constituting 37.04 *per cent* of cost of power (***Annexure 29***).

The Company stated that most of the machines in operation were 25 years old which was the major reason for high power consumption. The Company also stated that they were vigilant in bringing down the power consumption and had achieved 1647 unit per MT of production during the month of June 2012.

High rate of rejection

The production process should be managed efficiently to ensure product conformity with customer requirement keeping the rejection level to the minimum. While industrial norm for in-house rejection was 4 *per cent* and customer rejection 1 *per cent*, the actual in-house rejection ranged from 4.90 to 7.61 *per cent* and customer rejection from 1.68 to 3.16 *per cent* during the last five years. The reasons identified by the Company for excessive rejections were poor quality of sand used, poor workmanship etc.

The Company replied that rejection was a matter of concern for them and steps had been taken for containing rejection. It further stated that current rejection levels were within the industry norm. The reply was not acceptable as present rejection levels were also very high i.e. 10.02 *per cent* and 9.55 *per cent* for July and August 2012 respectively as compared to the industrial norm.

Insufficient value addition

Value addition[11] achieved by the Company varied from ₹27678 per MT to ₹41068 per MT (100 to 127 *per cent* of the cost of raw materials) during the period. This, however, was not sufficient to meet even the manufacturing and labour cost of ₹36102 per MT to ₹51896 per MT (126 to 157 *per cent* of cost of raw materials) over the last five years ***(Annexure 30).***

The Company pointed out their inability to import steel scrap during import friendly time and hold sufficient stock of raw material due to working capital shortage apart from stiff competition in casting market as the reasons for insufficient value addition. The Government may consider addressing the issue of working capital shortage.

[10] Source: Detailed Project Report.
[11] Value addition = sales – cost of raw material.

Government assistance

The Government of Kerala invested (March 2011) ₹19.97 crore as equity in the Company. Against the above, the Government suffered a loss of ₹5.12 on every rupee of its investment. During the review period up to 31 March 2011, the Company received ₹27.63 crore by way of loans (₹23.81 crore) and grants (₹3.82 crore) from Government of Kerala which constituted ₹24735 per MT of sales and 103.13 *per cent* of the employee cost (₹23984 per MT).

4.1.4 The Kerala State Cashew Development Corporation Limited

The Kerala State Cashew Development Corporation Limited (Company) was incorporated in 1969 with the objective of developing cashew industry so as to provide employment to cashew workers in the State. During the year 2011-12 the Company provided on an average 179 working days (28.94 lakh mandays for 16137 workers) through its 30 cashew processing factories across the State. The Company had been continuously incurring operating losses during the five year period up to 31 March 2011. We found that high cost of procurement and low rate of sales realisation were the major reasons for the continuous losses. We also noticed that the Board of Directors failed to constitute Audit Committee, an important measure of internal control and corporate governance. These are discussed in detail below:

Functioning of the Board of Directors

In line with the provisions of Section 292A of the Companies Act, 1956, the Government, with a view to strengthen the corporate governance, issued (November 2008) direction for the formation of Audit Committees by every State Level Public Sector Enterprise. We observed that though 79 meetings of the Board of Directors of the Company were held during the last five years, the Audit Committee, an important pillar of corporate governance had not been constituted so far (June 2012). Hence the transparency in decision making, accuracy of financial reporting and disclosures, robustness of internal control and internal audit functions etc. were not being properly evaluated or monitored in the Company.

The Company replied (August 2012) that internal control system envisaged for the Audit Committee was looked after by the Board of Directors. The reply indicated the violation of Government direction.

Operational inefficiencies

The Company procures raw nuts and allots to 30 factories for processing. The raw nuts are drum-roasted/steam-roasted to produce roasted cashew nuts, which are shelled (removal of shells), peeled (removal of the outer skin of kernels) and graded into different varieties.

We noticed that the Company had to spend ₹3.02 lakh to produce one MT of cashew kernel. However, sales realisation was only ₹2.18 lakh per MT resulting in loss of ₹0.85 lakh per MT as shown below:

(Amount ₹ in lakh)

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11	Average
			(provisional)			
Sales quantity (in MT)	3660.18	3775.44	5327.56	7516.41	7719.49	-
Sales realisation per MT	1.73	1.64	2.38	2.38	2.75	2.18
Value of Materials per MT of sales	1.39	1.08	1.78	1.70	2.16	1.62
Employee cost per MT of sales	1.00	1.18	0.72	0.76	0.76	0.88
Other expenses per MT of sales	1.14	1.23	0.09	0.06	0.06	0.52
Total expenditure per MT of sales	**3.53**	**3.49**	**2.59**	**2.52**	**2.98**	**3.02**
Net loss per MT of sales	**1.80**	**1.85**	**0.21**	**0.14**	**0.23**	**0.85**

We observed that for every rupee of sale the Company incurred 74 paise towards raw materials, 44 paise towards employee cost and 30 paise towards other expenses leading to a loss of 48 paise.

Procurement of raw cashew nut

The Company procured raw cashew nuts from suppliers based on open tenders through advertisements. In this regard we noticed the following:

Dilution of tender process

Central Vigilance Commission (CVC) guidelines stated that '*as post tender negotiations could be a source of corruption, it is directed that there should be no post tender negotiations with L-1 except in certain exceptional situations*'. The Board of Directors, however, conducted post tender negotiations with all bidders and orders were placed with the lowest negotiated tenderer.

The Company stated (August 2012) that inviting only the lowest tenderer for negotiations would lead to cartel formation. The reply is not acceptable as it indicates the violation of CVC guidelines.

High rate of procurement

The major source of raw cashew nuts was imports. The average procurement rate of raw cashew nuts of the Company was higher than the average rate published by the Directorate of Cashew and Cocoa Development (DC & CD) as shown below.

(Amount in ₹)

Year	Procurement rate per MT		Excess
	Company	DC & CD	
2008-09	46782	43450	3332
2009-10	43445	40342	3102

We also observed that the Company was depending on a single supplier (JMJ Traders) for majority (49.50 to 99.77 *per cent)* of its raw nuts requirement for the period from 2008-09 to 2011-12.

The Company stated that the rates published by DC & CD may not reflect the actual rate as they were based on the statistics collected by them. But the fact remained that the present procurement procedure followed by the Company had not fetched the competitive rate as the procurement rate was higher than the average All India rate.

Low rate of sales realisation

Efficient marketing of the product through proper advertising and sale of the product at most competitive rates ensures increased sales realisation and thereby better profitability. The Company, however, had not formulated any marketing policy. We noticed that the Company marketed only a small quantity (three *per cent*) under its brand name 'CDC Cashew' and the remaining portion was sold to wholesale traders. In respect of wholesale trade, the Board of Directors entrusted the Managing Director to sell the cashew kernels based on the then prevailing market rates. Thus, the Company sold the cashew kernels on the basis of rates fixed by the Managing Director in a non-transparent manner without inviting any competitive tenders. This unfair practice of marketing resulted in low rate of sales realisation.

As a result, the average sales realisation per MT of cashew kernel obtained for the years 2008-09 and 2009-10 were less than the rate published by DC & CD, as shown below:

(Amount in ₹)

Year	Average sales realisation per MT		Shortage
	Company	DC & CD	
2008-09	217837	272858	55021
2009-10	213286	268759	55473

The Company replied that selling price of the cashew kernel was controlled by international market which varied day by day. Sales contract was finalised between MD and the buyer based on the price offered by the buyer on daily basis. The fact, however, remained that the recommendations of the Committee on Public Undertakings (CoPU) to adopt well defined sales and marketing policy in consultation with an expert agency is yet to be implemented.

Insufficient value addition- impact of high procurement cost and low sales value

The impact of high procurement cost and low sales realisation resulted in low sales margin which was insufficient to meet cost of production. Sales margin earned by the Company ranged from ₹33933 per MT to ₹67825 per MT (24 to 53 *per cent* of cost of raw material) during the review period. This was not sufficient to meet even the labour cost of ₹72190 per MT to ₹118039 per MT over the review period.

