

CHAPTER – IV
REVENUE SECTOR

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REVENUE SECTOR

4.1 General

4.1.1 Trend of revenue receipts

The Tax and Non-tax revenue raised by Government of Nagaland (GoN) during the year 2015-16, the State's share of net proceeds of divisible Union taxes and Grant-in-aid received from the Government of India (GoI) during the year and the corresponding figures for the preceding four years are mentioned below:

Table-4.1.1

₹ in crore

Sl. No.	Particulars	2011-12	2012-13	2013-14	2014-15	2015-16
I	Revenue raised by the State Government					
	• Tax revenue	303.88	339.95	333.39	388.60	427.10
	• Non-tax revenue	232.95	207.17	216.57	270.61	256.39
	Total-I	536.83	547.12	549.96	659.21	683.49
	Percentage of increase over previous year	30.79	1.92	0.52	19.86	3.68
II	Receipt from the Government of India					
	• States share of net proceeds of divisible Union taxes	803.20	917.14	1,001.27	1,062.69	2,540.72
	• Grants-in-aid	4,246.35	4,740.03	4,946.67	5,929.04	4,819.36
	Total-II	5,049.55	5,657.17	5,947.94	6,991.73	7,360.08
III	Total receipts of the State Government (I+II)	5,586.38	6,204.29	6,497.90	7,650.94	8,043.57
	Percentage of I to III	10	9	8	9	8

Thus, growth of revenue during 2015-16 over previous year was at 3.68 *per cent* against 19.86 *per cent* in the year 2014-15. Further, during the year 2015-16, the revenue raised by the State Government (₹ 683.49 crore) was eight *per cent* of the total revenue receipts against nine *per cent* in the preceding year. The balance 92 *per cent* of receipts during 2015-16 was from GoI.

4.1.2 The following table presents the details of Tax revenue raised during the period 2011-12 to 2015-16.

Table-4.1.2

							<i>₹ in crore</i>
Sl. No.	Head of revenue	2011-12	2012-13	2013-14	2014-15	2015-16	Percentage of increase (+) or decrease (-) in 2015-16 over 2014-15
1	Sales Tax/VAT	231.12	257.21	250.20	294.29	328.58	(+)12
2	State Excise	3.36	3.73	4.86	4.70	5.12	(+)09
3	Stamps and Registration Fees	1.85	1.58	1.77	1.93	2.04	(+)06
4	Taxes and duties on Electricity	0.04	0.05	0.04	0.03	0.06	(+)100
5	Taxes on vehicle	34.58	41.59	36.15	46.46	53.09	(+)14
6	Taxes on Goods and Passengers	4.85	6.71	10.79	9.73	5.88	(-)40
7	Other taxes on Income and expenditure	27.03	27.22	28.30	27.95	29.65	(+)06
8	Other taxes and duties on Commodities and Services	0.37	1.14	0.58	2.77	1.93	(-)30
9	Land Revenue	0.68	0.72	0.70	0.74	0.75	(+)01
	Total	303.88	339.95	333.39	388.60	427.10	(+)10

The reasons for variations over the previous year were not reported by the departments though called for.

4.1.3 The following table presents the details of Non-tax revenue raised during the period from 2011-12 to 2015-16.

Table-4.1.3

							<i>₹ in crore</i>
Sl. No.	Head of revenue	2011-12	2012-13	2013-14	2014-15	2015-16	Percentage of increase (+) or decrease (-) in 2015-16 over 2014-15
1	Interest Receipts	9.62	5.90	7.62	7.23	5.19	(-)28
2	Housing	4.38	5.12	5.13	5.01	5.36	(+)07
3	Water Supply & Sanitation	1.62	1.74	1.95	1.95	2.43	(+)25
4	Forestry and Wildlife	8.87	7.76	8.81	9.68	8.80	(-)09
5	Education, Sports, Art and Culture	12.16	45.57	67.83	103.56	76.52	(-)26
6	Miscellaneous General Services	29.01	6.60	6.57	13.08	13.43	(+)03
7	Power	94.28	102.83	88.31	98.91	111.10	(+)12
8	Medical & Public Health	0.21	0.35	0.55	0.52	0.59	(+)13
9	Co-operation	3.54	1.13	2.45	0.98	0.18	(-)82
10	Public Works	0.69	0.18	0.40	0.11	0.23	(+)109
11	Police	30.65	7.34	3.37	1.45	1.68	(+)16
12	Other Administrative Services	2.38	3.22	2.73	4.03	2.55	(-)37
13	Crop Husbandry	0.20	0.16	0.27	0.10	0.08	(-)20
14	Others	35.34	19.27	20.58	24.00	28.25	(+)18
	Total	232.95	207.17	216.57	270.61	256.39	(-)05

The reasons for variations over the previous year were not stated by the departments (December 2016).

4.1.4 Variation between the budget estimates and actuals

The variation between the budget estimates and actuals of revenue receipts under the principal heads of Tax and Non-tax revenue for the year 2015-16 are mentioned in the following table:

Table-4.1.4

Sl. No.	Head of revenue	Budget estimates (₹ in crore)	Actual receipts (₹ in crore)	Variation increase (+) decrease (-)	Percentage of variation
Tax Revenue					
1	Sales Tax/VAT	332.78	328.58	(-)4.20	(-)01
2	State Excise	4.90	5.12	0.22	04
3	Stamps and Registration fees	1.98	2.04	0.06	03
4	Taxes on vehicles	46.00	53.09	7.09	15
5	Taxes on Goods and Passengers	12.10	5.88	(-)6.22	(-)51
6	Land revenue	0.89	0.75	(-)0.14	(-)16
Non-tax Revenue					
7	Interest Receipts	4.40	5.19	0.79	18
8	Other Administrative Service	3.00	2.55	(-)0.45	(-)15
9	Medical & Public Health	0.62	0.59	(-)0.03	(-)05
10	Public Works	0.88	0.23	(-)0.65	(-)74
11	Forestry & Wildlife	14.37	8.80	(-)5.57	(-)39
12	Education, Sports, Art and Culture	40.21	76.52	36.31	90
13	Power	100.00	111.10	11.10	11.10

Source: Budget document and Finance Account for the year 2015-16.

The reasons for variations over the previous year were not stated by the departments (December 2016).

4.1.5 Analysis of arrears of revenue

The arrears of revenue as on 31 March 2016 in respect of principal Heads of Revenue as reported by the departments was ₹ 9.78 crore of which ₹ 2.44 crore (24.95 per cent) was outstanding for more than five years as per details mentioned in the following table:

Table-4.1.5

Sl. No.	Head of Revenue	Amount outstanding as on 31 March 2016	Amount outstanding for more than five years
1	Taxes/ VAT on Sales, Trades etc.	9.78	2.44

₹ in crore

4.1.6 Arrears in assessment

The details of Sales Tax/VAT assessment cases pending at the beginning of the year 2015-16, cases which were due for assessment during the year, cases disposed of

during the year and number of cases pending at the end of the year 2015-16 as furnished by Commissioner of Taxes are mentioned in the following table:

Table-4.1.6

Head of Revenue	Opening Balance as on 1st April 2015	New cases due for assessment during 2015-16	Total assessment due	Cases disposed of during 2015-16	Balance at the end of the 31st March 2016	Percentage of cases disposed to the total assessment due
1	2	3	4	5	6	7 (5 to 4)
Taxes /VAT on Sales, Trades etc.	1,833 ¹	8,997	10,830	5,004	5,826	46

The arrear in assessment increased from 1833 to 5826 cases with the addition of another 8997 cases which became due for assessment during the year 2015-16 and 5004 cases got disposed during the year. The percentage (46) of cases disposed during the year was lesser than the previous year (60 *per cent*) which needs to be improved.

4.1.7 Response of the Departments/Government towards audit

The Accountant General (Audit), Nagaland conducts periodical inspection of the Government Departments to test check the transactions and verify the maintenance of important accounts and other records as prescribed in the rules and procedures. These inspections are followed up with the IRs incorporating irregularities detected during the inspection and not settled on the spot, which are issued to the Heads of the Offices inspected with copies to the next higher authorities for taking prompt corrective action. The Heads of the Offices/Government are required to promptly comply with the observations contained in the IRs, rectify the defects and omissions and report compliance through initial reply to the Accountant General (Audit) within one month from the date of issue of the IRs. Serious financial irregularities are reported to the Heads of the Departments and the Government.

IRs issued upto June 2016 disclosed that 228 Paragraphs involving ₹ 73.37 crore relating to 76 IRs remained outstanding as mentioned in the following table along with the corresponding figures for the preceding two years.

Table-4.1.7

	June 2014	June 2015	June 2016
Number of outstanding IRs	94	74	76
Number of outstanding audit observations	352	226	228
Amount involved (₹ in crore)	82.58	50.62	73.37

The Department-wise details of the IRs and audit observations outstanding as on 30 June 2016 and the amount involved are mentioned in the following table:

¹ Opening balance taken as per the revised figure furnished by the Department.

Table-4.1.8

Sl. No.	Name of Department	Name of Receipts	No. of outstanding IRs	No. of Outstanding Audit Observations	Money Value involved (₹ in crore)
1.	Finance	Taxes/VAT on Sales, Trade etc	30	137	65.42
2.	Finance	Miscellaneous General Services/Lottery	03	16	2.59
3.	Transport	Taxes on Vehicles/ Taxes on Goods & Passengers	25	48	4.21
4.	Forest & Environment	Forest & Wildlife	18	27	1.15
Total			76	228	73.37

In respect of four IRs, even the first reply was not received which was required to be received within one month from the date of issue of the IRs (December 2016). This large pendency of IRs due to non-receipt of replies is indicative of the fact that the Heads of offices and Heads of departments failed to initiate action to rectify the defects, omissions and irregularities pointed out by the Accountant General in the IRs.

It is recommended that the Government takes suitable steps to install an effective procedure for prompt and appropriate response to audit observations within prescribed time schedules and also to take action to recover loss/outstanding demand in a time bound manner.

4.1.7.1 Departmental Audit Committee Meetings

In order to expedite settlement of the outstanding audit observations contained in the IRs, Departmental Audit Committees are constituted by the Government. These Committees are chaired by the Secretaries of the concerned Administrative Department and attended by the concerned officers of the State Government and officers of the Accountant General (Audit). The Audit Committees need to meet regularly in order to expedite clearance of the outstanding audit observations.

During 2015-16, no Audit Committee meeting was convened to clear the outstanding audit observations.

The Government may ensure holding of frequent meetings of these committees for ensuring effective action on the audit observations leading to their settlement.

4.1.7.2 Response of the Departments to the draft audit paragraphs

The draft audit paragraphs proposed for inclusion in the Report of the C&AG of India are forwarded by the Accountant General (Audit) to the Principal Secretaries/Secretaries of the concerned departments, drawing their attention to audit findings and requesting them to send their response within six weeks.

The fact of non-receipt of the replies from the departments/Government is invariably indicated at the end of such paragraphs included in the Audit Report.

Three draft paragraphs were sent to the Principal Secretaries/Secretaries of the respective departments by name during August 2016. The Principal Secretaries/Secretaries furnished replies (November 2016) in respect of two draft paragraphs which has been suitably incorporated.

4.1.7 3 Follow up on Audit reports - summarised position

The internal working system of the Public Accounts Committee (PAC), notified in December 2002, laid down that after the presentation of the Report of the Comptroller and Auditor General of India in the Legislative Assembly, the Departments shall initiate action on the audit paragraphs and the action taken explanatory notes thereon should be submitted by the Government within three months of tabling the Report, for consideration of the Committee.

However, *suo-moto* explanatory notes were not furnished to Accountant General (Audit) by the departments and were also not received through Nagaland Legislative Assembly Secretariat in respect of paragraphs/reviews appeared in the Audit Reports. Hence, status on delay of submission of explanatory notes cannot be commented upon.

During 2015-16, one PAC meeting was held and no Action Taken Notes were received.

4.1.7 4 Compliance with the earlier Audit Reports

In the Audit Reports 2009-10 to 2014-15, cases of under assessments, evasion/non/short levy of taxes/penalty, loss of revenue, failure to raise demands etc., involving ₹ 19.72 crore were reported. As of March 2016, the departments concerned have accepted observations of ₹ 2.24 crore and recovered ₹ 0.33 crore which was 14.73 per cent of accepted money value. Audit Report wise details of cases accepted and recovered are given in the following table:

Table-4.1.9

₹ in crore

Year of Audit Report	Total Money Value	Accepted money value	Recovery made
2009-10	0.23	0.16	0.16
2010-11	7.99	0.43	0.00
2011-12	0.20	0.00	0.00
2012-13	1.20	0.17	0.17
2013-14	8.46	1.23	0.00
2014-15	1.64	0.25	0.00
Total	19.72	2.24	0.33

4.1.8 Analysis of mechanism for dealing with the issues raised by Audit

In order to analyse the system of addressing the issues highlighted in the IRs/Audit Reports by the Department/Government the action taken on the paragraphs and Performance Audits included in the Audit Reports of the last five years in respect of one Department is evaluated and included in each Audit Report.

The succeeding paragraphs 4.1.8 (a) and 4.1.8 (b) discuss the performance of Taxation Department in dealing with the cases detected in the course of local audit conducted during the last ten years and also the cases included in the Audit Reports for the years 2005-06 to 2014-15.

4.1.8 (a) Position of Inspection Reports (IRs)

A summarised position of IRs issued during the last ten years, paragraphs included in these Reports and their status as on 30 June 2016 are given in the following table:

Table-4.1.10

₹ in crore

Year	Opening Balance			Addition during the year			Clearance during the year			Closing Balance		
	IRs	Paras	Money Value	IRs	Paras	Money Value	IRs	Paras	Money Value	IRs	Paras	Money Value
2005-06	20	45	10.01	-	-	-	-	-	-	20	45	10.01
2006-07	20	45	10.01	-	-	-	-	-	-	20	45	10.01
2007-08	20	45	10.01	-	-	-	0	6	11	20	39	9.90
2008-09	20	39	9.90	-	-	-	0	5	0.01	20	34	9.89
2009-10	20	34	9.89	1	1	0.06	-	-	-	21	35	9.95
2010-11	21	35	9.95	-	-	-	1	2	0.03	20	33	9.92
2011-12	20	33	9.92	2	21	9.87	-	-	-	22	54	19.79
2012-13	22	54	19.79	1	3	0.77	-	-	-	23	57	20.56
2013-14	23	57	20.56	1	7	1.00	-	-	-	24	64	21.56
2014-15	24	64	21.56	1	20	21.30	0	11	6.64	25	73	36.22
2015-16 Up to 06/2016	25	73	36.22	1	22	26.44	0	0	0.80	26	95	61.86

Audit reminded the Department periodically to furnish the replies to the outstanding audit observations.

4.1.8 (b) Assurances given by the Departments/Government on the issues highlighted in the Audit Reports

4.1.8 (b) (i) Recovery of accepted cases

The position of paragraphs included in the Audit Reports of the last five years and those accepted by the departments and the amount recovered are mentioned in the following table:

Table-4.1.11

Year of Audit Report	Paragraphs included		Paragraphs accepted		Amount recovered (₹ in crore)	Cumulative position of recovery of accepted cases
	Number	Money value (₹ in crore)	Number	Money value(₹ in crore)		
2010-11	-	-	-	-	-	-
2011-12	1	0.20	-	-	-	-
2012-13	2	0.53	2	0.17	0.17	0.17
2013-14	2	8.46	-	-	-	-
2014-15	3	1.64	3	0.25	-	-
Total	8	10.83	5	0.42	0.17	0.17

From the above table, it is seen that during the last five years, an amount of ₹ 0.42 crore was accepted and ₹ 0.17 crore was recovered by the Department.

4.1.8 (b) (ii) Action taken on the recommendations accepted by the Departments/ Government

The draft Performance Audit (PAs) conducted by the Accountant General (Audit) are forwarded to the concerned Departments/Government for their information with a request to furnish their replies. These PAs are also discussed in the exit conference and the Department's/Government's views are included while finalising the PAs for the Audit Reports.

During the period 2010-11 to 2014-15, one Performance Audit i.e. "Utilisation of declaration of forms in Inter State Trade" on the Finance (Taxation) Department featured in the Report of the Comptroller and Auditor General of India for the year ended 31 March 2011. Five recommendations were made by Audit for consideration by the Government. The report was discussed by the Public Accounts Committee (PAC) of the State Legislative Assembly, however, neither the Action Taken Notes of the Department nor the recommendations of the PAC had been received.

4.1.9 Audit Planning

The unit offices under various departments are categorized into high, medium and low risk units according to their revenue position, past trends of audit observations and other parameters. The annual audit plan is prepared on the basis of risk analysis, which *inter alia* include critical issues in Government revenues and tax administration *i.e.* budget speech, reports of the Finance Commission (State and Central), statistical analysis of the revenue earnings during the past five years, features of the tax administration, audit coverage and its impact during the past five years *etc.*

During the year 2015-16, there were 75 auditable units, of which 14 units were planned and 12 units had been audited, which is 16 *per cent* of the total auditable units.

4.1.10 Results of Audit

4.1.10 (a) Position of local audit conducted during the year

Test check of the records of 6 units of Transport and Finance (Taxes) departments conducted during the year 2015-16 revealed under assessment/short levy/loss of revenue/non-realisation of outstanding revenue aggregating ₹ 27.43 crore in 53 cases.