Thus, considering the import/export rates published by DC &CD, there was scope for reducing the raw material cost by ₹0.13 lakh[12] and increasing sales revenue by ₹0.55 lakh per MT of cashew kernels. Thus, ensuring transparency in procurement and sales alone has a scope for reducing the loss of the Company by ₹0.68 lakh per MT of sales.

The 42nd Report of CoPU (July 2003) stated that:

- The Company should adopt well defined sales and marketing policy in consultation with an expert agency.

[12] **four kilograms of raw cashew nuts required to produce one kg of Cashew kernel ie., (₹3332+₹ 3102/2) * 4**

- The system of procurement of raw cashew nuts required to be streamlined in such a way that the same does not exceed the All India procurement cost.

In spite of CoPU recommendations, the Company had neither streamlined the system of procurement of raw cashew nuts nor regulated the cost so as to ensure sufficient margin to meet the expenses. We also observed that the recommendation of the expert agency appointed by the Government with regard to inviting only the lowest tenderer for negotiations was relaxed by the Government themselves and permitted the Company to continue with the prevailing practice of giving chances to the bidders to amend their rates after knowing the rates quoted by other bidders.

The Government should review the permission granted to the Company for conducting negotiations with all the tenderers. The Company replied that measures would be taken to reduce the cost of production.

Government assistance

Government assistance to the Company is for strengthening its financial base to enable it to achieve better performance. We noticed that Government of Kerala had invested (March 2008) ₹200.64 crore as equity in the Company. Against the above, the Government suffered a loss of ₹3.66 on every rupee of its investment. The Government provided ₹176.41 crore from the exchequer to the Company by way of loans (₹93.19 crore) and grant (₹83.22 crore) during review period. This amounted to ₹63005.11 per MT of sales as against ₹71886 per MT incurred towards salary and wages (₹201.27 crore) of factory staff and workers.

The matter was reported to Government in July 2012; their reply was awaited (November 2012).

4.2 Transformers and Electricals Kerala Limited

Avoidable loss

Reckoning the gross weight including the weight of kraft paper as the weight of copper conductor returned after fabrication resulted in loss of ₹1.08 crore.

Transformers and Electricals Kerala Limited (Company) is engaged in the manufacture of Power Transformers and one of the major raw materials used in the process is Paper Covered Copper Conductor (PCC). Annual requirement of PCC is around 900 MT. The Company procures Continuous Cast Copper Wire Rod from copper manufacturing companies and gets it converted into PCC by insulating with imported kraft paper on a weight to weight basis through fabricating contractors. During the fabrication process, copper rod is converted into rectangular conductors of specified sizes by drawing, rolling, annealing and covering with imported kraft paper of specified number of layers. After completing the process, the PCC is returned on a weight to weight basis, ie. for 100 kg of copper rod supplied, the contractor returns 100 kg of PCC to the Company. This indicated that the process does not involve any loss/ wastage of copper.

During the scrutiny of the contracts for fabrication of PCC for the period 2010-11 and 2011-12 we noticed (December 2011) that while returning the finished product (PCC) on a weight to weight basis, for every 100 kg of copper rod supplied, the contractor returned 100 kg of PCC including the weight of the kraft paper ranging from 0.9 to 9.04 *per cent* of PCC resulting in advantage to the contractor and loss to the Company. The Company thus lost ₹1.08 crore in respect of 1127.37 MT[13] of PCC consumed in the manufacture of 127 power transformers during 2010-2012.

The Company stated (July 2012) that when copper rods were converted into rectangular conductors there was scrap, the amount of which may vary on case to case basis. It was further added that there was no loss to the Company and even the notional profit/loss was minimal after considering a scrap of 3 *per cent* of which 60 *per cent* was saleable. Further, the contractors were not willing to change the prevailing practice and return 103 kg of PCC for every 100 kg of copper rod supplied. The Government endorsed (August 2012) the reply of the Company.

The reply was not correct as the supply condition of 'weight to weight basis' itself indicated that the process did not involve any loss. No scientific assessment as to copper scrap, if any, generated *vis a vis* the quantity of paper used and its cost implication was carried out by the Company. The Management, however, admitted that the realisable price of scrap was only notional and not actual. On being pointed out (October 2011) by us, the Company took up the matter and the contractors offered a reduced rate of ₹6.80 per kg towards conversion charges in the subsequent tender (November 2011) as against ₹9.35 per kg charged for the past three years.

4.3 Kerala Minerals and Metals Limited

Avoidable extra expenditure

Purchase of Liquid Oxygen by unwarrantedly enhancing the accepted rates resulted in avoidable extra expenditure of ₹0.55 crore.

The Kerala Minerals and Metals Limited (Company), manufactures Titanium Dioxide Pigment from the raw material Ilmenite. Liquid Oxygen (LOX) with 99.5 *per cent* purity is used in the production process to remove impurities from Ilmenite. The estimated annual requirement of LOX is about 18000 MT. The Company has a captive plant that produces about 50 *per cent* (9000 MT) of the requirement. The balance 50 *per cent* is purchased at the rate of 750 MT per month (9000 MT annually) from private suppliers.

The Company invited (August 2009) limited tenders from five suppliers for the supply of 9000 MT (6930000 SM^3)[14] of LOX for one year and four firms offered their rates. Though the lowest bidder (₹10.35 per SM^3 (landed cost)) was Bhuruka Gases Limited, they could offer only about 387.5 MT per month (52 *per cent* of the monthly requirement). Hence, the Company negotiated with the other suppliers and placed (November 2009) orders with all the four firms[15] at the rate offered by Bhuruka Gases Ltd.

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[13] **2010-11 (708.33 MT) and 2011-12 (419.04 MT).**

[14] **1 MT equals 770 SM^3, SM^3 - Standard Meter Cube.**

[15] **Bhuruka Gases Ltd. (4500 MT), Praxair India (P) Ltd. (1800 MT), Inox Air Products Ltd.(1800 MT) & National Oxygen Ltd.(900 MT).**

Praxair India (P) Ltd (firm), one of the four suppliers, supplied 2292112 SM^3 of LOX during the period from January 2010 to January 2011 at a total price of ₹3.40 crore. We observed the following deficiencies in the contract/supplies made by the firm:

- Orders were placed with the firm though, according to the Company, the firm was not dependable and not even completed supplies against earlier orders.
- As per Clause 3 of the agreement, the price was fixed and firm, and not subject to any escalation till the completion of supply of the entire ordered quantity. The firm, however, demanded (January 2010) enhanced rate of ₹13.74 per SM^3 (landed cost). The reason cited was increase in power costs. The firm supplied 40764 SM^3 (53 MT) during January 2010 at the original rate. Meanwhile, the Company accepted the request and increased (1 March 2010) the price to ₹13.74 per SM^3 (landed cost) and reduced the total quantity to 616000 SM^3 (800 MT). The other firms were, however, supplying at the original rate itself. Thus, amendment to price, contrary to the agreement, after finalisation of tender and award of contract resulted in avoidable extra expenditure to the extent of ₹0.11 crore in respect of 463667 SM^3 of LOX supplied during March 2010 to June 2010.
- The Company, during the contract period, placed (8 July 2010) another order with the firm for the supply of 2307000 SM^3 of LOX at the mutually agreed rate of ₹18 per SM^3 (landed cost) without inviting competitive tenders.
- Subsequently, the Company amended (20 October 2010) the order giving it retrospective effect from 8 May 2010 and clarified that the price applicable for supply of 150 MT in a calendar month would be ₹13.74 per SM^3 and for supplies over and above 150 MT during the same month would be ₹18 per SM^3. Accordingly, the firm supplied 805960.6 SM^3 (150 MT per month for the period from July 2010 to January 2011) at ₹13.74 per SM^3 and 981720.7 SM^3 (quantity supplied over and above 150 MT) at ₹18 per SM^3. This was in violation of tender stipulation that the successful tenderer should cater to any increase in requirement during the contract period. During the same period, the other two firms supplied LOX @ ₹12.78/12.48 per SM^3. Award of a new contract at mutually agreed higher rates during the currency of the existing contract resulted in avoidable extra expenditure of ₹0.44 crore. The monetary impact on the post contract modification of prices are summarised below:

PO No.	Period of Supply	Rate per SM^3(₹)	Quantity (SM^3)	Actual payment effected (₹)	Payment to be made (₹)		Excess Payment (₹)
					Rate	Amount	
2374/09-10 dtd.23.11.2009	Jan & Feb 10	11.19	40763.8	456031	11.19	456147	**Nil**
3507/09-10 dtd.3.3.2010	Mar to June 10	13.74	463667	6338629	11.19	5188434	**1150195**
1153/10-11 dtd.8.7.2010	July to Jan 11	13.74	805960.6	10996051	12.78	10300177	**695874**
	May to Dec 10	18	981720.7	16223681[16]	12.78	12546390	**3677291**
	Total		**2292112**	**34014392**		**25648734**	**5523360**

Thus, the procurement was made in an adhoc, arbitrary and non-transparent manner without satisfying the prime requirement of establishing

[16] **After deducting ₹13, 03,420 withheld from the invoiced amount.**

competitiveness, fairness and transparency. The decisions for enhancement of accepted rates and placing of further orders at higher rates without inviting competitive tenders were made by the Managing Director and never placed before the Board for discussions. Post contract modification of the prices to the advantage of the supplier without analysing the financial implications and placing of orders at mutually agreed rates vitiated the objective of procurement through competitive tenders and resulted in extra expenditure of ₹0.55 crore to the Company.

Management stated (September 2012) that procurement of LOX at higher rates was unavoidable for uninterrupted operation since production from captive plant had come down to 30 TPD[17] whereas the requirement for targeted production was 65 TPD.

The reply was not acceptable as the captive production envisaged for assessment of requirement was 9000 MT per annum i.e. 25 TPD only which was below the production of 30 TPD from captive plant. Further, the actual average monthly procurement for the period from March 2010 to January 2011 was 702.41 MT (i.e. 23.41 TPD).

The matter was reported to Government in July 2012; their reply was awaited (November 2012).

4.4 Role of Kerala SIDCO as a facilitator of Small Scale Industries in Kerala

Kerala Small Industries Development Corporation Limited (Company) was incorporated (November 1975)[18] with the objectives of protecting and promoting the interest of Small Scale Industries (SSIs) in the State. The major restricting factors[19] of Micro/Small Enterprises (MSEs) in Kerala were lack of demand for their products/deficient marketing and shortage of working capital. The activities pertaining to facilitation of MSEs were carried out by Industrial Estate/Park Division, Raw Material Division and Marketing Division of the Company. These three Divisions together contributed approximately 89 *per cent* of total turnover. We analysed the performance of these Divisions to assess the role of the Company as a facilitator of MSEs in the State. The major findings are discussed in the succeeding paragraphs.

Infrastructure support to Small Scale Industries

Industrial Estate (IE)/Industrial Park (IP) Division of the Company is responsible for providing infrastructure support to MSEs. The support is provided in two forms; Industrial Estates with all infrastructure facilities and Industrial Parks where only plots are allotted. Total area of Estates and Parks was 322.348 acres of which 258.32 acres (220.43 acres in IEs and 37.89 acres in IPs) were allotted to 1374 units till March 2012.

[17] Tonne Per Day.

[18] Company was originally incorporated as Kerala State Small Industries Development and Employment Corporation Ltd. to which the erstwhile Kerala State Small Industries Corporation Ltd was amalgamated (March 1977).

[19] As per MSME Census (2007) of Ministry of Micro, Small and Medium Enterprises, GOI.

Industrial Estate Division

The Government of Kerala transferred (March 1975) seventeen IEs and 36 mini IEs to the Company. Sheds/ land in IEs were allotted to prospective entrepreneurs on lease[20] /hire purchase basis. In accordance with the amendment (1971) to the Rules for allotment by Government to encourage the small scale industrialists and enable them to become the owners of factory sheds occupied by them in industrial estates, the Company gradually shifted (February 1996) from allotment of shed/land on lease basis to Outright Sale basis (ORS). During the period up to March 2012, out of the allotted 220.43 acres of land, the Company sold off 215.35 acres of land under ORS scheme to 1158 units. Currently, the Company's role is limited to management of the remaining 5.08 acres of land on lease under the possession of lessees for which it incurs an annual establishment expenditure of ₹1.01 crore (March 2012). The Company should take measures to reduce this unproductive expenditure.

Issues in transfer of ownership

Outright sale of sheds/land

Consequent to enhancement of land value by Government (April 1994), the Company fixed (February 1996) the price for land on hire purchase/ORS. The Government, based on the recommendations of One Man Commission (November 2001) decided (January 2003) to fix ORS value of land/shed considering the cost of land as on 1 April 1975 *plus* value addition @ six *per cent* per annum from April 1975 to the date of assignment *less* 75 *per cent* of lease rent paid.

Subsequently, the Government decided (May 2005) to give remission of 75 *per cent* of rent paid before adding six *per cent* for value addition. But a final decision to accept this formula was taken only in January 2011. Adoption of this formula was against Rule 8 of Rules of Assignment of Government land for industrial purpose for fixing land value[21]. We noticed that in case of 91 allotments (2005-2009), 38 lessees got the lease hold property at nil value and 53 lessees at nominal value consequent to which the Company suffered loss to the extent of ₹1.69 crore.

In line with enhancement of land value by Government in 1994, the Company revised the lease rent of sheds/land from April 1996. However, the Monitoring Committee appointed (May 2005) by the Government decided to realise lease rent at the rate applicable at the time of application for ORS (i.e. 31 January 1996) and accordingly the Company waived (March 2007) rent arrears amounting to ₹1.83 crore. As the lease rent was revised based on the enhancement in value of land, realisation of rent at pre-revised rates lacked justification and resulted in loss of ₹1.83 crore to the Company.

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[20] Lease rent fixed based on cost of land and development expenses. Amount is payable monthly.
[21] Land value to include interest @ six *per cent* per annum up to date of assignment.

Outright sale based on fair value

The Company started (February 1996) allowing ORS based on fair value fixed by revenue authorities. We noticed that the Company did not get the fair value[22] refixed periodically. In two out of 17 estates test checked, there was delay upto 12 years in revising fair value and allotments were made at the last available rates which were far below the prevalent fair value. However, as the fair value as on the date of allotment was not available, total loss on this account could not be quantified. In one instance where fair value was revised after one month of allotment, the loss worked out to ₹16.01 lakh.

Transfer policy promoting sale of industrial land

Consequent on change in policy from allotment of sheds/land on lease basis to ORS, the Company sold (1996 to 2012) 95.86 *per cent* of the allotable area in the Estates. Unprecedented appreciation in land value encouraged many of the ORS allottees to make profit from sale of land instead of using it for industrial activity. Outright Purchase Rules 1996, provided (Rule 16 (b)) for transfer of shed/land after remitting the difference between the current fair value and value already remitted to the Company. The Company relaxed (November 2009) the rule by allowing transfer without remitting the differential amount. We observed that this relaxation paved way for large scale transfer of land/shed as was evident from the transfer of 137 units during the period from January 2010 to April 2012 as against 17 units from January 2007 to December 2009. In respect of 49 units test checked, the difference between fair value (which was far below the market value) as at the date of transfer and the ORS value realised was ₹5.90 crore which could have been earned by the Company, had the transfer allotment policy not been liberalised.