4.1.10 (b) Coverage of this Report

This Report contains findings on Performance Audits of 'Nagaland State Lotteries' and 'Computerisation of Motor Vehicles Department' and three compliance audit paragraphs involving financial effect of ₹ 10.48 crore. The audit findings are discussed in succeeding paragraphs.

Performance Audit

FINANCE DEPARTMENT/DIRECTORATE OF LOTTERIES

4.2 Nagaland State Lotteries

4.2.1 Introduction:

Lottery means a scheme for raising money for Government, charity etc., in which tickets are sold and draw is held for distribution of prizes by lot or chance to those persons who participated in it by purchasing tickets. Lotteries organised by Government of India or the Government of a State is a Union subject². However, the tax on sale of such lotteries is a State subject.

In order to regulate conduct of lottery, Government of India (GoI) enacted the Lotteries (Regulation) Act, 1998. In April 2010, GoI enacted Lotteries (Regulation) Rules 2010, which provides for organisation of lottery, appointment of distributor or selling agent and procedure to prohibit the sale of lottery tickets by the Central Government. The Government of Nagaland notified the rules framed by the Central Government in its official Gazette on 02 June 2010 outlining the purpose, scope, limitation and methods for conducting of lotteries.

Highlights:

The selection of distributor for conducting of lotteries was not transparent which led to a court case. Further, instead of sale proceeds as per the Rules the distributor had to pay a Minimum Guaranteed Revenue.

(Paragraph 4.2.10)

Against the total sale proceeds of ₹ 17,653.76 crore the share of the State Government in the form of MGR was only ₹ 56.93 crore (1.24 per cent) of the total

² Entry 40 of the List I – Union list in the Seventh Schedule to the Constitution of India

sale proceeds whereas the distributor's share was ₹ 4522.24 crore (98.67 per cent) during 2010-11 to 2015-16.

(Paragraph 4.2.11)

As unsold tickets were not identified and segregated, the possibility of an unsold ticket (lying with the distributor) winning a draw was high. This was especially true of Online lotteries.

(Paragraph 4.2.13.1)

Location of Central Server outside the state was against the Rule and agreement with the distributor.

(Paragraph 4.2.13.2)

Profit and Loss Accounts of the distributor revealed that there was a receipt of ₹ 10.73 crore (from 2010-11 to 2014-15) as income from the unsold tickets.

(Paragraph 4.2.14)

4.2.2 Evolution of the scheme of lotteries in Nagaland:

With the objective to generate revenue of the Government for developmental activities 'Nagaland State lotteries' was introduced in September 1971 and the Directorate of State Lottery was established in the year 1972 under the supervision of the Finance Department to conduct and monitor the lotteries. The Government of Nagaland (GoN) had entered into an agreement with a distributor³ in March 2010 to conduct draws of lotteries. Some of the important terms and conditions of the agreement are given in **Appendix 4.2.1**. The agreement expired in August 2012. GoN invited fresh tender on 10 December 2011 for selection of distributors. However, due to court case pertaining to selection of distributors there were no lottery draws during September 2012 to September 2013 which is discussed at **Paragraph No. 4.2.9**. However, the State Government resumed (30 September 2013) operation of lottery draws through an interim agreement with the distributor.

4.2.3 Organisatiuonal Structure

The Directorate of Nagaland State lotteries functions directly under supervision of the Finance Department. The day to day running of Nagaland State lottery is looked after by the Directorate, the Finance Department exercises overall control over it and is involved in most of the important functions like notification, tendering, selection of distributors, approval of schemes, fixation of revenue target *etc.* The Directorate is headed by a Director, who is assisted by a Deputy Director and other subordinate staff. An Officer on Special Duty (OSD) in the rank of Secretary is designated under the Finance Commissioner to supervise the activities of the Directorate.

³ M/s Future Gaming Solutions India Pvt Ltd

4.2.4 Rationale for taking up audit:

Rule 3 (20) of the Lotteries (Regulation) Rules empowers the Central Government to conduct an audit of any lottery or lottery scheme organized by any State through the Comptroller and Auditor General of India. Accordingly, to examine the procedures as laid down in the Lotteries Regulation Act 1998, the Lotteries Regulation Rules 2010, the Nagaland Lotteries Regulations (Rules), 2010 and the overall functioning of the Department, a performance audit of Nagaland State lotteries was conducted covering the period from April 2010 to March 2016.

4.2.5 Statutory conditions regulating lotteries:

As per the Lotteries (Regulation) Act, 1998:–

Lottery– means a scheme, in whatever form and by whatever name called, for distribution of prizes by lot or chance to those persons participating in the chances of a prize by purchasing tickets {Section 2(b)}.

Bumper draw of a lottery– means a special draw of lottery conducted on or during any festival or other special occasion wherein the prize money offered is greater than the prize money offered in the case of other ordinary draw of lotteries {Section 2 (a)}.

The Law/Act/ governing the organizing, conducting or promoting of lottery includes:

- *The prizes shall not be offered on any pre-announced number or on the basis of a single digit {Section 4 (a)};*
- *The State Government shall print the lottery tickets bearing the imprint and logo of the State {Section 4(b)};*
- *The State Government shall sell the tickets either itself or through the Distributors or selling agents {Section 4 (c)};*
- *The State Government itself shall conduct the draws of all lotteries {Section 4 (e)};*
- *The number of bumper draws in a year shall not be more than six in a calendar year {Section 4 (j)};*
- *Any State Government has the power to prohibit the sale of tickets within the State, of a lottery organized, conducted or promoted by other State (Section 5);*
- *Section 7(1) to 7(3) of the Lotteries (Regulation) Act provides that organizing/ promoting/conducting any lottery by any Department of the State Government in contravention of the provisions of the Act or sale, distribution or purchase of the tickets of such lottery by any person or agent or Distributor, shall be punishable with rigorous imprisonment for a term which may extend to two years or with fine or with both.*

Other main provisions of the Lotteries (Regulation) Rules, 2010 and Nagaland Lotteries (Regulation) Rules, 2010 which regulates the lotteries in the State are given at **Appendix 4.2.1.**

4.2.6 Audit Objectives:

The audit on Nagaland State lotteries was conducted to determine whether:

- i. Procedures laid down in the Lotteries (Regulation) Act, Rules and the State specific Rules, and terms and conditions of the agreement with the distributor were followed in letter and spirit while organising lotteries by the States;
- ii. Revenues from the lotteries accrued to the State Governments were properly assessed and got remitted through the distributors/selling agents and taxes on income wherever applicable had been deducted at source and remitted into proper head of accounts;
- iii. All records relating to printing, sale, and return of unsold tickets were maintained by the Directorate of Lotteries as well as the distributors/selling agents;
- iv. The internal control mechanism was adequate, effective and
- v. The revenue generated was being used for the prescribed purposes.

4.2.7 Audit Criteria:

Audit findings were benchmarked against the following criteria:

- The Lotteries (Regulation) Act 1998;
- The Lotteries (Regulation) Rules 2010;
- Nagaland Lotteries (Regulation) Rules 2010;
- Competition Act 2002 (amendment in 2009);
- Supreme Court/High Court judgements;
- Agreements made with the distributors/selling agents and
- Notification/orders issued by the State and Central Governments from time to time.

4.2.8 Scope and methodology of Audit

The Performance Audit of Nagaland State lotteries covered the period from April 2010 to March 2016. The methodology consisted of issue of questionnaires and examination of records/reports etc. in the Finance Department; Directorate and distributors/selling agents. During the audit coverage period (2010-11 to 2015-16), tickets of Nagaland State lotteries were marketed in the following states:

- 1 West Bengal (Paper lottery)
- 2 Punjab (Online lotteries)
- 3 Maharashtra (Paper and Online lotteries)
- 4 Sikkim (Online lotteries)

Audit team inspected the markets at Kolkata (West Bengal) and Mohali (Punjab), printing press at Hyderabad and Data Centre at Bengaluru. An entry conference with the Officer on Special Duty (OSD) and Director of Nagaland State lotteries was held on 19 January 2016 wherein the audit objectives and criteria were discussed. The draft report was issued in May 2016. An exit conference was held on 17 August 2016 with the representatives of the Department and the Government. The replies furnished by the Government as well as the views expressed during the exit conference has been appropriately incorporated in respective paragraphs of the report.

4.2.9 Acknowledgement

Indian Audit and Accounts Department acknowledges the co-operation extended by the Finance Department and the Directorate of Nagaland State lotteries in providing necessary information and records during Audit.

Audit Findings

The audit findings are discussed in the following paragraphs.

4.2.10 Tendering process

Section 4(c) of the Lotteries (Regulation) Act 1998 envisaged that the State Government shall sell the lottery tickets either itself or through distributors or selling agents. Rule 4(1) of Lotteries (Regulation) Rules 2010 envisaged that the Organising State may specify qualifications, experience and other terms and conditions for appointment of distributors or selling agents. Further Rule 2 (h) of the Rules stipulates that “sale proceeds” means the amount payable by the distributor to the Organising States in respect of sale of tickets calculated at the face value printed on each ticket in respect of lotteries of a particular draw or scheme or both.

The basic principle for any tendering process is to have a fair and transparent selection system. The Government should explore all available means to ensure that the participants in tenders are genuine and do not engage in collusive bidding which undermines the very purpose of selection through notice inviting tender (NIT).

The agreement with the distributor⁴ (which was in effect since March 2010 and extended through an Extension Deed and Amendment Deed executed on 30-3-2010 and 22-9-2010 respectively) was to expire in August 2012, GoN invited fresh NIT⁵ for selection of two distributors for five years period. In response to the tender notice, four companies submitted their quoted rates as shown in the following table:

⁴ M/s Future Gaming Solutions India Pvt Ltd
⁵ 10-12-2011

Table No.4.2.1

in ₹

Sl No.	Name of the Company	Minimum Guaranteed Revenue (MGR) ⁶ for Normal draw	MGR for Bumper draw
1	Gaming India distributor Ltd	35,000 (1 st and 2 nd years) 36,000 (3 rd year) and 50,300 (4 th and 5 th years).	1,59,00,000
2	Pooja Fortune Pvt. Ltd.	21,000	Not quoted
3	Divyajyoti distributors Pvt. Ltd	15,100	5,00,600
4	Future Gaming Solutions India Pvt. Ltd	12,005	5,00,500

The Government selected (March 2012) two distributors (M/s Gaming India distributor Ltd and M/s Future Gaming Solutions India Pvt. Ltd.) for both paper and Online lotteries.

Examination of the selection process of the distributors revealed the following:

4.2.10.1 Collusive bidding

According to clause (d) of Section 3 of Competition Act 2002 (amendment in 2009) “any agreement, between enterprises or persons referred to in sub-section (3) engaged in identical or similar production or trading of goods or provision of services, which directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition.”

Further, the Act defines Cartel as: “Cartel includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, or, trade in goods or provision of services.”

Cross examination of the profile of these Companies which participated in the bidding revealed the following:

- Managing Director of M/s Future Gaming Solutions India Pvt. Ltd. and M/s Divyajyoti distributors Pvt. Ltd. were the same person.
- One of the Board members of M/s Divyajyoti distributors Pvt. Ltd. was also the Managing Director of M/s Pooja Fortune Pvt. Ltd.
- M/s M.J. Associate is an associate of both M/s Future Gaming Solutions India Pvt. Ltd. and M/s Gaming India distributors Ltd.
- The Financial Accounts of M/s M.J. Associate was signed by MDs of Future Gaming and Gaming India as partners.

⁶ Minimum Guaranteed Revenue (MGR) is amount payable by the distributor to the State Government for each draw,

From the tender documents it was established that the three companies who participated in the tender were of the same group and the fourth company had business association with the three companies. It was therefore evident that the tenders submitted by these companies were in collusion. However, instead of declaring the companies, who engaged in collusive bidding, as disqualified, the Government awarded the contract to M/s Gaming India distributors Pvt. Ltd. and M/s Future Gaming Solutions India Pvt. Ltd. as per the recommendation of the Screening Committee.

Examination of the evaluation of the NIT revealed that one of the firms i.e., M/s Gaming India distributor Pvt. Ltd. did not fulfill the criteria given in the tender notice as there was no evidence of payment of Income Tax as a company as well as experience certificate fulfilling the condition of having sufficient experience and possessing good knowledge in lottery business. This decision of the Government led to litigation by M/s DivyaJyoti Distribution Pvt. Ltd. in the court of law. Resultantly, the Hon'ble Court directed (July 2012) the State Government not to enter into any agreement with M/s Gaming India distributor Pvt. Ltd. and M/s Future Gaming solution India Pvt. Ltd.

Thus, due to selection of distributors which was not transparent led to court case and suspension of lottery draws during September 2012 to September 2013. Further, M/s Future Gaming Solutions India Pvt. Ltd. who had engaged in collusive binding was engaged by executing an interim contract with the State Government for all draws from 30 September 2013 till date of audit.

The Department in reply (August 2016) stated that the Government had selected M/s Gaming India distributor Pvt. Ltd., for having quoted the highest rate and M/s Future Gaming solution India Pvt. Ltd., on being found to be the most experienced and for having an immaculate track record. The Government also admitted that the Hon'ble High Court quashed the selection of M/s Gaming India distributor Ltd. as it was ineligible and directed to invite a fresh tender.

The Government did not follow the Hon'ble Court order to invite fresh tender. Moreover, the reply is not acceptable as the Department/Government did not scrutinize the profiles of the company diligently to prevent collusive bidding and the selection of the distributors was not transparent which led to a court case and consequently Government suffered a revenue loss during the intervening period of 13 months.

4.2.10.2 Absence of due diligence

The State Government selected Gaming India distributor Pvt. Ltd., and Future Gaming Solution India Pvt. Ltd., for distributorship stating that the Screening Committee had recommended the two firms for conduct of lotteries on the following rates of MGR:

Normal lottery ₹ 35,000 per draw

Bumper lottery ₹ 7,50,000 per draw

However, the basis for fixation of above rate of MGR for both normal and bumper lotteries were not recorded. The concept of MGR does not exist in the Rule which only elaborates sale proceeds from sale of ticket. This resulted in undue financial benefit to the distributor at the cost of State's proceed which is discussed in **Paragraph No. 4.2.11.3.**

4.2.10.3 Lottery schemes

Section 4(h) of Lotteries (Regulation) Act 1998 states that no lottery shall have more than one draw in a week.

Though the Lotteries (Regulation) Act 1998 envisaged one draw a week for a scheme, it does not impose a ceiling on the number of schemes that can be operated in a week. The Lottery Rules 2010, however, allowed maximum twenty four draws from all the lottery schemes put together per day except bumper draws by an organising state i.e a maximum of 168 (24 x 7) different schemes in a week can be conducted in a week. Taking benefit of these situations, same/similar lottery schemes by suffixing or prefixing sub-names words/terms⁷ under 18 lottery group/set name were operated every day of the week during the audit coverage period, thereby compromising the spirit of the Act to limit the number of draws. As the Government was not in a position to monitor effectively all the lottery schemes in a week lottery became an unregulated business which is discussed at **Paragraph No. 4.2.11.**

The Department in reply (August 2016) stated that the names of the lottery schemes are proposed in such a way that the players can remember them easily. No draws are conducted on daily basis and each draw is conducted only on a weekly basis and there was no instance of draws exceeding 24 in any single day.

The fact however remains that the Government could not effectively monitor the lottery schemes. Moreover, the same scheme name of draws were being held daily by prefixing or suffixing the words/terms as sub names, which was against the Act. The details of number of weekly draws operated both paper and Online are given in **Appendix 4.2.2.**

4.2.11 Revenue receipt by the State Government from lotteries

4.2.11.1 Assessment of Revenue from lotteries

As per rule 3 (17) of the Lotteries (Regulation) Rules, 2010, the Organising State shall ensure that proceeds of the sale of lottery tickets, as received from the distributors or

⁷ **Examples:- Scheme Name: Nagaland Super Cards, prefixing/suffixing sub-names on**
Mondays :Pragati, Dawn, Aries, Puppy, Pottasium, Barzona, Takj, Tarachand, Tajdar, Sharla, Shaw, Shell, Shirley **Tuesday** : Ranjani, Dusk, Tarus, Kitten, Sodium, Dextor, Tallen, Tarakan, Talib, Safari, Sahara, Sally, Sam **Wednesday** : Bairavi, Morning, Gemini, Calf, Calcium, Bradford, Tamkinat, Tarang, Tamal, Fairfax, Faith, Falk, Fancy; **Thursday** : Naatai, Afternoon, Cancet, Foad, Ammonium, Jersey, Tanay, Tarik, Tanimay, Tiffany, Tiger, Tilly, Tina; **Friday** : Hindolam, Evening, Leo, Chick, Sulphur, Murraygrey, Tanuj, Tarit, Tanveet, Walden, Walker, Wallace, Wally; **Saturday** : Vasantaa, Night, Virgo, Infant, Magnesium, Redpoll, Tapan, Tausiq, Tapas, Tab, Tacey, Tad, Taima; **Sunday**:Mohanam, Midnight, Libra, Lamb, Phosphorous, Sussex, Tapomay, Tejas, Tarakanth, Mabel, Mace, Maddox, Maddy.

selling agents or any other source, are deposited in the Public Ledger Account or in the Consolidated Fund of the Organising State. Further, Para 4.2 (ii) of GoI letter⁸ instructed all the State Governments to ensure that the entire sale proceeds of the lottery tickets, as received from the distributors or selling agents are first credited into the Treasury/Public Ledger Account/Consolidated Fund of the Organising State without any deduction etc. Payments of commission to distributors/sole selling agents etc. and other sundry payables should be made after the entire proceeds are deposited in the Government Accounts.

“Sale Proceeds” is defined in Lotteries (Regulations) Rules, 2010, as “the amount payable by the distributor to the Organizing State in respect of sale of tickets calculated at the face value printed on each ticket in respect of lotteries of a particular draw or scheme or both”.

However, Clause 7.5 of the Interim agreement made by the GoN with the distributor⁹, stipulated that the distributor shall purchase the lottery tickets from the Government and payments shall be made by the distributor to the Government for such tickets.

As per Rule 3(10) the Organising State shall charge a minimum amount of five lakh rupees per draw for bumper draw of lottery and, for all other forms of lottery, a minimum amount of ten thousand rupees per draw.

Examination of records revealed that the provision of Rule 3(10) fixing the minimum charges on lottery for sale proceed realisable from sale of tickets was misinterpreted when the Addendum Deed was initially executed (7 April 2010) with M/s Future Gaming solutions India Pvt. Ltd., which continued in the subsequent NIT (10 September 2011). The bid document was designed on the above assumption of minimum rate of sale proceed per draw per scheme basis for paper/online/bumper lottery and the tenders were invited on the basis of MGR instead of Commission payable to distributors. This wrong interpretation of Rule 3 (10) by the Department for fixing the MGR instead of sale proceeds led to execution of agreement contrary to the provisions of the Lottery Rules and resulted in huge loss to the State exchequer and undue windfall gain to the distributors at the cost of the state Government.

The entire sale proceeds of ₹ 17,653.74 crore during 2010-16 was not credited directly into the Consolidated Fund of the State violating the Lottery (Regulations) Rules 2010 and GoI order. The revenue for the State in the form of MGR was only ₹ 56.93 crore (0.32 *per cent*) out of the total sale proceeds of ₹ 17,653.74 crore as discussed in **Paragraph No. 4.2.11.3.**

4.2.11.2 Loss of revenue to the Government

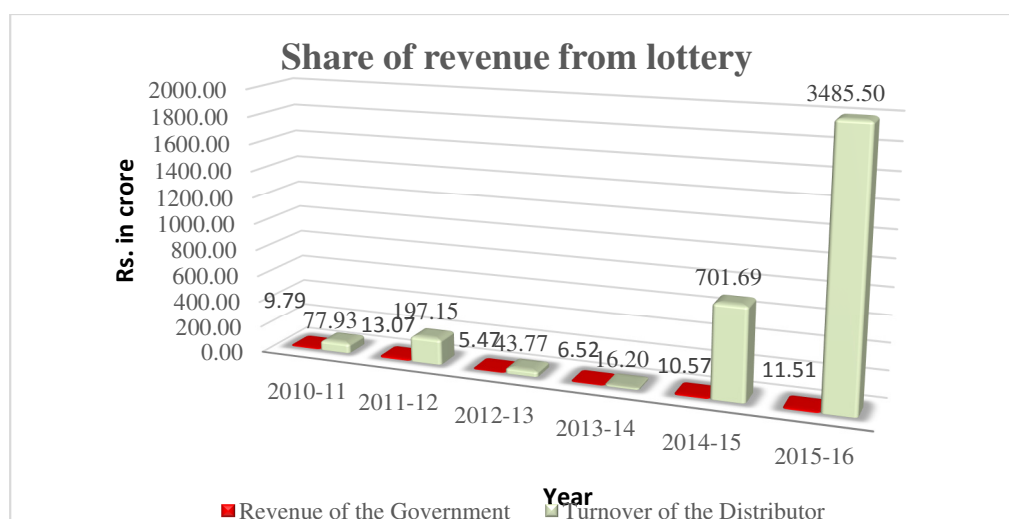
As per para C 19 of the Annexure to the Nagaland Lotteries (Regulation) Rule 2010, the distributor shall lift all the printed lottery tickets at the whole sale/discounted price to be mutually agreed and decided upon by the Director and the distributor, in such advance period as may be laid down in the agreement.

⁸ No.F.No.V.17013/2/2011 CSR-1 dated 2 August 2011

⁹ M/s Future Gaming and Hotel Services Pvt. Ltd.

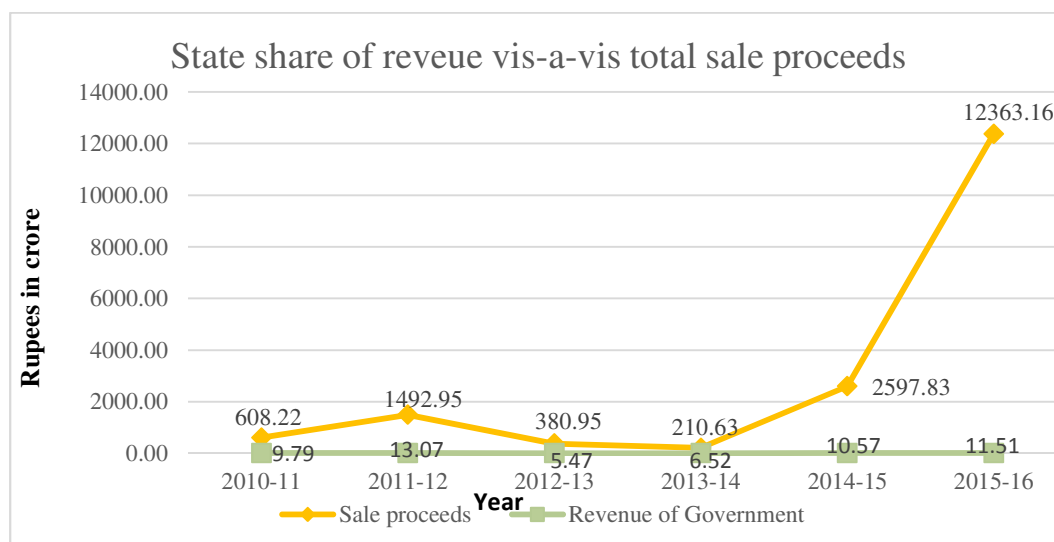
Examination of records revealed that the Department delivered all the tickets to the distributor on all sold basis for a fixed MGR of ₹ 15,000 per draw in contravention of the Government orders. It was also noticed that the distributor deposited the amount of the MGR (calculated on the basis of number of draws per day) to the Consolidated Fund of the State and not the actual Sale proceeds as discussed in the preceding Paragraph. This was not correct as MGR was the minimum guaranteed revenue. This clause should not have prevented the government from the full revenue earned through sale of tickets which should have been credited to Government accounts.

The ratio of share between the Government and the distributor is depicted in the bar chart below:



As seen from the above chart, the ratio of revenue share between the State Government and the distributor during 2010-11 was 1:8 which increased at 1:303 in 2015-16.

The Chart given below depict the state share of revenue with respect to total sale proceeds.



As can be seen from the chart, the total sale proceeds of tickets rose steeply from ₹ 608.22 crore in 2010-11 to ₹ 12363.16 crore in 2015-16, however the revenue of

the Government increased marginally from ₹ 9.79 crore in 2010-11 to ₹ 11.51 crore in 2015-16. The marginal increase was due to conduct of four bumper lottery draws during 2015-16, for which MGR was @ of ₹ 7,50,000 per draw received by the State Government.

4.2.11.3 Windfall gain to the distributor due to MGR

Government of Nagaland fixed the Minimum Guaranteed Revenue (MGR) at ₹ 15,000 per draw in April 2010 (for normal lottery) through an Amendment Deed with M/s Future Gaming Solutions India Pvt Ltd. to conduct both paper and Online lottery in the states of Punjab, West Bengal and Maharashtra.

Audit observed that the Government issued a notification¹⁰ to extend the tenure of M/s Future Gaming Solutions India Pvt. Ltd. for one month w.e.f. 1 August 2012 to 31 August 2012 and raised the MGR from ₹ 15,000 to ₹ 35,000 per draw. The order of the Government was not accepted by the Company, citing the Deed of Agreement with the Government which had fixed the MGR at ₹ 15,000. It was noticed in audit that the Government failed to take legal opinion on this matter and issue an Addendum to the Agreement or renew the deed of agreement while extending the tenure without raising the MGR to ₹ 35,000.

However, it was observed that before the court issued its verdict, M/s Future Gaming Solution India Pvt, Ltd., submitted a proposal (August 2013) to the Government for an interim arrangement to allow them to commence sale of Nagaland lotteries with immediate effect, quoting the MGR at ₹ 15,000 for normal lottery and ₹ 7,50,000 for bumper lottery. Accordingly, the Government approved an interim arrangement (26 September 2013) with M/s Future Gaming Solution India Pvt. Ltd with MGR of ₹ 15,000 for normal lottery and ₹ 7,50,000 for bumper lottery despite the Court's order (4 September 2013), directing the state Government to select the distributors through fresh tender.

It was also observed that the same Company had accepted the MGR of ₹ 35,000/draw when the distributorship was initially awarded on 16 January 2012. Therefore, the interim arrangement of fixing MGR for normal lottery at ₹ 15,000 per draw was not justified. It is also pertinent to mention here that the same Company was paying MGR at the rate of ₹ 36,000 per draw to Sikkim State Government during the same period. Interestingly, M/s Gaming India distributor, Ltd., who had quoted ₹ 35,000 per draw in their tender, also applied for award of the distributorship of the Nagaland State lotteries during the interim period but the Department neither considered the request nor negotiated with the two firms to fix the MGR to at least ₹ 35,000 per draw.

Moreover, due to fixing of the MGR at ₹ 15,000 per draw instead of ₹ 35,000 per draw during the interim period of September 2013 to March 2016 resulted in revenue loss of ₹ 37.80 crore as shown in the following table.

¹⁰ No.Fin/Lot-01/2009(vol-) dated 27th July 2012

Table No.4.2.2

₹ in crore

Year	Total No. of Normal draws	Total Revenue earned (at MGR @ ₹ 15,000 per draw)	Total Revenue that could have earned (at MGR @ ₹ 35,000 per draw offered by M/s Gaming India distributor Ltd)	Revenue loss
2013-14	4344	6.52	15.20	8.68
2014-15	7046	10.57	24.66	14.09
2015-16	7514	11.27	26.30	15.03
Total	18,904	28.36	66.17	37.80

Details in Table (a) and Table (b) of Annexure-2

An analysis was made on the turnover and profit of both the Government and the distributor for the last five years which is tabulated below:

Table No.4.2.3

(₹ in crore)

Year	Number of tickets sold (in crore)	Total Sale proceeds of tickets (₹)	Total Number of draws	Total Prize money pay off (₹)	Expenditure on Printing and Advertisement (₹)	Lottery tax to other states (₹)	Turnover of distributor (₹)	Total Proceeds (₹)	Revenue received by State Govt.(MGR) (₹)	Percentage of Govt. Revenue to Proceeds	Percentage of distributor's share to proceeds
2010-11	304.11	608.22	6528	514.81	0.16	5.53	77.93	87.72	9.79	11.16	88.84
2011-12	709.26	1492.95	8712	1257.86	2.03	22.84	197.15	210.22	13.07	6.22	93.78
2012-13	183.37	380.95	3648	331.24	0.14	0.32	43.77	49.25	5.47	11.11	88.89
2013-14	90.02	210.63	4344	172.22	0.19	15.51	16.19	22.71	6.52	28.69	71.29
2014-15	583.31	2597.83	7046	1835.92	10.71	38.94	701.69	712.26	10.57	1.48	98.52
2015-16	2590.95	12363.16	7518	8717.06	53.50	95.59	3485.50	3497.01	11.51	0.33	99.67
Total	4,461.02	17,653.74	37,796	12,829.11	66.74	178.72	4,522.24	4,579.17	56.93	1.24	98.76

Source: Compiled from data provided by Directorate of Lotteries (Details in Annexure -4.1.2 a & b)

As can be seen from the above, against the total sale proceeds of ₹ 17,653.76 crore the share of the State Government in the form of MGR was only ₹ 56.93 crore (1.24 per cent) of the total sale proceeds whereas the distributor's share was ₹ 4522.24 crore (98.67 per cent) during 2010-11 to 2015-16. Thus, it indicated that the operation of lottery by the State Government was more beneficial to the distributor than the Government.

The Government in reply (August 2016) stated that the revenue of the Government as per the agreement was not reduced. The MGR was net revenue to the Government as all other expenses like printing, advertisements, Lottery tax to other States, etc. were paid by the distributor. Further, it was stated that the quoted rate of ₹ 35,000 per draw made by M/s Gaming India distributor Ltd. was highly unrealistic and complying with the court order would have rendered the Department to remain idle without earning any revenue for six months or so to complete the entire process of fresh tender.

The reply of the Department is not acceptable as MGR was the minimum amount to be paid to the Government and it should not have prevented payment due to the government beyond this amount. Moreover the contention that MGR of ₹ 35,000 per draw was highly unrealistic is not acceptable as the company (M/s Future Gaming & Hotel Services Ltd.) had already accepted the MGR of ₹ 35,000 per draw when the distributorship was initially awarded on 16 January 2012. Besides, the same company was paying higher MGR at the rate of ₹ 36,000 per draw per day to the State of Sikkim during the same period. Moreover, 98.76 per cent earned by the distributor was arrived at after deduction of all the expenses.

4.2.11.4 Violation of Lottery (Regulation) Rules, 2010 led to revenue loss to the Government.

Audit also noticed that the MGR received by the State Government was the net revenue from lottery as all other expenses were borne by the distributors which was against the Act/Rules. Non-taxable prize money and charges to other States were paid by the distributor without producing vouchers for reimbursement from the Government. The value for taxable prize money, cost of printing charges, advertisement cost and draw expenses were deposited by the distributor in separate bank accounts¹¹ operated by the Director of the Department and subsequently disbursed by the Department to meet the respective expenditure from these bank accounts. The balance of sale proceeds were accounted as the earnings of the distributor/area distributor/agents.

The Government in reply stated that (August 2016) regular payment of MGR by the distributor as per the agreement does not result in any revenue loss. The entire sale proceeds after payment of MGR was the earnings of the distributor was misconceived as numerous expenses met by the distributor like printing charges, draw expenses, promotional expenses, commissions to stockiest, sub-stockiest, charges to other States where tickets were marketed etc. had to be taken into account before calculating actual revenues.

The reply is not acceptable as the findings of audit were based on Government instructions, provision of the Act and Rules and agreements executed with the distributor. Also, the net amount of the distributor was arrived at after taking into account all the deductions and expenses.

4.2.12 Draw process of Paper lottery

4.2.12.1 Lottery as gambling

Lottery as a subject is listed at entry 40 of the List I - Union list and entry 62 of the List II - State List of the seventh schedule to the Constitution of India while “Betting and Gambling” is listed separately as entry 34 of the State list. Thus, the Constitution had distinguished lottery from gambling activity.

¹¹ (1) Axis Bank A/c Nos.911010051345554, (2) 911010056176010,(3)Vijaya Bank A/c Nos 810101011003509, (4) 81010101004336, (5) UCO Bank A/c No.08990110014097

Further, section 2(b) of the Lotteries (Regulation) Act 1998 defines “Lottery” as a scheme, in whatever form and by whatever name called, for distribution of prizes by lot or chance to those persons participating in the chances of a prize by purchasing tickets.

During joint inspection of sale of paper lottery tickets at Kolkata, it was noticed that Nagaland paper lottery tickets were sold in a bulk bearing book number 4-6-8-9-20-40 etc., and the players selects a bunch of booklet having the same numbers but different series based on their special numbers.

Nagaland State lotteries sold in bunch of same numbers; bunch numbered 6 and 20 shown below:



The selection of the numbers are predetermined by the players themselves based on previous draw results, their hunch or intuition, lucky numbers, important dates etc. The idea is to purchase similar number of bulk tickets and keeping a scope to maximise their gain by winning multiple prizes. In all these activities, the players take calculated risk in the hope of getting larger pay-outs as in a gambling.

Except for the first prize (which was declared on the entire series of seven numbers), winners for second prize were declared on the last five numbers of any series and for the third prize onwards to sixth prize, winners were declared on the last four digits of any series. Prize money for first prize was ₹ one lakh and from second to sixth it ranged from ₹ 9500 to ₹ 130. Multiple number combinations were declared winners for third to sixth prize. A sample result of Nagaland lottery is shown alongside:

NAGALAND STATE LOTTERIES	
EVE RESULT 18/02/2016	
NAGALAND STATE LOTTERIES DEAR FAITHFUL EVENING 43rd Draw at 18/02/2016 M.R.P. ₹.5/-	
1st Prize	₹ 1,00,000/- 63L 38210
2nd Prize	₹ 9,500/- 52167
3rd Prize	₹ 9,000/- 01934 03068 10363 14697 16585 27609 31056 61010 86052 87954
4th Prize	₹ 500/- 1513 1546 1650 2227 2855 4431 4616 6257 8843 9908
5th Prize	₹ 300/- 0364 2214 2288 6531 6982 7500 7552 7781 9139 9449
6th Prize	₹ 130/-
0165 0714 1704 2779 3949 4763 5419 7291 8025 8899 0257 0830 1967 2888 4043 4805 5466 7334 8067 8949 0301 0864 2004 3160 4185 4816 5662 7481 8147 8963 0320 0910 2038 3208 4219 4866 5687 7490 8169 9019 0362 0979 2050 3305 4354 5044 5939 7625 8254 9198 0485 1283 2391 3600 4356 5047 5940 7634 8334 9542 0564 1521 2501 3649 4511 5120 6558 7676 8337 9586 0600 1574 2509 3756 4518 5171 6582 7925 8352 9594 0689 1615 2594 3857 4573 5173 6824 7970 8426 9770 0698 1684 2754 3866 4680 5268 6842 7992 8703 9869	
ISSUED BY: THE DIRECTOR, NAGALAND STATE LOTTERIES	
EVE RESULT 18/02/2016	
Result of Draw No.43 of Nagaland State Lottery dated 18-2-2016	

It was observed that the manner in which Nagaland State lottery is being organised at present, distorts the distinction between an equal opportunity scheme and gambling. The system of sale of bulk tickets and multiple tickets in same number with different series is rather being organized as gambling and not as lottery as defined.