One of the beneficiaries of the liberalised transfer allotment policy was a Director of the Board to whom the Company allotted (May 2010) a unit at Karunagappally estate. This unit was subsequently transfer allotted (October 2010) based on his request (July 2010). The land included in the transaction was worth ₹31.68 lakh against the original ORS value (April 2003) of ₹2.54 lakh. The Director did not bring this to the notice of the Board of Directors as required under section 299(1) of the Companies Act, 1956 for which he was liable to vacate the Office of the Director under section 283 (1)(i) of the Act. The transfer allotment was hence voidable at the option of the Company under section 297 (5) of the said Act.

The Company stated (August 2012) that the liberalisation in respect of the amount to be collected from the transfer allottees was based on the complaints received from the industrialists. The reply was not correct as the Company had no mechanism to ensure that the concession was passed on to the transferee with the objective to protect and promote the interests of MSEs. The concession was passed on to the transferor besides the loss to the Company.

Failure to ensure compliance of conditions of allotment

As per Rules 5 (e) and 6 (a) of Rules of Allotment of the Company, sheds/land allotted should not be transferred without prior permission and the Company

[22] **Value fixed by Revenue Authorities.**

had the power to resume the property if the unit became defunct/utilised for other purposes/transferred unauthorisedly.

We observed:

- The Company allowed transfer allotment[23] of 14 defunct units and six unauthorisedly transferred units instead of resuming those units. Based on fair value, the Company sustained a loss of ₹1.66 crore.
- In three estates visited, three allottees had not started business (for periods upto 32 years), 16 units remained idle for more than one year and six units were utilised for non-industrial purposes. The Company, however, did not initiate action to resume possession in case of 24 units (March 2012).
- The Company deleted (June 2009) the condition in the sale deed that the Rules of allotment of the Company will form its part. This enabled the purchaser to transfer the shed/land without permission of the Company and utilise it even for non- industrial purpose.

The Company stated that transfer allotment was allowed to units which became sick due to unforeseen reasons and it could revive considerable number of idling units. The reply of the Company is not acceptable as the action of the Company was contrary to the Rules of Allotment. The Company should have resumed these units and allotted afresh to eligible entrepreneurs and prevented the transferor making undue advantage.

Diversion of sales proceeds

During the period 2007-2012, the Company realised an amount of ₹6.48 crore from outright sale of industrial sheds/land. We observed that the Company utilised the sales proceeds for working capital requirements consisting of pay and allowance and other revenue expenses instead of acquiring and developing new estates for further promotion of industrialisation. In the absence of any new projects, the Company has abysmal role in the field of development of infrastructure for MSEs.

Industrial Park

In Industrial Parks, vacant plots are allotted to prospective entrepreneurs on 90 years lease basis realising lease premium[24]. Lease premium was fixed based on auction. The Company had seven Industrial Parks covering an area of 45.82 acres of which 37.89 acres had been allotted to152 units since 2003-04 leaving 0.37 acre.

As per Rule 9 (h) of Rules for Allotment of land in industrial parks, production was to commence within a period of two years from the date of agreement. Further, Rule 10 (a) provided for termination of agreement and resumption of land if positive action was not taken to start the industry within two years of allotment.

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[23] Transfer by the original allottee to another person.

[24] Sixty *per cent* of lease premium is collected upfront and balance 40 *per cent* in two yearly instalments. Token yearly rent of Re.1 /cent is also collected.

We observed:

- In four parks[25], 82 plots covering an area of 8.49 acres were idling and production was not commenced for periods ranging from two to six years. In six parks[26], with regard to 49 plots covering an area of 5.10 acres, only construction works were in progress/not completed even after one to eight years of allotment. Inaction on the part of the Company in resuming the idle plots as per Rules led to poor development of industrial parks. The Company assured (August 2012) to resume the idle plots immediately.
- Transfer allotment was not allowed within a period of 10 years. But, this period was reduced to 5 years (May 2010), 2 years (November 2010) and finally to one year (January 2011) thus enabling allottees to transfer the plots immediately after acquisition and make profit therefrom instead of setting up industrial units.
- Spot visit at IP Angamaly revealed that there was lack of infrastructure like boundary wall and common water supply. Two candle marketing units were allotted 59.24 cents of which one was used as shuttle court and parking area and the sheds were kept idle for long periods. It was also noticed that auction had not been conducted since August 2009 and land was being allotted at the rate fixed in 2009.

Transfer allotment policy adopted by the Company encouraged ingenuine entrepreneurs to make profit from sale of land rather than promoting industrial activity. Non-resumption of idle sheds/land and allotment to new entrepreneurs defeated the purpose of allotment. The Company did not have any policy regarding development of new estates. Non-utilisation of sale proceeds from outright sale for acquisition and development of new industrial estates led to non-achievement of objective of facilitating industrialisation in rural and backward areas.

Raw Material Support

Raw material division was formed for procurement and distribution of raw materials required for Small Scale units when there was scarcity of materials. The proportion of turnover of the Division to total turnover of the Company declined from 95 *per cent* in 1994-95 to 55.38 *per cent* in 2008-09. The Division incurred net loss during the period 2007-2011.

The sales mix of the Division during the period 2007-2011 comprised mainly wax (47.26 *per cent*), bitumen (25.95 *per cent*) and iron & steel (24.66 *per cent*). Wax and iron & steel were the only items that were in demand from the Small Industries Sector. About 38 *per cent* of the turnover of the Division was from sale to non-MSE Sector. We observed that the Division supplied raw materials to only 1.24 *per cent* of the total MSEs in Kerala and served only two industries viz. candle and iron & steel out of a total of about 747 types of small industries operating in the State. Despite incurring establishment expenditure of ₹1.50 crore (approximate) *per annum*, service rendered by the Division was minimal on the sector of the State.

[25] **Angamaly, Shornur, Moodadi and Chelakkara**
[26] **Angamaly,Shornur,Moodadi,Chelakkara,Thiruvarpu and Athani**

A detailed analysis of the items dealt with by the Division revealed the following:

Wax

Paraffin wax is the major raw material required for the candle industry and the main source of wax is Chennai Petroleum Corporation Ltd. (CPCL). After removal of quota restrictions, consumers directly procured wax from CPCL which was affordable only for larger units and based on the request of the Company, CPCL agreed (September 2008) to supply a minimum quantity of 300 MT per month based on the availability of wax to the Company for equitable distribution to units in Kerala. It was observed that of the 6000 units in Kerala, the Company could cater to the requirements of only 450 units. We further noticed that about 57 *per cent* of sale of wax by Ernakulam Depot during October 2008 to March 2012 was to three units of a single owner, a major consumer/importer/ distributor of wax. The average monthly purchase by these units was 61700 kg as against 50 to 3000 kg by any single MSE.

The Company also supplied wax to these units at concessional rate excluding employee cost and other indirect expenses. This resulted in passing on undue benefit of ₹28.90 lakh during 2008-2012.

The Company stated that the supply of wax to these units was to avoid parallel trading by them to other small units. The reply was not acceptable as the supply of wax to trading units was detrimental to the smaller units as the Company curtailed the supply to them to cater to the requirements of the trading units in full. The Company further justified the concession given to the units stating that they were also MSEs and were remitting the price in advance. The reply was not correct as the advance payment was compensated by granting special discount of ₹600 / MT.

Iron & Steel

Small Scale Industry Co-ordination and Review Committee allocates iron & steel items to Small Scale Industries Corporations for supply to MSEs as per demand raised by them and allows a rebate (for meeting handling charges) of ₹500/MT for quantity lifted so that raw materials would be delivered at the site of MSEs . In addition to this, the Company procures iron & steel items from local traders mainly to cater to the needs of State PSUs.

During 2007-2012, the Company procured only 8336.80 MT (21.33 *per cent*) out of 39092 MT offered by the manufacturers. In this connection we observed the following:

- The Company could cater to the needs of only 36 units (3.29 *per cent*) during 2009-2012 due to low demand though there was 1093 registered iron & steel units in the State.
- Trading of iron & steel items sourced from private traders increased from 629.07 MT in 2008-09 to 1101.64 MT in 2011-12 whereas sale to MSEs decreased from 3075.77 MT to 1240.33 MT (81.75 *per cent* to 48 *per cent* of total turnover) during the corresponding period. The Company

thus acted merely as a trading agent of local suppliers and not as a facilitator of Small Scale Industry.