The matter was referred to the Government, however, no reply has been received (December 2016).

4.2.13 Online lottery

As per Rule 2(1)(e) of Lottery(Regulations) Rules 2010, "Online lottery" means a system created to permit players to purchase lottery tickets generated by the computer or Online machine at the lottery terminals where the information about the sale of a ticket and the player's choice of any particular number or combination of numbers is simultaneously registered with the Central Computer Server.

Audit observed the following deficiencies in the conduct of Online lottery:

4.2.13.1 Draw process of Online lottery

Section 4 (a) of Lottery (Regulations) Act 1998 stipulated that “prizes shall not be offered on any preannounced number or on the basis of a single digit”.

Further Rule 14 of Lottery (Regulations) Rule 2010 laid down that “An Organising State shall not offer a prize on a lottery ticket or in an Online lottery on the basis of single, double or triple digit in any form or combination”.

Lottery draws of the Nagaland State Online lottery were to be conducted within the premises of the Directorate of Lottery under the supervision of an Officer of the Department and two judges.

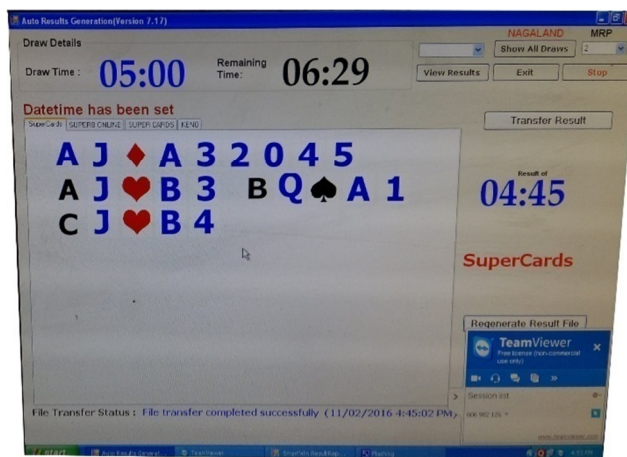
Audit observed that no specific stoppage time for sale of Online tickets before the actual draw was fixed by the Department and the Online draw was done through a computer programme by random draws and the tickets were sold till the last moment before the draw. No sale reports were generated before the draw and there were also no records at the disposal of the Government officer/judges to verify that the lottery draw was conducted on sold tickets only.

Examination of the serial numbers of the Online lottery tickets revealed the composition of the ticket number as follows:

Series No.	1 st letter	2 nd symbol	3 th letter	4 th digit	5 th to 8 th digits			
A/B/C	J/K/Q	♠♣♥♦	A/B	1-4	0-9	0-9	0-9	0-9

For example, a first prize winning number can be AJ B20354 or CK A41234.

It was noticed during the joint physical inspection of the market, at the Point of Sale (PoS), the players could choose only the letters/symbols/ number from the 1st to 4th letter/digit of any series (suffixing one numeral from 1 to 4 at the end), for which second prizes are awarded. The software in the terminals did not display the four digit number sequences under 5th to 8th digits. For the first prize the complete set of the number i.e. all the 8 letter/digits



Online Lottery draw from the computer of Directorate of Lotteries, Nagaland in respect of Online Lotteries

were to be considered. However, since the players cannot opt for the numbers under 5th to 8th digits and therefore it is obvious that they do not play for the 1st prize. When the tickets are printed the software automatically generates the numbers under the 5th to 8th digits to form randomly generated number from 0001 to 9999.

According to information furnished by the distributor, the average number of tickets sold per Online lottery draw worked out to 4,33,892 tickets¹² whereas 36,00,000 combination of tickets could be generated from the entire 8 digits including the number sequence from 0001 to 9999 in one single draw. The players were allowed to choose only for the first 4 combination of letters and symbols/digit but were not allowed to select the numbers under the 5th to 8th digits of the ticket number whereas the draws for the 1st prize were held for entire 36,00,000 combinations with the 8 digit combination of all the tickets including random generated numbers from the 5th to 8th digits. Audit noticed that draws were conducted on the entire range of 36,00,000 tickets without considering the number of tickets sold and unsold, as no system exists to filter sold/unsold tickets before the draw. Thus, the chances of winning of prizes falling on an unsold ticket was extremely high as all 36,00,000 combinations were never sold out in a single draw (1 out of 36,00,000 is the probability of 1st prize winning number, whether there is 100 per cent sale of tickets or not).

Further, draws for second prize to the last prize are drawn using only the 1st to 4th letter/symbol/digit combinations suffixing a single digit from 1 to 4. For example, a second prize winning number can be:

AJ□B2 or AJ□ A1 or BK□ A4

Therefore, draws for the second prizes onward was done on a single digit with combination of letters and symbols prefixed, which was in violation of Rule 14 Lottery (Regulations) Rules 2010 and section 4(a) of the Act.

¹² Calculated on an average of last 5 years.

Thus, the system adopted for Online tickets violated the Act and Rules and rendered the scope of winning almost impossible as the actual sequence were never sold.

The Government in reply stated (August 2016) that there were huge transactions involved in any Online draw and to verify them before each draw was not practically viable. The software in the PoS was designed for easy purchase/sales in the market and the player could select any eight digits number as per his wish in the terminals in a separate screen. It was not correct that players were not allowed to play for all 8 digits as the operators used different screens for selection of combinations as per the player's preference.

The reply of the Department is not acceptable as the Department did not know the number of PoS used by the distributor. Although it was obligatory on the part of the Government to check systems and procedures in the PoS, it was observed that there was no control of the State government on the system of online lotteries since actual physical and financial database were inaccessible to the State Government. Moreover, the State Government did not provide system test certificate of the software used for Online lottery that players could select any eight digits number as per their wish in the terminals and the players were allowed to choose only the first four combination of letters/symbols and digits. In the PoS, Mohali audit along with departmental officials in a joint verification, observed that there was no system in the software to segregate the sold tickets to limit the lottery draw on sold tickets only and the players were allowed to choose only first four combination of letters/symbols and digits. Government needs to verify the system and procedure being followed by PoS to ensure that all the 8 digit numbers could be chosen by the buyer of lottery ticket.

4.2.13.2 Conduct of Online lottery without Server database

As per Rule 2(1)(b) of the Regulations, "Central Computer Server" means a system of multiple computers at a central location under the direct control of the Organising State that accepts, processes, stores and validates the Online lottery transactions or otherwise manages, monitors and controls the entire system of Online lottery.

Further, as per Clause 14.4 of the Agreement with the distributor, for Online lotteries, the Central Server should be located within the geographical limits of the State of Nagaland and the Information and Technology Department and the lotteries of the State of Nagaland shall have free access to the server.

The State Government did not furnish any documents in respect of maintenance of database of Online lottery conducted prior to 10 May 2015. As no records were shown to audit it appears that the stated distributor did not have a server-based database of Online lottery conducted prior to 10 May 2015. Further, audit noticed that neither the Central Computer Server was located within the geographical area of the State nor the State Government had free access to the server in violation of the Rules and agreement.

An agreement was executed (10 May 2015) by the distributor in May 2015 (M/s Fortune Enterprise, Mumbai and M/s Net4India, New Delhi) for hosting the database of Nagaland lottery and to allow M/s Fortune Enterprise to utilize "a certain

pre-agreed space” or “area” occupied by M/s Net4India from M/s Tata Communications Services Ltd.

The agreement did not state the relationship between the distributor and M/s Fortune Enterprise nor does it state that M/s Fortune Enterprise will be utilizing Datacenter for hosting the database of Nagaland lottery. Moreover, this agreement was executed only on 10 May 2015, whereas Online lottery of Nagaland was being conducted by the distributor since May 2010.

The Department in reply (August 2016) stated that physical location of the server was not located within the state but kept at Data Centre (Central Server) in the premises of renown M/s Tata Communication Services, Bangalore with three tier security system.

The fact however remains that having the Central Server outside the state was against the provision of the agreement and also this arrangement was done only after 10 May 2015. There is nothing on record to show the system being followed before May 2015.

4.2.13.3 Mirror Server not installed

A mirror server is a file server that contains a duplicate set of files, so that the site or files are available from more than one place. As per para C (2) of the Annexure to the Nagaland Lotteries (Regulation) Rules 2010 a Mirror Server shall be monitored in the Directorate of Nagaland State Lotteries by the Director or his authorized officer.

According to Clause 14.5 of the agreement entered between the Government and distributor for effective monitoring and security in case of Online lotteries, the distributor shall also maintain a mirror server to have a ready backup of the data and the mirror server should be updated simultaneously with the Central Server.

Joint physical verification of the Server placed in the Directorate revealed that the Server was not configured as a Mirror Server but just a LAN server with Internet connection. There was neither a database in the server nor was any database applications installed on it. However, the server was configured to access a remote server placed in an unknown location through web browser for printing customized tailor-made reports on Online lotteries. The two servers placed with the Department were only used for printing custom made reports by accessing a Remote Server.

The Department accepted (August 2016) the audit observation and stated that installations of new mirror servers are being made and is expected to be functional within the month of August 2016. However, the facts remains that no Mirror Server had been installed in the Directorate till date (December 2016).

4.2.13.4 Periodical backups of database

During joint physical inspection of the servers installed in the Directorate, it was noticed that the Servers did not have any database of the Online lottery. The Department stated that backups are maintained by the Directorate in flat files¹³ but could not furnish copies of the backups of the database to audit. It was also observed

¹³ Text file (csv format)

that the Server placed in the Department, was not configured as a mirror server, and therefore the Government/ Department did not have access to the database or create backups of database of Online lottery. As the Data Centre (Central Server) was also not within the geographical limits of the State, the Government remains inaccessible to its own database and the actual physical and financial status of the Online lottery.

The Department in reply (August 2016) stated that the distributor had submitted the copy of the backup of all the data of the audit period.

The reply is not acceptable as the observation was on maintenance of periodical backups by the Department. Incidentally, the backup data provided by the distributor to audit also could not be restored. The server installed in the Department did not have a database system. This is indicative of the facts that the claim made by the Department that backups of database were provided by the distributor to the Department not factually correct.

4.2.13.5 Software for conduct of Online lottery

Examination of the Information Technology (IT) systems for Online lottery revealed that the distributor uses a custom developed software for conduct of lottery, reporting and for draw by engaging M/s Acentech, Mumbai. Audit observed that the distributor did not submit the User Requirement Specification (URS) and Software Requirement Specification (SRS) to the Government for verification and approval. The State Government did not test the system nor provide the System Test Certificate (STC) to the distributor for using the software for Online lottery. As a result audit could not draw an assurance that the software being used by the distributor protected the interest of the State. Thus, the Government by not certifying the software as well as the technical documents, provided an opportunity to the distributor to develop the software to suit his interest.

Further, joint physical verification (24 February 2016) of Online lottery sales at Mohali, Punjab, revealed that the sale of Online lottery was carried out from Hard Disk of PCs connected to the net. In such a scenario, it was possible to customize the software in selected terminals of the geographically distributed PoS to query from its own database installed in the PC and conduct the sales of tickets offline, which would not be reflected in the Central Server database. Thus, it could not be ruled out that Online lotteries were conducted offline using Personal Computer (PC) terminal since May 2010 to 10 May 2015.

The Department in reply (August 2016) stated that the software was exclusively developed for Online lottery operations and hence the design and operations fit perfectly for the purpose it was designed. Various PoS were set up in the market which are connected to the Central Server and communicate each and every transaction, adding relevant data to the database and then on the tickets printed. The draws of the Online lotteries are conducted in the Directorate in the presence of the Government appointed Judges so that the distributor would not take any undue advantage over the draws in anyway.

The reply is not acceptable as the distributor did not have a server-based database of Online lottery conducted prior to 10 May 2015. It was also not possible for the Department to certify the software and its capability without examining the design and operations as the State Government did not provide the STC for using the software of Online lottery.

4.2.13.6 Deficiency in Audit trail of internal access controls

Joint inspection (22 February 2016) of the Data Center (Central Server) at Bengaluru where the database of the Department is hosted was carried out to verify the various internal controls in the Data Centre.

The Data Centre provided three layers foolproof security as far as Physical Access is concerned. However, it does not provide any audit trail to verify the adequacy of internal controls like, Logical Access Controls, Remote and Virtual Access Controls, Input Controls, Output Controls etc., to the database. Since access to the Data was provided to an IT consultant, M/s Acentech (placed in Mumbai) through remote access without defining the privileges/roles granted to the consultant, audit could not draw an assurance regarding the integrity of the Online data. Moreover, there was no audit trail to access the internal controls built into the system. Further, the Data Centre being a third party organization, with whom the Government had not made any agreement, audit was denied access to server logs and other documents relating to breakdown or disruption of server systems, access controls to database, remote servers, etc.

It was also observed that the database of Online lottery consists of details of Online sales, through which reports on sales and income generated on sale of Online tickets are printed by the distributor. Therefore, providing full privilege to the IT Consultant (who works for the company) render the database susceptible to modifications to the advantage of the distributor.

The Department in reply stated (August 2016) that the 3-tier Data Centre of M/s Tata Communication Services is well known for its high standards and adequate security measures. The premises are totally under high security and no unauthorized persons can gain entry into the data enter.

The reply of the Department that the database was kept under a fool-proof security is not acceptable as the Department had not accessed the database or conducted audit on the Online lottery system. Further, the Department was silent on the adequacy of internal controls like, Logical Access Controls, Remote, Virtual Access Controls, Input Controls, Output Controls etc. to the Server and its database.

4.2.13.7 Non availability of experienced IT personnel or support

Organising of Online lotteries require the services of an expert on Information and Communication Technology (ICT) to handle the complex operations and to safeguard Government's interest.

Audit observed that the Online distributors used IT solutions of their own choices and convenience without the approval or knowledge of the Government for running their respective lottery schemes. Audit also observed that there was no regular

officer/official in the Lottery Directorate having adequate knowledge of the operating systems, programme software and applications and communication technology used in running the Online lottery schemes to regularly monitor the draw process. The entire Online lottery draw process was handled by representatives of the distributor in a draw room of the Directorate. Thus, the Directorate was not in a position to monitor the functioning of Online lotteries or issue specific instructions regarding the quality, make and the uniformity of ICT applications to be used from time to time.

The Government in reply stated (August 2016) that appointment of experienced IT personnel in the Department would be examined. However, the fact remains that conduct of Online lotteries without any IT personnel in the Directorate failed to safeguard the interest of the State.

4.2.14 Claim of prizes on unsold tickets

As per Rule 4(5) of Lotteries (Regulations) Rules 2010, the distributors or selling agents shall return the unsold tickets to the organising State with full accounts along with the challans of the money deposited in the Public Ledger Account or in the Consolidated Fund of the Organising State through the sale of tickets.

Paragraph 4.6 and 4.7 of the agreement also stipulated that the distributor shall prepare and submit a statement showing the number and the aggregate value of all the tickets sold per draw before the draw is conducted. The unsold tickets shall be returned by the distributor to the Director, Nagaland State lotteries to be excluded from the draw.

During joint physical verification (February 2016) of the godown of the distributor at Kolkata, it was noticed that huge quantity of unsold tickets in respect of Nagaland State lotteries were dumped in the godown without being reported or returned to the State. It was also seen from the records that an amount of ₹ 1.44 crore (excluding TDS of ₹ 61.97 lakh) as prize money during 2010-16 were paid to the agents, distributor/sub-distributors/selling agents on unsold tickets (of taxable prize money) directly by the directorate office.

Further, cross examination of the Profit and Loss Accounts of the distributor revealed that there was a receipt of ₹ 10.73 crore (from 2010-11 to 2014-15) as income from the unsold tickets which was against the provisions of the Lottery Act and Rules.

The Government in reply stated (August 2016) that the agents appointed by the distributor for selling of lottery tickets in the market were in effect the end purchasers of lotteries. They purchase the lotteries in bulk on payment of the price of the lottery tickets thereby assuming the risks incidental thereto and such lottery tickets purchased by the agents from the distributor are deemed to have been fully sold. There is no system of return of unsold tickets to the distributor from stockiest, sub-stockiest, retailers, etc. Therefore, there are no unsold tickets from the perspective of the State Government and the claim of ₹ 10.73 crore as per accounts of distributors is not based on actual facts.

The reply is not acceptable as it contradicts the provisions of the Lottery (Regulation) Rules 2010 and the conditions of the terms of agreement. The distributor also did not

remit the amount from unsold prize winning tickets to the Government and therefore in effect participated in the draw which violated the provision of the Rules. Hence, the amount of ₹ 10.73 crore retained by the distributor as prize money from the unsold tickets should be deposited to Government account.

4.2.15 Printing of tickets without inviting rates of quotation from empaneled Printers

As per Rule 3 (5) the paper lottery tickets and the stationery on which the Online lottery tickets are issued shall be printed by the Organising State at a Government Press or any other high security press included in the panel of the Reserve Bank of India or the Indian Banks' Association, Mumbai.