- Sale to MSEs located in Ernakulam (of which 71.64 *per cent* of sales were to two MSEs) and Thrissur districts alone contributed to 83.59 *per cent* of the turnover during the period 2008-2011. The Company did not serve any of the units in other eight districts where they had raw material depots.
- The Company received ₹41.16 lakh during 2007-2012 towards nominal handling charges for supply of steel materials at the doorsteps of MSEs. The Company, however, neither passed on the same nor delivered the material at their site.

The Company stated that with decontrol there was free availability of raw material in the market and that it was not able to stock in bulk and sell it at competitive prices due to fund constraints. It was further stated that it was giving discount of ₹200/MT from the rebate received. We observed that this discount was passed on only from February 2012.

Bitumen

Though bitumen was not required by MSEs, sale of bitumen constituted 25.55 *per cent* of the turnover of the Division during the period 2007-2011. During the said period, the Company traded in 12827.57 MT of bitumen valued at ₹42.21 crore. The Company procured bitumen from petroleum companies[27] and supplied to Local Self Government Departments (LSGDs).The margin of the Company was the discount ranging from ₹172 to ₹1000/MT (net of loading charges) allowed by Petroleum Companies.

The Company did not take advantage of the higher discount offered by MRPL as compared to BPCL/HPCL for purchases meant for four northern districts[28] leading to loss of ₹18.40 lakh (up to January 2012).

The Company stated (August 2012) that there were restrictions to purchase from MRPL because of the preference for BPCL bitumen among customers and non-availability of trucks at Kasargod. The reply was not factually correct as the purchase from MRPL registered an increase of 816 *per cent* during 2011-12 compared to 2010-11 and contractor was engaged for transportation of bitumen all over Kerala.

The Division served only 1.24 *per cent* of the total MSEs in Kerala despite incurring huge establishment expenditure. In the post liberalisation period, availability of raw material was not a constraint for MSE Sector and hence a dedicated Division for extending raw material support to MSEs has lost relevance.

Marketing Support

Marketing support to MSEs is extended through the Marketing Division of the Company. The performance of the Division during the period 2007-2011

[27] **Bharath Petroleum Corporation Limited (BPCL), Hindustan Petroleum Corporation Limited (HPCL) and Mangalore Refinery and Petrochemicals Limited (MRPL).**

[28] **Malappuram,Kozhikode,Kannur and Wayanad.**

showed that the Division was making gross profit in the range of 8.67 *per cent* to 9.96 *per cent* and net profit in the range of 1.22 *per cent* to 2.57 *per cent*.

Product-wise analysis of turnover showed that 72 *per cent* of turnover was from supply of furniture to Government departments/PSUs based on preferential Government orders. We observed the following:

Process of selection

The Company, as and when requested by the suppliers empanelled them. Hence transparency and equity could not be ensured in the selection and listing of prospective suppliers. As a result, only three to five major large scale suppliers were benefited in each emporium of the Company.

The Company assured (August 2012) to take necessary steps to make a comprehensive vendor list.

Assistance to MSEs

The Company's marketing support was limited to furniture industry. Major purchases were made only from 178 units (7.80 *per cent*) out of 2283 furniture units registered in Kerala during 2011-12. Fifty *per cent* of the purchases of each emporium were made from three to four units showing that the Company could support only a meagre number of units. The Company is also giving marketing support to various traders to market non-MSE products deviating from its objectives.

The Company replied that steps were being taken to serve maximum MSEs.

Delay in revision of rates and payment to MSEs

The Government did not revise the rates of furniture supplied by the Company to Government Departments annually commensurate with increase in cost of raw material and labour. This resulted in the MSEs compromising the quality of items supplied. During the year 2010-11, the average payment period to MSEs was 285 days against the maximum credit period of 45 days as stipulated by MSMED Act 2006.

The Company stated that revision of rates was under consideration of the State Government and that Government had been approached for allotting revolving fund to the Company so as to provide funds to MSEs.

The Division, however, failed to extend intended support so as to ensure marketing of MSE products at reasonable price and timely payment to the units.

Conclusion

The Company, with the objective of facilitating and supporting Small Scale Industries by providing infrastructure facilities and resources so as to ensure industrial growth in the State, did not fulfill its objectives. Instead, it has diversified its activities into areas which are not related with the prime objective to serve MSEs.

The matter was reported to Government in July 2012; their reply was awaited (November 2012).

4.5 Sanction and Disbursement of Loans by Kerala Transport Development Finance Corporation Limited

Introduction

Kerala Transport Development Finance Corporation Limited (Company) was incorporated in 1991 and registered with the Reserve Bank of India (RBI) as a Non-Banking Financial Company (NBFC). The main objective is to finance Kerala State Road Transport Corporation (KSRTC) for building up commercially viable infrastructural facilities and for the purpose of acquisition of transport vehicles and machinery. The Company also disburses other category loans viz, construction, housing, vehicle and personal loans and finances BOT projects.

The Company mobilises funds mainly through cash credit from banks and deposit from public. During the five years up to March 2012, the Company disbursed ₹1377.62 crore (***Annexure 31***). The total loan outstanding as on 31 March 2012 was ₹1014.70 crore (KSRTC ₹899.11 crore, construction loan ₹95.71 crore, housing loan ₹16.94 crore, vehicle loan ₹2.90 crore and personal loan ₹0.04 crore). Thus the loan to KSRTC constituted 90.70 *per cent* of the total loan disbursed. Construction and housing loans constituted 92.71 *per cent* and 2.37 *per cent* respectively of the other loans distributed during the period of five years. Construction loans comprised loans to builders/promoters for housing projects, hotels and commercial complexes. The Company sanctioned both construction and housing loans under the Aiswarya Griha Housing Finance Scheme[29].

We analysed the appraisal, sanction, disbursement and recovery of Construction and Housing loans during the period 2007-08 to 2011-12 in Head office and Thiruvananthapuram branch.

The major findings are discussed in succeeding paragraphs:

Lack of Guidelines for Construction loans

The Company did not have codified procedure/guidelines for appraisal, sanction and disbursement of construction loan. Procedures for the loans were, however, issued in piece meal in various circulars for guidance.

The Company stated (August 2012) that it followed the guidelines of Aiswarya Griha Housing Finance Scheme for these loans also. Construction loans were sanctioned based on financial viability and credit worthiness of the applicant/company and also considered the land value.

The fact remained that the Company sanctioned/disbursed construction loans on a case to case basis. Absence of codified guidelines for construction loan led to deficiencies in sanction, disbursement and recovery as summarised below:

[29] **Housing finance scheme introduced in 2005 for purchase/construction/repairs/alteration, etc of house/flat for own/family's residential purpose.**

<table>
<tr><th>Sl. No.</th><th>Nature of failure</th><th>No. of cases</th><th>Impact</th></tr>
<tr><td>1</td><td>Failure to ensure credit worthiness</td><td>35</td><td>Loans amounting to ₹ 83.14 crore</td></tr>
<tr><td rowspan="2">2</td><td rowspan="2">Non-compliance with eligibility</td><td>1</td><td>Repayment obligation beyond 50 per cent of monthly income– ₹2 crore</td></tr>
<tr><td>3</td><td>Loan to NRI- ₹7.51 crore</td></tr>
<tr><td>3</td><td>Non-compliance with conditions of take over</td><td>2</td><td>Enhancement loan beyond maximum limit – ₹5.11 crore</td></tr>
<tr><td>4</td><td>Failure to ensure capacity, sufficient security, asset creation, etc</td><td>1</td><td>Loan of ₹20 crore</td></tr>
<tr><td>5</td><td>Non-compliance with Board decision</td><td>1</td><td>Charged fixed rate instead of floating rate– ₹5 crore</td></tr>
<tr><td>6</td><td>Disbursement of loans</td><td>7</td><td>Disbursement without ensuring initial investment and utilisation – ₹32.20 crore</td></tr>
</table>

We observed that though construction loans were sanctioned under the broad frame work of Aiswarya Griha Housing Scheme, the competent authority took various decisions involving deviation from the scheme without obtaining concurrence of the Board.