The Government of Nagaland engaged the following Security press from the panel of the Indian Banks' Association, Mumbai for printing lottery tickets:

1. M/s Sreenidhi Secure Print (P) Ltd, Hyderabad
2. M/s Nutech Security Printers, New Delhi
3. M/s Gemini Graphics, Bengaluru

Examination of records revealed that the name of printing press were proposed by the distributor for approval of the Government for all the lottery scheme. The printing cost was borne by the distributor. Thus, the Government has only a token role in the selection of Printers for printing of the tickets which violated the spirit of the Rule.

4.2.16 Distribution of lottery tickets

According to Clause 4.7 of the Agreement, the Agent and/or any of his sub-agents or retailers shall not be involved in receipt or dispatch of the lottery tickets or stationeries from the Government Press/Security Press.

During joint inspection of the printing press and Nodal Officer, Kolkata, it was observed that:

- the Department does not have an office or godown of its own in Kolkata to receive the huge volume of printed tickets;
- the printed lottery tickets were directly delivered to the area-distributors of the paper lottery ;
- the distributor submitted a copy of delivery challans to the Government official for onward submission to the Directorate does not guarantee transparency and accountability.
- in Mumbai, also when paper lotteries were conducted (2013-14), no Government representative was posted to oversee or receive the printed lottery tickets, indicating that the printed lottery tickets were delivered directly to the distributor/area distributors;

These were the serious lapse on the part of the Government as printed tickets should have been delivered to the Government representative only with adequate facility/manpower to receive and verify the tickets. This indicated that the

Government had no control over the number of tickets printed nor on the quality of the tickets.

The Government in reply stated (August 2016) that the tickets are distributed by the distributor throughout the market with their well-established network of stockists, sub-stockists, agents, sub-agents, retailers/sellers etc., as it involved huge manpower, time and cost.

The reply of the Government confirms the fact that adequate control over receipt and delivery of lottery tickets by the Government from the printing press to the distributor was not adhered to. Moreover, Government representative was posted only in Kolkata (West Bengal) and not to other states where Nagaland State lottery tickets were sold conducted.

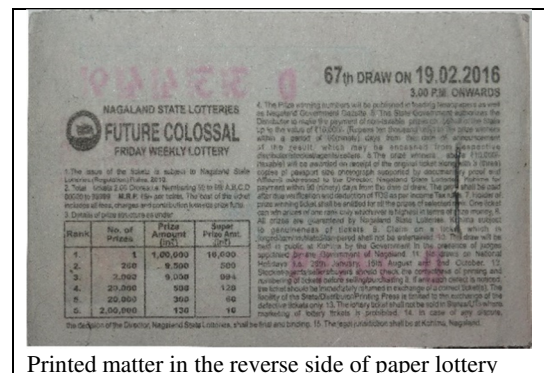
4.2.17 Form, size and design of Paper lottery tickets

According to Para C (6) of Annexure to Nagaland Lotteries (Regulation) Rules 2010 states that “The printed tickets for a particular draw shall bear the imprint and logo of the State Government, distinctive number, the date/time of draw and the sale price of the ticket/maximum retail price (MRP) and facsimile signature of Director, Nagaland State lotteries. On the reverse side of the tickets, there shall be a printed information in English/Hindi or any Regional language showing prize structure and such other essential details and conditions as the State Government may consider necessary for the purchasers. Such terms and conditions which appear on the lottery tickets shall be determined by the State Government through the Director.”

Examination of the tickets revealed that the size of the fonts of the information printed on the back side of the paper lottery tickets of Nagaland State lottery marketed in West Bengal were in fine prints which were barely legible even to a person of normal vision as shown in the photograph.

Further, it was observed that the reverse side of the tickets did not contain address, contact number and website address of the Directorate for easy reference of the customers.

Thus, the customers were deprived the opportunity to read the information of the lottery schemes printed on the reverse side of the ticket



Printed matter in the reverse side of paper lottery

Audit further observed that the name of the organising State and its logo were given less importance in comparison to the name of the lottery scheme as evident from the size of the fonts and logos. Audit also noticed that the lottery tickets of Nagaland and Mizoram were so similar to one another that they could not be easily distinguished as shown in the following photographs.

<p>Nagaland State Lottery: Dear Gentle Evening Sunday Weekly Lottery</p>	<p>Mizoram State Lottery: Dear Gentle Sunday Weekly Lottery</p>

As different state lottery tickets were printed in the same printing presses, the bidders were proposing similar design and size to minimize printing cost. This indicates that the design and size of the paper lottery were determined by the distributor and the printing presses and the Department merely approves whatever designs the distributor proposed.

Thus, the Nagaland State lottery tickets were not differently designed from the other state lottery tickets and the players were not able to recognize the tickets distinctly from other state lottery tickets. As a matter of fact, there was nothing on record to indicate that the Directorate had taken any action to ensure that the unique identity of Nagaland state lottery ticket was maintained.

4.2.18 Commission to distributors/selling agents

As per the Lotteries (Regulation) Act 1998, the rate of commission payable to the distributors for marketing the lottery of the State was required to be fixed by the State Government. Income Tax¹⁴ from the commission at the rate of 10 per cent was also required to be deducted at source by the Directorate before payment of commission and credit the sum so deducted to the credit of the Central Government.

It was observed that, the State Government, instead of fixing the rate of commission, fixed the rate of MGR to be received from the distributors per draw. In this scenario, the net revenue from the sale of lottery ticket after printing cost, prize pay-out, cost of publication of result, charges given to other States, and MGR etc., was retained by the distributors.

The Government in reply stated (August 2016) that the Financial Statements and Income tax assessment details are required from the distributor only during tender process and these are not submitted by the distributor annually. The Government further stated that to earn revenue the State depended upon the distributor to sell its ticket in West Bengal, Punjab, Maharashtra, etc. as it did not have any market of its own within Nagaland. For the purpose of marketing, vast expertise, numerous establishments and enormous expenses were involved. In order to safeguard the revenue being spent for organising the lottery, the Government decided to opt for

¹⁴ Section 194G of Income Tax Act, 1961

fixed MGR. This ensured that the Government had a steady flow of funds whether the lotteries were marketed or not.

The reply is not acceptable as the decision of the Government to resort to MGR instead of commission basis violated the provision of the Lotteries (Regulation) Act 1998. The replies are also indicative of the fact that the amount retained by the distributor is not known to the State Government. The State Government also did not ascertain the net amount of revenue accrued to the distributors and failed to deduct Income Tax at source as per the Act.

4.2.19 Prizes of Online tickets kept at ₹ 10,000 and below to avoid Income Tax

According to Section 198B of the Income Tax Act, 1961, the State Government was required to deduct 30 per cent Income Tax at source on any prize money in excess of ₹10,000 and other winnings from games, lotteries etc.

Examination of records revealed that all the Online lottery schemes (including the fixation of prizes) were approved by the Government as proposed by the distributor without any alteration. It was also observed that the maximum prize money in respect of all the Online lottery schemes sanctioned/approved were fixed at a maximum of ₹ 10,000 for the first prize.

A condition was imprinted on the Online ticket that only prize money valued more than ten thousand rupees was required to be claimed from the concerned Government. All the 1st prizes of the Online lotteries were kept at ₹ 10,000 and the other prizes were ranged between ₹ 9000 and ₹ 40. The percentage of total prize money vis-à-vis total sales of Online tickets during 2010-11 to 2015-16 is given in below:

Table No.4.2.4

₹ in crore

Year	Total Sale proceeds of online tickets	Total number of Draws	Total Prize money payoff	Percentage of Prize payoff to Total sale proceeds
2010-11	607.34	6,474	514.21	84.67
2011-12	1,289.68	8,180	1,107.19	85.85
2012-13	366.34	3,584	320.63	87.52
2013-14	172.11	4,123	143.27	83.24
2014-15	217.43	6,723	179.02	82.33
2015-16	496.26	4,626	415.33	83.69
Total	3,149.16	33,710	2,679.65	85.09

Source: Compiled from data furnished by Directorate of Lotteries

As can be seen from the above, the total prize payoff ranged from 82.33 to 87.52 per cent of the total sale proceeds. However, the maximum prize money was fixed at ₹ 10,000 resulted in non- payment of Income Tax. This also permitted the distributors to claim the first prize from unsold winning tickets without TDS as discussed in Paragraph No.4.2.14

The Government in reply stated (August 2016) that as per the Income Tax Act, 1961, income tax is applicable only on prize money exceeding ₹ 10000. The Lotteries (Regulation) Rules, 2010, Clause 3(9) stipulated that “the first prize in any lottery scheme shall not be less than ten thousand rupees”. All schemes are formulated without violation on this score.

The reply is not acceptable as the first prize were kept at ₹ 10,000 and the total prize pay-out ranged from 82.33 to 87.52 *per cent* of the sales proceeds to avoid deduction of Income Tax at source on prize money from winners.

4.2.20 Inadequate supervision of lottery in the states where lottery is conducted

As per Rule 3 (15), Rule 3 (21) of Lottery Rules, it is the responsibility of the Organizing State to effectively supervise the conduct of lottery till publication of results and to ensure that the distributor/Agents engaged by the Organizing State acts in conformity to the provisions of Acts and Rules.

GoN conducts lottery in the states of West Bengal, Maharashtra, Punjab and Sikkim. The lottery tickets are printed in Hyderabad and Delhi.

During joint physical verification (18 February 2016) of the nodal office at Kolkata, it was observed that one State Government official was posted as Nodal Officer with no other supporting staff. The responsibility of the official was to receive the consignment of paper lottery tickets from the Printers and deliver them to the area distributors as per printing order issued by the Department as well as maintenance of records of receipt and delivery. A large quantity of consignment is received (around 52 crore of lottery tickets per week) and therefore it is practically impossible for a single person to verify the quantity/quality of the lottery tickets received by the nodal office. Thus, the duty of the official is practically limited to record keeping as per print order. Monitoring of lottery draws conducted by the agencies or inspection of records maintained by the area distributor/stockiest or agencies was not conducted at any level. Further, joint inspection of Online lottery at Mohali, Punjab and the Printing Press¹⁵ in Hyderabad, revealed that no officers from the Government were available to inspect the proper conduct of the lottery and printing of tickets on regular basis.

The Government in reply stated (August 2016) that inspection and verification are carried out by the Department periodically in States where Nagaland State lottery tickets are being sold. Regular monitoring will require an establishment to be put in place which will involve a huge expenditure negating the very purpose of conducting lotteries.

The reply is not acceptable as the Lottery Regulations Rules clearly states that it is the responsibility of the Department to oversee the conduct of lottery till publication of results.

¹⁵ M/s Sreenidhi Printers

4.2.21 Internal Control

Internal control is an integral function of an organisation which ensures achievement of the objectives of the organisation. It is intended to provide reasonable assurance of proper enforcement of Acts and Rules.

The internal control system in the Department was found inadequate and ineffective as the mandatory returns such as unclaimed prize money, sales report, audited accounts were not prepared by the Department. The accounts/records submitted by the distributor/area distributor *etc.* were also not inspected or verified. As a result, the practice of non-preparation of sale report/audited accounts/unclaimed prize continued unabated.

Monitoring of the activities of the distributors or their sub-agents to detect illegalities/irregularities was found lacking as occasional surprise checks and physical verification of records of distributors and printers were never carried out. It was noticed that the distributors paid the draw charges in advance to the States where the State lottery were marketed but the certificates issued by the concerned State authorities were not submitted to the Directorate.

The Government in reply stated (August 2016) that the distributor submitted the sales reports, unclaimed prize money, audited accounts, the tax paid challans and certificates regularly and was also monitoring the sales and related activities. The State Government was also intimating the concerned State Governments where the Nagaland State lotteries were being marketed with the details of the games, distributor and sub-distributors, the person liable for payment of taxes and other charges.

The reply of the Department is not acceptable as there were no records of verification to authenticate the correctness of the accounts/records submitted by the distributor.

4.2.21.1 Financial and System audit

Rule 3(19) of Nagaland Lotteries (Regulation) Rules 2010 stipulated that every Organising State shall conduct an annual financial and systems audit of the various lottery schemes organised by it including Online lottery. In addition, according to para C (25) of Annexure to Nagaland Lotteries (Regulation) Rules 2010, the State Government/Director may appoint a locally based renowned firm/company of Chartered Accountants and technical experts for the purpose of conducting annual financial and system audit.

Examination of records revealed that the Department did not conduct any financial and system audit of the lottery schemes organized by the State during 2010-11 to 2015-16. Instead the Department relied upon the statements furnished by the distributor on the number of draws conducted and MGR payable per draw. The Department also did not initiate to conduct an IT Audit of the installations by the IT, Departments on Online lottery.

Thus, the Department was unaware of the daily sale proceeds and annual sale proceeds of the distributor, the total number of tickets sold/unsold, actual price payoff, total expenditure on conduct of lottery and compare with the MGR received by the State.

4.2.21.2 Internal Audit wing

The Directorate did not have an internal audit wing. The Government also had not appointed any personnel or entrusted any State Government Departments to conduct internal audit to evaluate the functioning of the lottery schemes.

The Government in reply (August 2016) stated that the rule provisions to appoint local auditor was a major obstacle as no renowned firm/company existed in Nagaland.

The reply is not acceptable, as the Department could not provide any documentary evidence of the attempt made by the Government (by way of advertisement on dailies or otherwise) to find a locally renowned firm/company of Chartered Accountants and Technical Experts for conduct of financial and system audit.

4.2.21.3 Conduct of lottery without specific scope and purpose

Rule 3 (2) of Lotteries (Regulation) Rules 2010 states that the State Government may organise a lottery or lotteries if it so decides by issuing a notification in its Official Gazette outlining the purpose, scope, limitation and methods thereof. However, the Government of Nagaland introduced lotteries with the objective to generate of revenue of the Government for developmental activities and specific scope or purpose was not defined.

Examination of the records revealed that the MGR received from the sale of lotteries was deposited in the Consolidated Fund of the State. The rules framed by the Government of Nagaland regarding conduct of lotteries and the notifications published in the Official Gazette approving the conduct of the lottery inconspicuously mentioned that the proceeds shall be deposited into the Consolidated Fund. The fund intended to be appropriated from the revenue of lotteries for developmental activities were not clearly defined. Thus, it is clearly established that the conduct of lottery by the Government was not for any targeted social or developmental schemes.

The Government in reply stated (August 2016) that the revenue generated from organizing lotteries was deposited in the Consolidated Fund which was utilized for various developmental activities. It further stated that it was difficult to precisely earmark a particular defined activity for utilization of the revenue generated from lotteries as the State is faced with extremely short on resources for generation of revenue.

The reply is not acceptable as para "C" of the Annexure to the Nagaland Lotteries (Regulations) Rules 2010 clearly stated that the main purposes and scope of organizing the lotteries is to earn additional revenue of the State for developmental activities. The targeted developmental activities were not defined and revenue

intended to be earmarked from the conduct of the lotteries were not clearly stated while approving each scheme.

4.2.22 Conclusion

The Nagaland State lotteries was introduced to earn revenue for developmental activities. There was irregularities in selection of distributors which led to litigation in court case and suspension of lottery draw for 13 month. Running of Nagaland lotteries was mainly controlled by the distributor while the State Government was left with its revenue to Minimum Guaranteed Revenue (MGR) per draw in violation of the Lotteries (Regulation) Rules 2010.

The distributor made huge profit from the sale proceeds of Nagaland State lotteries whereas revenue of the State Government was in the form of MGR only. The rate of MGR had not been revised or reviewed since May 2010. Out of the total sales of ₹ 17,653.76 crore during 2010-16 the distributor deposited only ₹ 56.93 crore being MGR to the Consolidated Fund of the State. The distributor neither deposited the balance amount of ₹ 17,596.83 crore to the Consolidated Fund of the State nor it was demanded by the State Government. Against the revenue accrued to the distributor ₹ 4,522.24 crore (26 *per cent* of gross sale) during 2010-16 the Government received ₹ 56.93 crore (0.32 *per cent* of gross sale). The main factor contributing to this was fixing the revenue realizable from the lotteries per draw at the MGR which had no relation with the volume of sale of tickets. Thus, due to conduct of lottery on the basis of MGR, the distributor revenue was without bounds while the Government revenue was capped to MGR formula. This resulted in loss of revenue and undue financial benefit to the distributor. In violation of Act and Rules the entire sale proceeds calculated at face value of the tickets was not deposited to the Consolidated Fund of the State without any deduction.

The State had not verified the system being used by the distributor to conduct the online lotteries as a result audit could not draw an assurance that they were adequate. Physical location of the Central Server of online lotteries was not located within the State. The Data Centre (Central Server) does not provide any audit trail to verify the adequacy of internal controls. Online lotteries were not properly monitored due to absence of Information Technology personnel in the Department. Unsold tickets were not excluded from being part of draw resulting in claim of prize from unsold tickets. The maximum prize money of Online lotteries were fixed by the distributor at ₹ 10,000 or below to avoid payment of Income tax. Monitoring and internal control system of the Department was inadequate as no vital records such as unclaimed prize money, sales report etc., were not prepared by the Department. The Department did not conduct any financial and system audit of lotteries in violation of the Nagaland Lotteries (Regulation) Rules 2010. The utilization of revenue generated from Nagaland lotteries for developmental activities were not clearly defined in the Rule.

4.2.23 Recommendations

For effective running of the State lotteries and to safe guard financial interest of the State, the State Government may ensure to:

- to retender for selection of distributors and allocated the job for conducting of lotteries as per Act and Rules;
- deposit the entire sale proceeds calculated on the face value of the tickets in the Consolidated Fund of the State without any deduction and deposit unclaimed prize money to the Government Accounts in time;
- Central Server should be under the direct control of the State Government and the activities of online lotteries should be effectively monitored;
- strengthen monitoring and internal control by appropriate measure like conducting of financial and system audit annually and set up Internal Audit wing in the Directorate; and
- define clearly the purpose of conducting lotteries by evolving the mechanism to allocate funds necessarily to the intended purposes out of the revenue generated from lotteries in the annual budget of the State

MOTOR VEHICLES DEPARTMENT

4.3 Computerisation of Motor Vehicles Department

The Motor Vehicles Department in the State of Nagaland was established in 1963 as per section 133-A of the Motor Vehicle Act, 1939. The Department is governed by the Central Motor Vehicles (MV) Act 1988, the Central Motor Vehicles Rules 1989, the Nagaland Motor Vehicles Taxation Act 1967 and the Nagaland Passengers and Goods Taxation Act 1967. For effective implementation and integration of the data the Transport Department introduced (1996) Computerisation of Motor Vehicles in Nagaland in a DOS based FoxPro database application on Novell Software developed by M/s NagaSoft, Kohima. By the year 1997, all RTOs/DTOs were fully computerised using this application software till 2008. From July 2008, the software packages of 'Vahan' and 'Sarathi' software introduced by GOI on an Oracle platform was implemented in the Regional Transport Office (RTO), Kohima and subsequently in October 2009 in all the seven Regional Transport Officers/District Transport Offices (DTOs), with support from NIC Nagaland. Online issue of National Permit System (NPS) was implemented on September 2010 in the Office of the Transport Commissioner, Nagaland, Kohima.

Performance Audit for the period from April 2011 to March 2016 on computerisation of the Motor Vehicles Department revealed inadequacies in implementation of IT software, planning, management, training, monitoring and internal control of computerization as brought out in this Report.

Highlights

The Department did not formulate and adopt any IT policy and therefore the risk involved in record keeping of user data, statutory documents, revenue collection and data security, were not ensured.

(Paragraphs 4.3.8.1)

The Department had not completely migrated to the more advanced system of Vahan and Sarathi from the old legacy system to provide smooth interface with the data of Regional Transport Officers and District Transport Officers while issuing authorisation for national permits and collection of taxes/fees by State Transport Authorities. The Department also did not incorporate provision for validation checks in the software to compulsorily capture statutory fields at the time of data entry.

(Paragraphs 4.3.8.2)

Non-utilisation of complete permit module resulted in irregular issue of permits for goods and passenger vehicles and also resulted in underutilisation of the Vahan database for integration with databases across India.

(Paragraphs 4.3.10)

Instances of short remittance of revenue to Government account ranging from ₹ 1.06 lakh to ₹ 2.55 crore in the selected districts were noticed. As of March 2016, a revenue of ₹ 8.37 crore was retained in the bank account of Axis bank in contravention of the terms of agreement.

(Paragraphs 4.3.14.2 and 4.3.14.3)

4.3.1 Introduction

The Motor Vehicle Department introduced Computerisation of Motor Vehicles in Nagaland in the year 1996 in a DOS based FoxPro database application for capturing data such as issuance of driving licences, certificate of fitness for transport vehicles, registration of motor vehicles and granting regular and temporary permits to the vehicles, collection of taxes and fees. The Department in 2008 decided to implement 'Vahan' and 'Sarathi' software systems developed by the National Informatics Centre (NIC) in order to have a national database of registered vehicles and driving licences issued and for providing valuable data to the Central Government security agencies. In spite of the decision to implement Vahan and Sarathi in 2008, Audit noticed that even after eight years of its implementation the Department continued to operate the old software (2016). It was also noticed by audit that both old and new software were used ignoring the quality controls for data such as data integrity, data security, correctness of data and usage of data. This resulted in under achievement of the benefits of computerisation.

4.3.2 Overview of the IT application systems

In 1996 the Motor Vehicle Department commenced introduction of computerised system in capturing data, issuing licences, certificates etc., in a FoxPro database

application. Thereafter, Vahan and Sarathi an Oracle platform was introduced by GoI in July 2008.

FoxPro:-It is a database management system and a relational database management system which extensively supports multiple relationships between multiple database files.

Vahan: It is an application developed by NIC Headquarters, Delhi for registration of Vehicles and collection of road tax, issue various certificates and permits and record fitness of vehicles by the RTA/RTO.

Sarathi: It is an application developed by NIC Delhi for issue of Learner’s driving licenses, Permanent driving licenses, conductor’s licenses and Driving School licenses.

National Permit System: It is an electronic system for grant of National Permit and was developed in consultation with the NIC and operates in web-based environment with a central server in Delhi.

All offices of the Department were provided the facility of separate LAN systems functioning under three tier architecture (Database Server, Application Server and clients) for Vahan and a two tier architecture for Sarathi on a Client-Server relationship architecture. The database server runs on a Linux Server with Oracle 10g database and Windows OS on application Servers and Clients. System support is provided by NIC, Nagaland for customization and modifications of Vahan and Sarathi according to local requirements. Smart Card based registration certificates and driving licenses are being printed and activated using web page application namely Key Management System (KMS) software.

The comparison of functions of FoxPro and Vahan/Sarathi are as follows.

FoxPro	Vahan and Sarathi
<ul style="list-style-type: none"> • Collection of authorisation fees of National Permit • counter-signature of temporary permits, • collection of goods tax, • passenger tax, • late fines for inter-State vehicles and all Nagaland tourist taxi/bus permits 	<ul style="list-style-type: none"> • registration of Vehicles • collection of road tax, • issue of various certificates and permits • fitness of vehicles • issue of Learner’s driving licenses • Permanent driving licenses, • conductor’s licenses and Driving School licenses

The old system under FoxPro and the new system under Vahan and Sarathi are running simultaneously in the Department.

4.3.3 Organisational setup

The Secretary to the Government of Nagaland (GoN), Transport & Communication Department is the Administrative Head of the Motor Vehicles Department and the Transport Commissioner (TC) as the Head of the Department. There are two Regional Transport Officers (Kohima & Mokokchung) and six District Transport Officers (Dimapur, Phek, Mon, Tuensang, Zunheboto & Wokha) in the state.

4.3.4 Audit objectives

The objectives of Performance Audit on the Computerisation of Motor Vehicles Department were to assess whether:

- The IT applications of Vahan, Sarathi and National Permit System were implemented fully in all the RTOs and DTOs of the State.
- Adequate IT controls existed to ensure data integrity, data security and data accuracy.
- Funds sanctioned for computerisation were utilised economically and efficiently and revenue collection thereof deposited into Government account without undue delay and leakages.
- Appropriate monitoring and internal control mechanism was in place at all levels to monitor the implementation of the IT systems.

4.3.5 Audit Criteria

The Performance Audit was carried out based on the following criteria:

- Motor Vehicles Act 1988 (MV Act)
- Central Motor Vehicles Rules 1989
- Nagaland Motor Vehicles Taxation Act 1967
- Nagaland Passengers & Goods Taxation Act 1967
- IT Act 2000 (As amended by IT (Amendment) Act 2008) of GOI.
- Notifications, circulars and orders issued by the GOI and GON from time to time.
- Operational guidelines of Vahan, Sarathi & National Permit System developed by NIC.

4.3.6 Audit Scope and Methodology

Audit covered the offices of the Transport Commissioner, all the two RTOs (Mokokchung & Kohima) and two DTOs (Dimapur & Phek) out of six DTOs selected on the basis of Simple Random Sampling Without Replacement (SRSWOR) method during May 2016 to July 2016. The Audit methodology included checks on validation of data integrity, data processing, reporting and security controls using the Computer Assisted Audit Technique Tools like IDEA, MS Access, MS Excel etc. The Performance Audit on Computerisation of Motor Vehicle Department for period 2011-16 was covered. An entry conference was held (6 May 2016) with the Transport Commissioner, Departmental Officers and NIC Nagaland to discuss the audit scope and methodology, criteria and objectives. The draft report was issued to the Department in September 2016. An exit conference was held with the Departmental Officers on 10 November 2016 to discuss the findings of audit. The views expressed during the exit conference and the replies furnished by the Department were considered and suitably incorporated in the report.

4.3.7 Acknowledgement

Indian Audit and Accounts Department acknowledges the co-operation of the Motor Vehicles Department, Government of Nagaland and NIC for providing necessary information and records to audit.

Audit findings

The findings of audit are discussed in the following Paragraphs:-

4.3.8 IT applications of FoxPro, Vahan, Sarathi and National Permit System

4.3.8.1 IT Policy and framework

IT policy is a comprehensive document to be developed by a user Department while implementing computerization. It includes security, purchase, user level definition backups and disaster recovery policy, password policy, copy right laws, privacy legislation of personal data, data protection, business continuity policy for efficient upgradation and modification in software packages, stock management etc.

Examination of records revealed that the Department did not formulate nor adopt any IT Policy for planning and implementation of the principle of action proposed to achieve the computerised functions and its objectives and to mitigate the risk of data management. Thus, the Department failed to specify and ensure capturing of complete data, proper record keeping and statutory documents, interlinking of database, data security and revenue collections etc.

The Department in reply (October 2016) stated that the IT policy is under draft stage.

4.3.8.2 FoxPro Application and Vahan and Sarathi modules in the State

Chapter V of Motor Vehicle Act 1988 empowers the State Transport Authority (STA) to authorise issue of National Permits, counter-signature of temporary permits, collection of goods tax, passenger tax, late fine etc., for inter-State vehicles and all Nagaland tourist taxi/bus permits. The current version of Vahan (2.0) has the modules for vehicle registration, fitness, taxation, permit, pollution under control certificate, trade license and enforcement whereas Sarathi (1.0) has the modules for driving license, learner's license, conductor's license and driving school license.

Examination of records revealed the following:

- **Fox Pro application software:**-Though the use of FoxPro application software was to be discontinued from the date of implementation of Vahan and Sarathi, the Department continued to use the FoxPro software developed by M/s NagaSoft, Kohima for the functions undertaken by STA for collection of authorisation fees of National Permit, counter-signature of temporary permits, collection of goods tax, passenger tax, late fine etc., for inter-State vehicles and all Nagaland tourist taxi/bus permits. Incidentally, the use of outdated database and deficiencies in the FoxPro application and instances of data manipulation was pointed out in the Audit Report of the Comptroller &

Auditor General of India- Government of Nagaland for the year ending 31 March 2008. However, no tangible action was initiated to address these issues.

Analysis of data captured in the FoxPro further revealed the following deficiencies:

- There was no validation check on date of receipt leaving a scope for entering incorrect dates in this field.
- There was no input validation check in any of the fields in the system as a result some fields were not captured while making data entry.
- There is no user hierarchy system for validation and approval of data entry thereby enabling possible entry of incorrect or unauthorised data.
- Database of daily receipts in respect of 69 records (26 June 2013) and 164 records (18 November 2014) from the database of national permit authorisation were deleted.
- Free access of the account with administrator rights (super user) were provided to the data entry level.

Thus, the Department continued to use the FoxPro software without adequate and requisite IT controls inspite of Government decision to implement Vahan and Sarathi. This led to capturing of incorrect date in the field, incomplete fields and entry of incorrect and unauthorized data.

Vahan and Sarathi: As per Section 47 of Chapter III, Central Motor Vehicle Rules 1989, certain documents such as valid insurance certificate, address proof documents, vehicles documents etc. are made compulsory for vehicle registration and issuance of driving license. In addition, IT applications should have in-built controls which automatically rejects data entry if such mandatory information are not captured. The Department issues Pollution Under Control Certificate (PUC) in Vahan software environment, however, permits, trade license and the enforcement module are being issued using FoxPro Software as a result the modules prescribed by GoI remained underutilized and also the mandatory information was not captured during registration of vehicles and issue of driving license as discussed below:

- Out of 80,349 vehicles¹⁶ registered in four districts during 2011-16, only 167 PUCs¹⁷ were found to be issued through Vahan software.
- Out of 6202 permit fees¹⁸ for goods and passengers vehicles realised and captured in Vahan software, only 74 certificates¹⁹ were found to be generated from the software indicating issue of permits using the old system or manually.

¹⁶ 31,857 vehicles (DTO Dimapur) + 1670 vehicles (DTO Phek) + 8653 vehicles (RTO Mokokchung) + 38,169 vehicles (RTO Kohima) = 80,349 vehicles

¹⁷ 140 certificates (DTO Dimapur) + NIL (DTO Phek) + 8 certificates (RTO Mokokchung) + 19 certificates (RTO Kohima) = 331 certificates

¹⁸ 4267 permit fees (DTO Dimapur) +145 permit fees (DTO Phek) +329 permit fees (RTO Mokokchung) + 1461 permit fees (RTO Kohima) = 6202 permit fees

¹⁹ 22 (DTO Dimapur) +NIL (DTO Phek) + 49 (RTO Mokokchung) + 3 (RTO Kohima) = 74

- No records were entered under the module of Enforcement in Vahan indicating non-utilisation of the module in all four test checked districts.
- The module under Sarathi for issue of conductor's license was not utilised at all in all the four test checked districts.
- It was observed that the modules and features provided under Vahan and Sarathi were not fully utilised which resulted in capturing of incomplete data in the database and irregularities in issuing of permits and PUCs.
- Out of 80,349 vehicles registered during 2011-16 in four selected districts, the date of purchase of 899 vehicle was not captured (**Appendix-4.3.1**).
- Out of 77,168 records of driving licenses issued in four selected districts during 2011-16, Pin Codes in permanent address of 366 applicants, PIN Codes in temporary address of 8190 applicants and identification mark of 1153 applicants were not captured (**Appendix-4.3.1**).

Though the Department decided to migrate to more advanced system of Vahan and Sarathi, provisions for compulsory and uniform applicability of the software was not made. The Department also did not lay down adequate IT controls nor incorporate provision for validation checks in the software to compulsorily capture statutory fields at the time of data entry and provisions for audit trail. This led to capturing of partial, incomplete and incorrect data coupled with potential loss of revenue as discussed in paragraphs **4.3.14.1 to 4.3.14.3**.

The Department in reply (October 2016) stated that the process for up-gradation or replacement of the legacy application has started. The Department further stated that the date of purchase of vehicles was not captured during the initial stage of digitalization. However, it has now been made mandatory. The Department also stated that all offices have been notified to mandatorily include the pin code.

The fact remains that the Vahan software were partially or under-utilised and the permits were issued manually.

4.3.9 IT controls, data integrity, data security and data accuracy

IT applications should have in-built controls which automatically check whether the data entered is accurate and valid. The accuracy of data input to a system can be controlled by incorporating computerised validation checks on the data presented to the system. As discussed in paragraph **4.3.8.1 and 4.3.8.2**, the Department did not formulate and adopt IT policy for planning and implementation of computerised functions and also continued to use the outdated software application instead of the comprehensive software application of Vahan and Sarathi. Audit therefore made an attempt to analyse the data in four selected districts which revealed that incorrect data were entered into the system due to lack of validation checks in the software. Instances of such incorrect and unusual data are discussed below:

- **Incorrect city name:** Out of 80,349 vehicles owner records in four selected districts, 56,052 (70 per cent) records with incorrect name of the city under

temporary address column and 45,287 (56 per cent) incorrect name of the city in permanent address were captured in the database.

- **Incorrect PIN Code:** 325 instances of incorrect PIN Code were captured in temporary address and 10681 records have incorrect PIN Code in permanent address (**Appendix-4.3.2**).
- **Incorrect pin code in driving licenses:** Out of 77,168 driving licenses issued in four selected districts, 8810 had incorrect PIN Code in the temporary address and 67 cases of incorrect PIN Code was recorded in permanent address.
- **Incorrect timing for issue of fitness:** Out of 88,631 records of fitness testing captured in four selected districts, 1303 vehicles were recorded as tested during 6 pm to 6 am of a particular day (**Appendix-4.3.2**).
- **Incorrect registration of vehicle:** Out of 36,959 vehicles already registered in other States and brought to Nagaland for re-assignment of new number, in 9555 vehicles, the old registration number assigned by other States were not captured in the database (**Appendix-4.3.2**).
- **Incorrect identification marks:** 2446 cases of incorrect identification marks were recorded in the database (**Appendix-4.3.2**).
- **Incorrect blood group:** In 1131 cases non-existent blood group *e.g.* Blood group 'U' were recorded (**Appendix-4.3.2**).

Thus, it was observed that there was no validation checks to reject entry of incorrect and inaccurate data rendering the data incomplete and unusable at both State and National Registers of Transport Department.

The Department while accepting the facts stated (October 2016) that necessary instruction has been issued to all the offices to mandatorily include the PIN code, identification mark and blood group in the addresses of the vehicle owners. The anomaly in the timing of fitness tests were due to failure of the CMOS Battery, which has now been rectified. It was also stated that the irregularity in vehicles having old and new registration numbers was due to a technical problem which has been resolved with the help of NIC officials.

4.3.10 Capturing of permits issued through the system

Section 66 of Central Motor Vehicle Act 1988 (Necessity for permits) states that no owner of a motor vehicle shall use or permit the use of the vehicle as a transport vehicle in any public place whether or not, such vehicle is actually carrying any passengers or goods save in accordance with the conditions of a permit granted or countersigned by a Regional or State Transport Authority or any prescribed authority authorising him the use of the vehicle in that place in the manner in which the vehicle is being used.