The deficiencies noticed at various stages of appraisal, sanction, disbursement, monitoring and recovery are discussed in succeeding paragraphs:

Sanction and Disbursement

Failure to ensure credit worthiness of loanee

The terms and conditions of the Aiswarya Griha Housing Finance scheme prescribe to ensure the credit worthiness of the loanee before sanctioning of the loan. We, in 35 cases amounting to ₹83.14 crore test checked, observed that the Company did not ensure the repaying capacity of the applicant. As a result, nine loans amounting to ₹7.02 crore as on 31 August 2012 were under default.

Government replied (September 2012) that loans were sanctioned after getting valuation, legal and inspection report from empanelled Engineers, Advocates and from verification agencies.

The fact was that the above mentioned loans were sanctioned without ensuring credit worthiness which ultimately resulted in default in repayment of loans. The verification agents did not consider existing liabilities of the loanees while recommending for sanction of loan in two cases (Sl no. 1 and 2 of ***Annexure 34***) and in one case (Grantech Builders) the Company did not consider the weakness pointed out by the credit appraisal agency.

Non- compliance with eligibility criteria

The terms and conditions of Aishwarya Griha Housing Finance Scheme of the Company and RBI Exchange Control Manual stipulates the eligibility criteria for sanctioning of loan. We observed non-compliance of these guidelines as detailed below:

- As per the terms and conditions, the repayment obligation (EMI) of the borrower should be restricted to 50 *per cent* of the monthly income. In an instance (Power link Builders), a construction loan of ₹2 crore with sixty EMI of ₹2.16 lakh was sanctioned (disbursed ₹1crore) in violation of the above condition considering the monthly income of ₹0.90 lakh. We observed that at the time of sanctioning the above loan, two housing loans amounting to ₹90 lakh with total EMI of ₹0.74 lakh availed by the applicants were outstanding. An amount of ₹49.78 lakh (August 2012) was under default.

- As per RBI Exchange Control Manual, loans to non-resident persons of Indian nationality/origin should not be sanctioned for investment in real estate business, dealing in land and other immovable property, for commercial purposes either singly or in association with others. The Company, contrary to the said direction sanctioned loans amounting to ₹7.51 crore to three NRIs (Sl no. 1, 2 and 4 of ***Annexure 32***). Out of these, two loans amounting to ₹84.28 lakh were in default. Of the above, a loan of ₹4.31crore was sanctioned (December 2006) to be repaid in 72 installments though the monthly salary of the applicant was ₹18 lakh with a liability of ₹6 crore. Further being a NRI, the Company was not in a position to recover salary given by foreign employer though the loan was under default.

Government stated that the loans were sanctioned based on the financial viability and credit worthiness of the applicant/company and also by considering the land value.

The reply was not correct as the sanctioning of loans to NRIs for construction of real estate/commercial purpose violated the provisions of RBI Exchange Control Manual and loans were sanctioned under Aiswarya Griha Housing Finance Scheme which was not meant for this purpose.

Non-compliance with conditions of takeover

The Company in addition to sanctioning of loan takes over loan disbursed by other financial institutions. As per the terms and conditions of Aiswarya Griha Housing Finance Scheme, the amount that can be enhanced was limited to 25 *per cent* of the takeover. If further top ups were required then it would be sanctioned at a later stage after evaluating the progress of construction. We noticed that:

- While taking over a loan of ₹1.37 crore (Paramount Studio) the Company sanctioned (July 2006) enhancement of ₹83.42 lakh (61 *per cent*) in violation of the above limit. The loanee defaulted installments amounting to ₹51.51 lakh (August 2012) besides the outstanding balance of ₹1.17 crore.
- While taking over a loan of ₹71.76 lakh (Venugopal & Bindu Venugopal) the Company sanctioned (August 2008) ₹5 crore including enhancement of ₹4.28 crore (596 *per cent*). The loanee defaulted 12 installments amounting to ₹90.87 lakh as on March 2011. Meanwhile the Company sanctioned (May 2011), an additional loan of ₹2 crore as top up and the same was disbursed by adjusting defaulted installments with penal interest (₹1 crore).

Thus the Company violated its guidelines/procedures to favour the loanees.

Government replied that there were no specific norms regarding the amount that could be sanctioned in the case of construction loan by take over from banks/ financial institutions.

The reply was not correct as the loans were sanctioned under Aishwarya Griha Housing Finance Scheme, terms and conditions of which limit the amount of enhancement to 25 *per cent.*

Failure to ensure promoter's contribution/repaying capacity

For timely completion and prompt repayment of loans the Company should ensure the repaying capacity of the loanee and the prescribed promoter's contribution (10 to 20 *per cent* of the project cost) before releasing the loan amount. Further, adequate security to alleviate risk for the loan amount has also to be obtained. The Company sanctioned (April / October 2010) two loans of ₹10 crore each for construction of residential villa – Green city phase I and II to Grandtech Builders and Developers Pvt Ltd (represented through its Directors), a company with a share capital of only ₹21.58 lakh. However, the amount disbursed in second loan was ₹4 crore. We noticed that:

- The Managing Director was empowered to sanction loan upto ₹10 crore only. The MD, however, sanctioned two loans of ₹10 crore each within a period of 6 months to the same firm to keep it within the delegated power;
- The credit worthiness and repaying capacity of the borrower was uncertain as the firm was newly incorporated and promoters had no previous experience in construction field;
- Land offered as security for the loan was reckoned (March 2010) at an inflated value of ₹3.64 crore as against the purchase (February 2010) cost of ₹28.50 lakh;
- The loan carried an EMI of ₹48.01 lakh; whereas the monthly income of the applicants was left blank. However, the first applicant in his personal details had shown an annual income of ₹6 lakh;
- The Company released first installment of ₹5 crore on 8 April 2010 though the land offered as security was valued at ₹3.64 crore only. The subsequent installments were released (₹2 crore on 27 May 2010 and ₹3 crore on 28 June 2010) within a gap of two months without ascertaining asset creation corresponding to the previous disbursements;
- For releasing subsequent installments, asset created out of previous disbursement were reckoned as security. The Company on inspection found that construction valuing ₹9.20 crore (March 2012) was completed as against the total cost of construction of ₹17.22 crore. Thus the loan was left without adequate security.
- The Company sanctioned (15 October 2010) another loan of ₹10 crore to the same borrower at a time when the third installment (due on 05 October 2010) of the previous loan was under default and released (15 October 2010) ₹2 crore as first installment. The borrower utilised a portion of the amount for remitting the third overdue installment of ₹48.01 lakh with penal charges of the first loan. The second installment (₹2 crore) was released on 26 October 2010 after a period of 10 days without ensuring utilisation of the first installment for asset creation. The project was yet to commence.
- The borrower defaulted repayment from thirteenth installment (August

2011) onwards. Total overdue amount was ₹3.15 crore (August 2012) besides outstanding loan amount of ₹5.21 crore.

Government stated that the loans were sanctioned based on the recommendations in report of the credit appraisal agency. Further, the Company considered the loans as two different loans since these were sanctioned on the mortgage of two different properties.

The reply was not factual as the recommendation of the credit appraiser was subject to valuation of property. Further, it was clearly mentioned as weakness in the appraisal report that the company was a new one and it was their first project. The second loan was sanctioned within a period of six months without ensuring the utilisation and prompt repayment of the loan disbursed earlier.