Analysis of data in four selected districts revealed that though the RTO/DTOs were realising permit fees through Vahan software for passengers and goods vehicles,

essential details such as permit number, type of permit and permit validity were not captured in the Vahan database rendering the data incomplete as detailed below:

Table No.4.3.1

Districts	No. of transport vehicles (excluding Government vehicles)		Total number of permit details captured in Vahan database
	Registered during 2011-16	Number of permit fees realised through Vahan	
Kohima	26,572	1,461	3
Mokokchung	6,143	329	49
Dimapur	6,763	4,267	22
Phek	721	145	0
Total	40,199	6,202	74

As can be seen from the table above out of 40,199 registered transport vehicles in these four districts during 2011-16 only 6202 (15.43 *per cent*) permit fees were realised through Vahan and 74 records of essential information for issue of permits were entered in the Vahan database.

Non-utilisation of complete permit module resulted in irregular issue of permits for goods and passenger vehicles and also resulted in underutilisation of the Vahan database. As a result, integration with databases across India was also impacted. Details of transport vehicles plying without permits or expired permits also could not be generated by the software. This would have aided the enforcement wing in effective control on these vehicles. Besides, the very purpose of computerisation and its benefits in implementation was not availed by the Department.

The Department in reply assured (October 2016) that the matter would be rectified with the support of the NIC.

4.3.11 Transport vehicles without fitness certificate

As per Section 56 of the Motor Vehicle Act 1988, every transport vehicle should carry an effective certificate of fitness issued by the prescribed authorities or by any authorised testing stations specified by the State Government. This certificate of fitness in respect of a transport vehicle granted under section 56 shall be in Form 38 and such certificate when granted or renewed shall be valid for the period as indicated: (a) two years for new transport vehicles and (b) one year for renewal of certificate of fitness.

Database of Vahan in four selected RTOs/DTOs were analysed and it was found that 5836 transport vehicles out of 40,199 registered during 2011-16 were plying without a valid fitness certificate as detailed in the following table:

Table No.4.3.2

Sl. No.	Districts	No. of transport vehicles	
		Registered during 2011-16	Plying with Expired Fitness Certificate
1.	Kohima	26,572	2,012
2.	Mokokchung	6,143	1,142
3.	Dimapur	6,763	2,252
4.	Phek	721	430
	Total	40,199	5,836

As illustrated in the above table, out of 40,199 transport vehicles registered during 2011-16, fitness certificate of 5836 transport vehicles (14.51 *per cent*) had expired but were not renewed. These vehicles were still plying which was a violation of MV Act. This indicated that the enforcement wing of the Department did not utilise the information available in the Vahan database to detect and penalise those transport vehicles plying without valid fitness certificate. The Department also failed to effectively use the system and enforce the provisions of the Act. The data captured in the system were also incomplete and incorrect which led to leakage of revenue as discussed in paragraph 4.3.14.1 and 4.3.14.2.

The Department, while accepting (October 2016) the facts, stated that fitness certificates had to be manually issued outside the application as the Department does not possess required infrastructure for vehicle inspection and certification. The upgraded version of the application would address this matter.

The fact however remains that there was already a provision in Vahan software to capture the data of all vehicles and therefore the database should have been effectively used.

4.3.12 Statutory provisions for imposing penalty on delayed registration

Section 43 of the Motor Vehicle Act 1988 stipulates that the owner of a motor vehicle may apply to the registering authority to have the vehicle temporarily registered with a validity period for a maximum of one month. Section 47 & 48 of Central Motor Vehicle Rules 1989 also stipulated that an application for registration of a motor vehicle shall be made in Form 20 to the registering authority within a period of seven days from the date of taking delivery of such vehicle, excluding the period of journey.

Analysis of the Vahan database revealed that out of 80,349 vehicles registered in four selected districts, 24,751 vehicles were registered after a delay of 30 days as shown in the following table.

Table No.4.3.3

Districts	Total number of vehicles (2011-16)	No. of vehicles registered after delay of				Total
		1-6 months	6-12 months	1-2 years	More than 2 years	
Kohima	38,169	7,537	859	423	285	9,104
Mokokchung	8,653	1,562	313	247	320	2,442
Phek	1,670	425	165	153	133	876
Dimapur	31,857	8,463	2,517	910	439	12,329
Total	80,349	17,987	3,854	1,733	1,177	24,751

It can be seen from the table that 17,987 vehicles were registered after a delay of one to six months, 3854 vehicles after a delay of six to twelve months, 1733 vehicles after a delay of one to two years and 1177 vehicles after a delay of more than two years.

The Department accepted (October 2016) the facts and assured that necessary steps were being taken to impose penalty on defaulters.

4.3.13 Inbuilt mechanism for vehicle registration

Section 40 of the Motor Vehicle Act 1988 requires every owner of a motor vehicle to register his/her vehicle in the jurisdiction of the registering authority where he has the residence or place of business or where the vehicle is normally stationed. Thus, as per the provision of the Act, the Registering Authority is responsible to process only those applications for registering the vehicles whose owner's residence or place of business fall under their jurisdiction.

Examination of Vahan database revealed that the system did not have an in-built mechanism to ensure that the temporary or permanent address of the vehicle owner was within the jurisdiction of the registering authority. It was also observed that the address of the vehicle owners were captured even though the addresses provided were outside the jurisdictions of the registering authorities or from outside the State. Data analysis of the four selected districts revealed that during the period from 2011-16, 1727 registered vehicles belonged to districts outside the registering authority and 421 vehicles owners were from outside the State as detailed in the following table.

Table No.4.3.4

District	Total number of vehicles (2011-16)	Other districts of Nagaland	Outside the State	Total
Kohima	38,169	1,239	130	1,369
Mokokchung	8,653	396	76	472
Phek	1,670	40	195	235
Dimapur	31,857	52	20	72
Total	80,349	1,727	421	2,148

As can be seen from the above table, registration of 2148 vehicles whose address of the vehicle owners or where the residence/place of business of the owner or where the vehicle is normally stationed were outside the jurisdiction of the registering authority.

Thus, registration of vehicles whose addresses fall outside the jurisdiction of the respective RTO/DTOs without capturing the correct addresses of the vehicle owners violated the provision of the Act. Besides, the Department failed to control and detect incorrect registration and also compromised the objective of issuing demand notice to the defaulters and tracking of owners of the vehicles for law enforcing agencies.

The Department in reply (October 2016) stated that all efforts would be made to enable the owners to seek registration or submit application for grant of licenses in their own areas.

4.3.14 Fund management

4.3.14.1 Payment of goods and tax by commercial/transport vehicles

As per Section 3 of the Nagaland Passengers and Goods Taxation Act 1967, there shall be levied, charged and paid to the State Government a tax on all fares in respect of all passengers and goods carried in a taxable vehicle²⁰. Further as per Section 9 of this Act, if the prescribed authority is satisfied that the owner is liable to pay tax in respect of any period but has failed to pay the tax, the said authority may after giving the owner a reasonable opportunity of being heard, assess the amount of tax if any, due from the owner and also direct that the owner shall pay in the prescribed manner.

Analysis of Vahan database in four selected districts revealed that out of 64,558 commercial/transport vehicles registered during the last ten years²¹, 36,040 vehicles defaulted in payment of goods/passengers tax amounting to ₹ 5.64 crore and 45,631 vehicles defaulted payment of road tax of ₹ 17.25 crore. However, there was no record to indicate that the Department had taken action to realise the tax from the defaulters. The enforcement wing also did not utilise the information from Vahan software to compound those vehicles. This resulted in potential revenue loss of ₹ 22.89 crore²² (Appendix-4.3.3).

The Department stated (October 2016) that “Demand Notice” would be served to all defaulters and followed up in collaboration with the District Administration.

4.3.14.2 Non-capturing of transaction

Rule No. 6 (1) of Receipt & Payment Rules 1983 states that all moneys received by or tendered to Government Officers on account of revenues or receipts or dues of the Government shall, without any undue delay, be paid in full into the accredited bank for inclusion in Government account. The RTOs/DTOs receive Government revenue in the form of road tax, goods tax, passenger tax, registration of vehicles, permit fees, fitness fees etc. which are computerised and received through Vahan application software. At the end of each day’s transaction, summary sheets for ‘cash receiving users’ were printed in a separate sheet from the software and the total amount

²⁰ All commercial transport vehicles including passengers and goods

²¹ Life span of transport vehicles was considered for ten years i.e. from April 2006 to March 2016

²² Tax defaulting amount was calculated as per the rate of tax paid last

reflected in the summary sheets were accounted for in the cash book as Government revenue receipts for the day.

Examination of the summary sheets and daily revenue receipts recorded in the cash book in the four selected RTOs/DTOs along with the revenue receipts generated and extracted by audit from Vahan database revealed that there was a difference of ₹ 5.28 lakh²³ between the two records. Thus, the revenue of ₹ 5.28 lakh collected through Vahan was not deposited into Government account and the possibility of misappropriation cannot be ruled out.

The Department in reply stated (October 2016) that two RTO (Dimapur and Mokokchung) and DTO, Phek had deposited an amount of ₹ 5.09 lakh to the treasury.

The fact remains that an amount of ₹ 0.19 lakh still need to be recovered and deposited into Government account. The Department was also silent on initiating disciplinary action for temporary misappropriation of Government revenue.

4.3.14.3 Irregularities in remittances of revenue collected by the Department

Rule No. 6 (1) of Receipt & Payment Rules 1983 states that all moneys received by or tendered to Government Officers on account of revenues or receipts or dues of the Government shall, without any undue delay, be paid in full into the accredited bank for inclusion in Government account. Money received as aforesaid shall not be utilised to meet departmental expenditure nor otherwise kept apart from the accounts of the Government.

The Motor Vehicles Department, Nagaland entered (September 2011) into an agreement with Axis Bank Ltd. for collection of cash, cheques or demand drafts etc. from the office premises of Regional Transport Officers/District Transport Officers in Kohima, Dimapur, Mokokchung and Transport Commissioner's Office on every working day. As per Clause A (2) of the agreement, Axis Bank will remit the collection of the first to fourteenth day of the month on the 15th of each month and the balances from the 15th till the month end would be remitted on the 1st day of the subsequent month. For the month of March, the amount would be deposited on the 31st March itself through treasury challan to the designated Government account in the State Bank India.

Examination of revenue collected and deposited by the Department into Government account revealed that there were short remittances into Government account ranging from ₹ 1.06 lakh to ₹ 2.55 crore in respect of Dimapur, Kohima and Mokokchung districts as shown in the **Appendix – 4.3.4**. It was also noticed that as on 31 March 2016, the Department had a closing balance of ₹ 8.37 crore²⁴ in Axis Bank accounts even though the full amount was required to be remitted into Government account as per the agreement.

²³ ₹ 3.23 lakh (DTO Dimapur) + ₹ 1.43 lakh (RTO Mokokchung) + ₹ 0.62 lakh (DTO Phek) = ₹ 5.28 lakh

²⁴ ₹ 0.83 crore (DTO Dimapur)+ ₹ 5.88 crore (RTO Kohima)+ ₹ 1.66 crore (RTO Mokokchung) = ₹ 8.37 crore

The Department in reply stated (October 2016) that the onus of depositing the revenue into Government Treasury lies with the Axis Bank.

The fact remains that the Department has to monitor and ensure that the bank carries out the provisions of the agreement. Moreover, no action was taken by the Department against the bank for the delay in depositing the revenue in Government account.

4.3.15 Monitoring and Internal Control Mechanism

4.3.15.1 Inadequate training and lack of training needs analysis

Computerisation in Motor Vehicles Department in the state of Nagaland commenced in the year 1996 by adopting a DOS based FoxPro database application which has since migrated to a more advanced system of Vahan and Sarathi based on an Oracle database platform. Computerisation requires imparting of computer and software operating knowledge to the user clients by way of conducting trainings at regular intervals.

Examination of records revealed that the Department did not conduct Training Needs Analysis (TNA) of the staff who were assigned to operate these software packages. The Department also did not formulate any annual training calendar for imparting training to the staff at regular intervals.

Thus, deficient training opportunities and development of IT skills of the staff operating the system resulted in wrong data entry, capture of incomplete information and under-utilisation of features/provisions of the application software.

The Department in reply stated (October 2016) that imparting training to staffs is being contemplated.

4.3.15.2 Lack of monitoring and internal control mechanism

An independent and effective internal control mechanism under the direct control of the Head of the Department is essential for ensuring compliance and adherence to provisions of Act/Rules regarding assessment of duties and overall functioning of the system. Computerisation in Motor Vehicles Department was introduced to ensure effective and smooth functioning of the day to day activities and to ensure that revenue leakage do not occur.

The Department did not have an effective internal control mechanism. Examination of records revealed that there was no mechanism for monitoring and inspection of various offices by the Senior Management. It was also observed that no IT Policy was adopted by the Department for effective monitoring and internal control of IT systems. The Department did not conduct any internal audit of the IT system and revenue collection thereof. Non-utilisation of enforcement module in Vahan and Sarathi also indicated ineffective utilisation of computerised data by the enforcement wing. Reporting mechanism of technical failure and system deficiencies for quick redressal and documentation of the problems faced by the user clients in different district offices was also not adequate

Irregularities in data capturing, IT infrastructure management and deficiencies in revenue collection were indicative of inadequate monitoring and internal control mechanism in the Department.

The Department in reply stated that (October 2016) the issue is being considered under IT policy which is in process of finalisation.

4.3.15.3 Physical access to IT facilities and damage by natural disaster due to improper maintenance of server rooms/IT Infrastructure

The objective of physical and environmental controls is to prevent unauthorized access and interference to IT services. To meet the objective, the computer equipment and the information they contain and control should be protected from unauthorized users. They should also be protected from environmental damages caused by fire, water (either actual water or excess humidity), earthquakes, electrical power surges or power shortages. The entity's IT security policy should include consideration of physical and environmental risks.

On verification of the IT Infrastructures at the Transport Commissioner's Office and test check of selected RTOs/DTOs, it was noticed that entry to the Server rooms and other IT facilities were not restricted. In TC's Office, many damaged and unused batteries, UPS, desktops, printers, network cables etc., were haphazardly dumped inside the server room. In RTO Kohima and RTO Mokokchung, no separate room was allocated for the servers and they were accommodated in the common office space accessible by any person and susceptible to damage and theft. In DTO Dimapur, the server room could be accessed by even the non IT staffs and clients. It was also found that many files were dumped in the server room of DTO Dimapur. Moreover, unused IT equipment were stored in the unused toilets and bathrooms of the TC Office and RTO Kohima resulting in possible risk to damage by water and moisture. Security devices like CCTV and intruder alarms were not installed in any of the offices. Fire extinguishers installed in the four selected offices were outdated which were manufactured in the year 2000 without any further refilling and maintenance.

The above instances indicated that effective measures to prevent unauthorised physical access to server rooms, installation of necessary equipment for prevention of damages by environmental factors and natural disasters were not ensured.

The Department in reply (October 2016) stated that it is actively considering steps to prevent access by unauthorized person to sensitive areas of IT installation.

4.3.16 Conclusion

Though the functions of the Department had been computerised, no IT policy for effective planning, management, training, monitoring and internal control of computerisation was formulated. Instead of migrating to Vahan and Sarathi, the Department continued to use the outdated FoxPro database. Modules prescribed under Vahan and Sarathi such as enforcement, permit, PUCC, trade license and conductor's license were not being used by the Department. There were several deficiencies in

validation checks of software application which resulted in capturing of empty fields, incorrect data like insurance details, permit details, vehicles owner's details etc. The Department failed to incorporate statutory provisions regarding jurisdiction of registering/licensing authority and realisation of penalty for delay in registration. There were instances of default in payment of road tax, renewal of road tax and goods and passengers' tax. 5836 transport vehicles were also plying without valid fitness certificate. The Department kept revenue amounting to ₹ 8.37 crore outside Government account.

4.3.17 Recommendations

The recommendations of audit are:-

- The Department may endeavour to implement all the modules of Vahan and Sarathi to make the State and National Register database complete.
- Effective data validation checks should be incorporated in the software and essential information as provided in the Acts and Rules made mandatory to capture valid, correct and accurate data.
- Efforts should be made to strengthen the enforcement wing and reports generated from Vahan for taking penal action on vehicles plying without valid fitness certificate, permits and tax defaulting vehicles.
- The Department should formulate and adopt an effective IT Policy for planning, management, training, monitoring, physical and environmental control, data security and internal control of computerization.

Compliance Audit

FINANCE (TAXATION) DEPARTMENT

4.4 Evasion of Tax

Acceptance of returns filed by the dealers and assessment of tax without proper verification by the Assessing Authorities resulted in evasion of tax of ₹ 5.65 crore.

Rule 28 of the Nagaland VAT Rules stipulated that every dealer registered under the act shall furnish Annual Returns containing information in respect of gross purchases including exemption, non-taxable purchases, gross sales including export sales, inter-state sales and consignment transfers, total tax due including interest and penalty less tax credit during the assessment year and tax payable and paid. Section 58 of the Act further states that where in any particular year, the gross turnover of a dealer exceeds rupees forty lakh, then such dealer shall get his accounts, in respect of that year audited by an accountant²⁵ within six months from the end of that year and obtain a report of such audit in the prescribed form duly signed and

²⁵ Chartered Accountant

verified by such accountant and setting forth such particulars as may be prescribed. A true copy of such report shall be furnished by such dealer to the Commissioner by the end of the month after expiry of the period of six months during which the audit would have been completed. Further, as per Section 49 of the NVAT Rules 2005, if the dealer fails to pay the amount of tax by the due date interest at 2 per cent per month is payable on the balance amount of tax.