Sanctioning of loans at interest rate below cost of borrowings

For the profitable operation of the Company the rate of interest on loans should be fixed with a margin over the cost of borrowings. During the year 2005-06, the cost of borrowings of the Company was 9.99 *per cent*. The Company, however, reduced (w.e.f 16 January 2006) the interest rate for housing loans by 0.75 *per cent* as discussed below. Subsequently, after four months the Company decided (09 May 2006) to restore the original rate w.e.f 16 May 2006 and to allow the pre-revised rate for all loans sanctioned till 15 May 2006 including those pending disbursements.

We observed that:

- The Company sanctioned 68 loans at the reduced rate of interest during the above four months period.
- Of the above, 38 loans amounting to ₹2.57 crore were sanctioned during 9 to 16 May 2006 without complying with necessary formalities. As the rate of interest during this period was fixed, it resulted in estimated revenue loss of ₹21.72 lakh (sl no.1 to 10 of ***Annexure 33***) in ten cases test checked.
- Out of the above, in seven loans amounting to ₹50.50 lakh, the date of sanction of loan was seen corrected as 15 May 2006.
- Though the higher rate was applicable w.e.f 16 May 2006, the Company sanctioned four loans amounting to ₹0.38 crore during 16 to 23 May 2006 at pre-revised rates resulting in forgone revenue of ₹4.54 lakh (sl no.11 to 14 of ***Annexure 33***).
- The Company sanctioned loans (₹60 lakh and ₹30 lakh) to the Managing partners of canvassing and verification agents (M/s Power link and M/s H-Work net) based on their own verification report.
- Out of 42 loans disbursed as above, two loans amounting to ₹45.53 lakh were defaulted.

Government, in their reply stated that they had charged the rate of interest as per the direction of the Board.

Non-compliance of Board Decisions

The Board decided to charge floating rate of interest for all construction and project loans w.e.f 4 July 2008. The Company, while sanctioning (16 May 2011) top up loan of ₹2 crore to Venugopal and Bindu Venugopal changed interest rate of first loan (₹5 crore sanctioned on 8 August 2008) from floating rate to fixed for three years and then floating rate resulting in benefit of ₹29.54 lakh to the loanee.

Government while admitting this as a mistake, stated that the interest was being reworked and loanee being intimated to remit the balance amount.

Disbursement of Loans

To safeguard the interest of the Company and to weed out non-serious promoters, the terms and conditions stipulates disbursement of 30 *per cent* of the loan on executing necessary documents including creation of mortgage and after the borrower has expended 30 *per cent* of his share (margin) in the construction. The Company, however, disbursed to seven loanees the initial installment (₹7.04 crore) without ensuring the investment of 30 *per cent* share and subsequent installments (₹25.16 crore) before utilisation of the amount already disbursed (Sl no.2 to 8 of ***Annexure 32)***.

Government replied that construction loans were released in installments based on nature of projects and conditions of normal housing loans were not applicable to construction loans.

The reply was not acceptable as the Company had not formulated any separate rules for construction loans.

Monitoring

Post disbursement monitoring is of vital importance for ensuring utilisation of loan for the purpose for which it was sanctioned and the project was progressing as per schedule. We observed that:

- The Company did not have any institutionalised mechanism for post disbursement monitoring of the progress (physical and financial) achieved. Hence the Company also could not ensure promoters contribution and asset creation before release of subsequent installments as already mentioned.
- As per special condition (a) of Annexure H to agreement, the collateral/ additional securities should not be released during the currency of loan. During 2008-09 the Company, however, in a case as per the request of loanee released the collateral security of 19 cents of land valued at ₹1.71 crore leaving only a security of 17 cents valuing ₹1.36 crore.

Government replied that the collateral security was released considering the completion of the project and its present value of ₹10 crore. This, however, was in violation of the terms and conditions of the agreement.

Recovery

Recovery of loan as per repayment schedule is essential to safeguard the financial interest of the Company. Slackness in recovery may lead to increased dependence on borrowings for disbursement of fresh loans. We, however, noticed that:

- The Company delayed the preparation and communication of the repayment schedule to loanee. Further post dated cheques collected to ensure prompt repayment were not presented for collection. This resulted in non-recovery of ₹0.94 crore in respect of two loans (Sl. no. 1 and 2 of ***Annexure 34***).

- The Company did not revise the interest rates for construction and housing loans in accordance with the loan agreement and Board decision despite the acceptance by the borrowers resulting in revenue loss of ₹0.31crore to the Company in respect of three loans (Sl. no.1, 4 and 5 of ***Annexure 34***).
- The Company released (January 2008) the mortgage created in respect of two loanees, valuing ₹3.99 crore, enabling them to sell the 49 built-up apartments/villas in two projects test checked. We observed that the Company, however, did not recover the proportionate loan amount of ₹0.56 crore (sl no. 2 and 3 of ***Annexure 34***) in respect of these apartments/villas before releasing the mortgage to safeguard its interest. Both the loans amounting to ₹3.65 crore were under default.

  Further, the Company did not obtain title deed of the mortgaged property from one of the above loanees. This enabled the loanee to sell 18 as against 11 apartments for which the Company had issued No Objection Certificate. The value of the seven apartments thus sold by the loanee without obtaining NOC amounted to ₹0.61crore.

Government replied that the repayment schedule was not forwarded to the loanee in time mainly due to inadequate skilled staff in the Branch office and that the interest on loans was charged as per Board decision.

The reply indicated that the internal control and monitoring mechanism was poor. Further there was no rationale behind Board's wavering decision for charging the interest which would ultimately result in loss of revenue to the Company.

Government further stated that necessary directions had been given to the MD to take urgent action for avoiding the shortcomings in future and to initiate recovery action in cases of default.

4.6 Kerala State Electronics Development Corporation Limited

Avoidable expenditure on penal charges

Failure of the Company in regularising the Unauthorised Additional Load and subsequent delay in conversion to HT connection resulted in avoidable penalty of ₹0.53 crore.

The Corporate office of Kerala State Electronics Development Corporation Limited (Company) was having a LT connection from Kerala State Electricity Board (KSEB) with connected load of 16 KW for meeting its power requirements. The Company ventured (1999) into software field by setting up an Information Technology Business Group (ITBG) in the premises of its Corporate office. With the expansion in operations over the years, new buildings were constructed and new electrical equipments were installed which led to increased power requirement and consumption.

The Company, without enhancing the connected load as per Rules[30], continued to draw power with the existing connected load. KSEB officials inspected (April 2009) the premises and detected Unauthorised Additional Load (UAL) to the extent of 189 KW and levied (April 2009) penalty of ₹14.16 lakh with direction to regularise the UAL. But the Company obtained the High Tension connection only in April 2012 and as such KSEB continued to levy penalty up to March 2012. The inaction of the Company to enhance the connected load commensurate with increase in business requirements or to regularise the UAL immediately on its detection resulted in avoidable expenditure of ₹0.53 crore ***(Annexure 35)*** towards penal charges during the period from April 2008 to March 2012.

The Government stated (November 2012) that the increase in connected electrical load came into notice only in 2009 when KSEB pointed out the usage of UAL and though action was initiated to set up substation it could be commissioned only in April 2012 due to various technical reasons and procedures involved.

The reply is not acceptable since the Company was bound to comply with the Rules and terms and conditions of KSEB and inaction of the Company for three years after detection of UAL in regularising the load resulted in penal charges of ₹0.53 crore.

4.7 The State Farming Corporation of Kerala Limited

Avoidable expenditure on interest

Failure to adhere to the provisions of Agricultural Income Tax Act resulted in avoidable expenditure on interest of ₹2.64 crore.

The State Farming Corporation of Kerala Limited (Company) is a profit making Public Sector Undertaking (PSU) engaged in farming activities and is an assessee under the Kerala Agriculture Income Tax (AIT) Act. Government of Kerala exempted (February 1994) the Company for six years (1992-93 to 1997-98) from paying AIT for providing financial assistance to Trivandrum Rubber Works Limited (TRW), a loss making PSU engaged in the manufacture of rubber based products. The Company transferred fund and material to TRW from 1993-94 onwards and this continued beyond March 1998 (up to 2007-08) to meet the working capital requirements and payment of salaries to employees.

Although the Company was liable to pay AIT from 1997-98, the Company did not have AIT liability[31] for six years (up to 2003-04). Though the Company was

[30] As per Clause 51 of the Kerala State Electricity Board Terms and Conditions of Supply, 2005, where a Low Tension (LT) consumer exceeds the connected load and/ or resorts to UAL and if the connected load exceeds 100 KVA, the UAL shall be disconnected by the consumer within twenty four hours of detection by the Board's Officers or take action to regularise the UAL. If the consumer fails to disconnect or regularise the additional load, penalty shall be levied at a rate equal to twice the tariff applicable (Section 126 of Electricity Amendment Act, 2007) for the entire period of unauthorised usage and if the period cannot be determined, for a period of 12 months immediately preceding the date of detection of UAL. The penalty for UAL shall be levied till the said UAL is either removed or regularised as per Rules.

[31] either on account of no profit from agricultural activities or due to set off of carry forward losses

liable[32] to self assess the tax and furnish returns and pay advance tax before the end of February each year, the Company belatedly filed returns for the years 2002-03 to 2007-08 (six years) and remitted ₹12.67 crore towards self assessed AIT only in February/March 2008 and October/November 2009. The details are as follows:

Sl. No.	Period (FY)	No of years	Self Assessed AIT liability (Admitted Tax) (₹)	Amount of Admitted tax paid (₹)	Interest adjusted by the Dept. for delay (₹)
1	1993-94 to 1997-98	5	Exempted	Nil	Nil
2	1998-99 to 2001-02	4	No profit from agricultural activity. Hence no AIT	Nil	Nil
3	2002-03 to 2003-04	2	Started making taxable income, but no AIT liability on account of set off of carry forward losses	Nil	Nil
4	2004-05 to 2007-08	4	126711438 (8715385+34866367+39357450+43772236) (paid in Feb/Mar 2008 and Oct/Nov 2009)	126711438	26412641

The Assistant Commissioner, Commercial Taxes Department finally assessed the AIT (August/October 2011) as ₹14.10 crore and an interest of ₹2.64 crore was charged.

The Company replied (July 2012) that the delay in payment of AIT occurred since the request for exemption was pending before Government in view of continued fund transfer to TRW. They also stated that the interest received from fixed deposits was ₹1.37 crore.

The reply is not acceptable since the Company was aware of the fact that the benefit of exemption (₹17.73 crore) available from payment of AIT up to 1997-98 was far in excess of the financial assistance (₹13.30 crore up to 2004-05) to TRW. The Company should have adhered to the provisions of AIT and filed the returns timely. This could have avoided the payment of interest of ₹2.64 crore on account of the AIT liability.

The matter was reported (July 2012) to Government; their reply was awaited (November 2012).

Statutory Corporation

4.8 Kerala State Road Transport Corporation

Avoidable expenditure

Failure to place orders for purchase of chassis within the validity period resulted in extra expenditure of ₹8.12 crore in subsequent purchase at higher rates.

In the Budget speech for the year 2008-09, the Finance Minister had announced that Kerala State Road Transport Corporation (Corporation) would commission

[32] **Section 37 of the Kerala Agricultural Income Tax Act, 1991 provides that every person liable to furnish a return under Section 35 of the Act, shall pay tax for the previous year on or before the end of February of the previous year. Any person who fails to pay the tax shall pay simple interest at the rate of 12 *per cent* per annum for every month of delay or part thereof on the unpaid amount of tax (Section 37(4)).**

1000 buses every year. As part of implementing this policy of introducing 1000 buses each year, the Corporation invited (November 2009) open tenders for purchase of 1000 bus chassis (280 numbers conforming to BS II and 716 nos conforming BS III and 4 nos fully built buses). Ashok Leyland and Tata Motors participated in the tender and quoted their rates (December 2009) for different variants, which was valid for one year from the date of offer ie. upto 08 December 2010.

The Board of Directors (BoD) of the Corporation decided (January 2010) to restrict the initial procurement of BS III variant to 20 (10 electronic and 10 mechanical each) on an experimental basis. The shortage in BS III chassis was proposed to be covered up by procurement of additional BS II chassis. During the period January 2010 to June 2010 out of the tendered quantity of 1000 chassis, the Corporation placed orders for 723[33] chassis.

We observed that the purchase of BS III chassis was done on experimental basis in order to evaluate the performance of its mechanical and electronic versions and also in accordance with the restrictions as per the date of implementation of BS III norms on 01 August 2010. Besides, there was delay in evaluating the performance of these chassis consequent to delayed delivery by the respective suppliers. The Technical Evaluation Committee, however, submitted their performance report on 30 November 2010. The Board considered to procure the balance 277 chassis on 10 December 2010 ie. after the validity period of offers. The suppliers turned down the request to supply at the earlier quoted rate of ₹7.27 lakh on grounds of expiry of validity period of the offer.

Hence, the Corporation invited fresh tenders for 500 BS III chassis (both mechanical and electronic) and orders were placed (September 2011) for supply of chassis (mechanical) with Ashok Leyland (300 numbers) and Tata Motors (200 numbers) @ ₹10.20 lakh. Thus, the failure to place purchase order within the validity period of offer led to subsequent purchase at higher rate involving extra expenditure of ₹8.12 crore [(₹1020000 – ₹726729) x 277)] on the balance 277 chassis.

The Government replied (September 2012) that though the Corporation indented for 1000 chassis in 2009-10, it required only 723 chassis to cater to its necessities. It was also added that since the purchases were arranged from loans availed, its repayment was an additional burden as there was no appreciable development in the revenue side.

The reply is not acceptable as the decision to procure 1000 chassis every year was part of package for renovation and restructuring of the Corporation with a view to improve its performance, expected improvement in mileage and consequent significant reduction in the annual expenditure. The Board, however, did not decide to procure the balance 277 BS III chassis within the validity period.

[33] **700 BS II, 20 BS III, 3 fully built.**

General

Follow-up action on Audit Reports

Explanatory notes[34] outstanding

4.9 The Audit Reports of the CAG represent the culmination of the process of scrutiny starting with initial inspection of accounts and records maintained in various Government companies and Statutory corporations. It is, 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 performance audits 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 2010-11 had been presented to the State Legislature but eight departments did not furnish explanatory notes on 29 out of 172 paragraphs / performance audits relating to the Audit Reports for the year 2004-05 to 2010-11 as of September 2012.

Compliance to Reports of Committee on Public Undertakings outstanding

4.10 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 258 paragraphs pertaining to 60 Reports of the CoPU presented to the State Legislature between July 2000 and July 2011 had not been received as of September 2012 as shown below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where ATNs not received
1998-2000	2	16
2001	1	4
2001-2004	5	22
2004-2006	12	37
2006-2008	16	69
2008-2011	24	112
Total	**60**	**258**

Response to Inspection Reports, Draft Paragraphs and Performance Audit Reports

4.11 Audit observations made during audit and not settled on the spot are communicated to the heads of the PSUs and the Departments of the State Government concerned through Inspection Reports (IRs).The heads of PSUs

[34] **Explanatory notes refer to the explanations furnished by Administrative Departments to the Legislature Secretariat, on performance audit / paragraphs contained in Audit Reports placed before the Legislature.**

were required to furnish replies to the IRs through the respective heads of Departments within a period of six weeks. IRs issued up to March 2012 pertaining to 86 PSUs disclosed that 2792 paragraphs relating to 525 IRs remained outstanding at the end of September 2012. Of these, 51 IRs containing 453 paragraphs had not been replied to for one to four years. Department-wise break up of IRs and paragraphs outstanding as on 30 September 2012 is given in ***Annexure 36.***

Similarly Draft Paragraphs and Reports on Performance Audit 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 Performance Audit Report forwarded to various Departments during July-August 2012 as detailed in ***Annexure 37*** had not been replied to so far (November 2012).

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/ Performance Audit Reports 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.

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Countersigned

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