Examination of records (July 2016) of the Superintendent of Taxes, Dimapur (Ward-B and D) under Assistant Commissioner of Taxes (ACT), Dimapur revealed the following:-

4.4.1 A dealer (M/s Nagaland Iron Store, TIN-13500167077 of Ward-D, Dimapur) dealing in hardware items purchased goods value at ₹ 35.76 crore during 2012-13 through utilization of 60 “C” forms²⁶ (259 invoices). However, the dealer declared the gross turnover of ₹ 26.68 crore only and the Assessing Authority (AA) accepted the returns filed by the dealer and assessed the tax payable for ₹ 1.60 crore (**Appendix-4.4.1**). Thus, the dealer concealed the turnover by ₹ 9.08 crore and evaded tax payment of ₹ 3.18 crore. In addition, the dealer is also liable to pay interest of ₹ 2.73 crore for the period from May 2013 to November 2016.

4.4.2 Total sales turnover of ₹ 7.83 crore was declared by 17 dealers for the year 2013-14 with a consolidated opening balance of ₹ 3.07 crore and the two AAs of ward B and D accepted the returns filed by these dealers and assessed the tax payable for ₹ 41.12 lakh. Audit cross verified the utilization of “C” form” from the Tax Information Exchange System (TINXSYS) website which revealed that these 17 dealers purchased goods valued at ₹ 23.36 crore during 2013-14 through 536 “C” forms (4026 invoices) and the dealers declared a closing balance of ₹ 10.20 crore during the assessment period. Therefore, the actual sales turnover during the year was ₹ 16.23 crore. Thus, these 17 dealers concealed sales turnover by ₹ 8.40 crore and evaded tax payment of ₹ 65.42 lakh (**Appendix-4.4.2**). In addition, these dealers were also liable to pay and interest of ₹ 41 lakh for the period from May 2014 to November 2016.

4.4.3 Similarly, 21 dealers declared a total sales turnover of ₹ 15.76 crore for the year 2014-15 with a consolidated opening balance of ₹ 8.51 crore and the two AAs of ward B and D accepted the returns filed by these dealers and assessed the tax payable for ₹ 88.25 lakh. Audit cross verified the utilization of “C” forms from TINXSYS website which revealed that these 21 dealers purchased goods valued at ₹ 30.56 crore by utilising 531 “C” forms (5183 invoices) and the dealers declared a closing balance of ₹ 17.22 crore during the assessment period. Therefore, the actual sales during the year was ₹ 21.84 crore. Thus, these dealers understated sales turnover by ₹ 6.09 crore and evaded tax payment of ₹ 46.28 lakh (**Appendix-4.4.3**). In addition, these dealers were also liable to pay and interest of ₹ 18 lakh for the period from May 2015 to November 2016.

²⁶ “C” form is a certain type of forms which was prescribed under Central Tax Rule, 1957 for making inter-state purchase

4.4.4 During 2011-12, a dealer (M/s Nagaland Iron Store TIN No. 13500167077 and CST No.13500121106) disclosed Central Sales Tax sales for goods worth ₹ 12.05 crore against “C” forms furnished by a dealer based in Manipur (M/s United Trading, Motbung, Senapati District, Manipur bearing TIN 14920261124 and CST 14920250212).

Examination of the tax return filed by the dealer and the assessment files revealed that the Assessing Authority (AA) accepted the Central Sales Tax (CST) sales of ₹ 12.05 crore by utilising three²⁷ “C” forms as claimed by the dealer which was issued (6 September 2011) by the Department of Taxes, Government of Manipur for purchase of goods from M/s Nagaland Iron Store. Accordingly, the AA allowed exemption for interstate sale and assessed CST of ₹ 24.10 lakh.

In order to authenticate the actual transaction of inter-state sales and the tax assessment the Accountant General (Audit), Manipur was requested to verify the “C” forms. Accordingly, the Accountant General (Audit), Manipur through the Commissioner of Taxes, Manipur confirmed that the dealer M/s United Trading was registered as a dealer only on 29 September 2011 and therefore no “C” forms were issued to them prior to the registration. Thus, the dealer (M/s Nagaland Iron Store) registered in Nagaland submitted unauthenticated “C” forms and evaded tax payment of ₹ 1.36 crore on total CST sales of ₹ 12.05 crore as detailed in the following table:

Table No.4.4.1

Particulars	Amount (in ₹)
Central Sales Tax sales turnover declared by dealer during 2011-12	12,05,33,110
Tax paid @ 2 per cent (CST)	24,10,000
Tax payable @ 13.25 per cent	1,59,70,637
Tax due	1,35,60,637
Interest @ ₹ 271213 per month from May 2012-November 2016	1,49,16,715
Total due	2,84,77,352

The above table shows that the dealer is liable to pay tax of ₹ 1.36 crore. In addition, the dealer is also liable to pay ₹ 1.49 crore as interest on the tax amount evaded by him for the period from May 2012 to November 2016.

Thus, by accepting the returns filed by the dealers and assessment of tax without proper verification by the AAs resulted in evasion of tax amount of ₹ 5.65 crore²⁸. In addition, an amount of ₹ 4.81 crore²⁹ was also leviable from the dealers as interest.

The matter was reported to the Department as well as the Government (August 2016) and no reply was received (December 2016).

²⁷ 95C0259284 (₹ 13052528/-), 95C0259285(₹ 63839654/-), 95C0259286(₹ 43640926/-)

²⁸ ₹ 3.18 crore + ₹ 0.65 crore + ₹ 0.46 crore + ₹ 1.36 crore

²⁹ ₹ 2.73 crore + ₹ 0.41 crore + ₹ 0.18 crore + ₹ 1.49 crore

4.5 Incorrect application of tax rates

Five dealers submitted incorrect tax returns and evaded tax payment of ₹ 2.71 crore. The Assessing Authority also assessed the tax returns without cross verifying with the utilisation certificate of “C” forms and the applicable rate of taxes.

Rule 28 of the Nagaland VAT Rules stipulated that every dealer registered under the act shall furnish Annual Returns containing information in respect of gross purchases including exemption, non-taxable purchases, gross sales including export sales, inter-state sales and consignment transfers, total tax due including interest and penalty less tax credit during the assessment year and tax payable and paid. The Assessing Authority (AA) is also required to consider all aspects during scrutiny to avoid any mistake, cross verify the items of inter-state purchase of goods through utilisation of “C” forms and the rate of taxes applicable in respect of those items submitted by the dealers. Further, as per Section 49 of the NVAT Rules 2005, if the dealer fails to pay the amount of tax by the due date interest at 2 *per cent* per month is payable on the balance amount of tax.

Examination (August 2016) of the Tax Return files and the assessment records for the years 2013-14 and 2014-15 of two Superintendent of Taxes (Ward-B and D) under the Assistant Commissioner of Taxes (ACT), Dimapur revealed that these two AAs accepted the assessment of tax returns submitted by five dealers without proper verification of the Gross Turn Over (GTO), cross verification of the items of inter-state purchase of goods through utilisation of “C” forms and the rate of taxes applicable in respect of those items submitted by the dealers. Further examination of records revealed evasion of tax as discussed below:-

4.5.1 Audit cross verified the utilisation of “C” Forms from the TINXSYS website with the returns filed by the dealers revealed that two dealer (M/s S.K enterprises and M/s Hindustan Trade Agency) purchased cosmetic goods and tobacco products valuing ₹ 21.67 crore from another State by utilising 24 “C” Forms (464 invoices). The entire interstate purchase of goods by the dealers were taxable at the rate of 13.25 *per cent*, 15 *per cent* and 18 *per cent*. The total turnover of these two dealer for 2013-14 and 2014-15 was ₹ 19.64 crore (excluding closing balance of ₹ 2.77 crore). However, the AA of ward-B assessed the tax on total turnover of ₹ 14.59 crore as declared by the dealers and assessed the tax payable at lower rates for an amount of ₹ 1.06 crore whereas the actual tax payable by the dealer was ₹ 2.90 crore. The understatement of the turnover by ₹ 5.05 crore by the dealers and acceptance of lower rate by the AA resulted in evasion of tax of ₹ 1.84 crore (**Appendix – 4.5.1**). In addition, an amount of ₹ 82 lakh @ 2 *per cent* for the period from May 2014 to November 2016 was payable by the dealer as interest (**Appendix-4.5.1**).

4.5.2 A dealer (M/s Super Tyre bearing TIN-13502034026) purchased tyres and tubes valued at ₹ 2.13 crore during 2014-15 through utilisation of 10 “C” Forms (321 invoices) which were taxable at 13.25 *per cent*. As per the returns submitted by

the dealer for the year 2014-15 the opening balance was shown as ₹ 9.91 lakh and the dealer declared the sales turnover of only ₹ 84.92 lakh out of which ₹ 77.95 lakh was declared by the dealer as taxable at the rate of 4.75 per cent and only ₹ 6.97 lakh taxable at the rate of 13.25 per cent. Further, the dealer declared closing balance of ₹ 1.10 crore and damaged goods worth ₹ 31.84 lakh. The AA of ward-D accepted the returns filed by the dealer and accordingly assessed the tax payable for ₹ 4.63 lakh.

As the entire goods was taxable at 13.25 per cent assessment of sale for ₹ 77.95 lakh at 4.75 per cent was incorrect. Acceptance of ₹ 31.84 lakh as damaged goods declared by the dealer is also not admissible as no supporting documents i.e. certificate from the Tax Authorities was furnished along with the returns. Thus, the dealer evaded tax of ₹ 10.85 lakh³⁰. In addition, the dealer was liable to pay interest of ₹ 3.77 lakh for the period from May 2015 to November 2016.

4.5.3 A dealer (M/s SD Enterprises bearing TIN-13502307040) registered for dealing with taxable as well as non-taxable items purchased goods for ₹ 7.10 crore during 2014-15 to 2015-16 from outside the State through utilisation of 50 “C” forms (411 invoices). The dealer declared goods valued at ₹ 3.64 crore as non-taxable and the remaining amount of ₹ 3.46 crore as taxable at the rate of 4.75 per cent and 5 per cent as detailed below:-

Table No.4.5.1

Sl. No	Particulars	2014-15	2015-16	Total
1	Purchases declared by the dealer @ 4.75%	1,43,45,300	1,81,40,200	3,24,85,500
2	Purchases declared by the dealer @ 5 %	0	20,65,000	20,65,000
3	Non Taxable purchases declared by the dealer	1,24,23,092	2,39,99,956	3,64,23,048
4	Total purchase	2,67,68,392	4,42,05,156	7,09,73,548
5	Goods returned	24,80,500	36,40,500	61,21,000
6	Goods expired/damaged/closing stock	56,24,800	84,38,930	1,40,63,730
7	Sub-total (Sl.No 4 (-) 5 (-) 6)	1,86,63,092	3,21,25,726	5,07,88,818
8	Tax leviable @ 13.25%	24,72,860	42,56,659	67,29,519
9	Tax paid	2,99,397	4,10,012	7,09,409
10	Tax Short Levied	21,73,463	38,46,647	60,20,110

The AA of ward-D accepted the returns filed by the dealer and assessed the tax payable for ₹ 7.09 lakh. Cross examination of the utilisation of “C” Forms by audit from the TINXSYS website however revealed that the entire goods valued at ₹ 7.10 crore purchased by the dealer was taxable at 13.25 per cent. Thus, the dealer by understating the taxable turnover evaded tax payment of ₹ 60.20 lakh. In addition, the dealer was liable to pay interest of ₹ 13.65 lakh³¹ from May 2014 to November 2016.

4.5.4 A dealer (M/s Bendangtola Enterprises, TIN-13040918052) purchased cushions, mattress and pillows etc. for an amount of ₹ 5.85 crore through utilisation of

³⁰ (₹ 77.95 lakh + (₹ 31.84 lakh) x 13.25 per cent – (₹ 77.95 lakh) x 4.75 per cent = ₹ 14.55 lakh - ₹ 3.70 lakh

³¹ ₹ 21.73 lakh * 2 * 19/100 = ₹ 8.26 lakh + ₹ 38.47 lakh * 2 * 7/100 = ₹ 5.39 lakh

36 “C” forms (475 invoices) during 2013-14 and 2014-15 which were taxable at 13.25 per cent. Audit cross verified and confirmed the utilisation of “C” Forms” from TINXSYS website that the entire goods valued was taxable at 13.25 per cent.

However, the dealer declared the sales turnover of ₹ 5.03 crore only and the AA of ward-D accepted the returns filed by the dealer and assessed the tax payable to ₹ 14.82 lakh as detailed below:-

Table No.4.5.2

Particulars	2013-14	2014-15	Total
Gross sales	2,72,18,326	2,30,36,017	5,02,54,343
CST 2%	1,49,35,296	1,55,05,547	3,04,40,843
Tax assessed @ 4.75%	1,15,90,760	6740,230	1,83,30,990
Tax assessed @13.25%	6,92,270	7,90,240	14,82,510
Closing stock	41,07,342	48,42,115	89,49,457
Total tax assessed	9,40,993	7,34,979	16,75,972

Thus, the dealer sales turnover was understated by ₹ 0.82 crore. The AA also assessed the tax at lower rate of tax of 4.75 per cent for an amount of ₹ 1.83 crore which was actually taxable at 13.25 per cent which resulted in evasion of tax payment of ₹ 15.58 lakh³². In addition, the dealer is liable to pay ₹ 8.29 lakh³³ as interest for the period from May 2014 to November 2016.

Thus, the five dealers submitted incorrect tax returns and evaded tax payment of ₹ 2.71 crore. The Assessing Authorities of Ward-B and D under ACT, Dimapur also assessed the tax returns without cross verifying with the utilisation certificate of “C” forms and the applicable rate of taxes as per Rules. The dealers are required to pay additional tax of ₹ 2.71 crore and are also liable to pay interest of ₹ 1.08 crore (up to November 2016) on the tax amount evaded by them.

The Government while accepting the facts (November 2016) stated that show cause notices have been issued to all the dealers.

4.6 Loss to the Government

Failure of the Department of taxes to cross verify the utilisation of “C” Forms from the selling States and initiate re-assessment resulted in loss of revenue of ₹ 1.30 crore to the Government. The Assessing Authority also did not scrutinise the returns filed by the dealer and invoke relevant provisions of the NVAT Act and Rules which resulted in evasion of tax of ₹ 0.82 crore.

Section 32 of the Nagaland Value Added Tax (NVAT) Act requires that the Assessing Authority (AA) on the basis of the information contained in the Return filed by the dealer scrutinises the correctness of the tax assessed by the dealer. For this purpose,

³² Tax payable at 13.25 per cent ₹ 24.29 lakh (-) Tax payable at 4.75 per cent-₹ 8.71 lakh

³³ ₹ 9.85 lakh * 2 *31/100 + ₹ 5.73 lakh *2*19/100

the AAs may require the dealer to produce any account details, documents or any other evidences as may be deemed necessary for such scrutiny. Further, as per Rule 49 of the NVAT Rules 2005, interest at 2 *per cent* per month is payable on the balance amount of tax. Further, as per sub-section (2) of Section 39 of NVAT Act, no re-assessment can be made after expiry of five year from the last day of the assessment year.

Examination of records (July 2016) of the Superintendent of Taxes (ST), Ward-D, Dimapur revealed that a dealer (M/S Karnex Trading Co. bearing TIN NVAT-1304009013 and CST-304000817) disclosed purchase turnover of ₹ 10.45 crore, during the period of 2009-10 to 2011-12 as detailed below:-

Table No.4.6.1

Tax period	2009-10	2010-11	2011-12
Opening Stock	14,68,093	6,93,753	4,90,160
Purchases	2,29,76,150	5,94,27,797	2,20,88,490
Sales	2,46,16,630	6,18,71,580	2,34,49,110
Closing stock	6,93,753	4,90,160	0
Tax paid	27,37,866	66,50,000	20,00,000

Examination of the tax returns filed by the dealer and the assessment files revealed that the Assessing Authority (AA) issued 157 “C” forms to the dealer for importing goods into the State of Nagaland. To authenticate the actual value of goods purchased by the dealer, audit forwarded details of 22 “C” forms to the Accountant General (Audit), Assam and seven “C” forms to the Principal Accountant General (Audit), New Delhi for verification. The results of the verification report received from the two Audit Offices and our examination of records of the ST revealed the following:

(A) Loss of revenue

During 2009-2010, the dealer purchased goods from Assam valued at ₹ 4.74 crore through utilization of five “C” forms against which the dealer disclosed only ₹ 0.40 crore in the counterfoils submitted to the Tax Authority which were taxable at the rate of 4 and 12.5 *per cent*. Thus, the dealer concealed the purchase turnover of ₹ 4.34 crore and evaded tax payment of ₹ 0.54 crore (*at the rate of 12.5%*). As the permissible period for re-assessment had expired on 31 March 2016, there is no future scope for recovery of the tax amount evaded by the dealer and therefore, an amount of ₹ 0.54 crore was a loss to the Government.

(B) Evasion of Tax

During 2010-12 the dealer purchased goods from Assam and Delhi valued at ₹ 6.61 crore³⁴ taxable at the rate of 12.50 *per cent* and 13.25 *per cent* by utilizing eleven “C” Forms. However, the dealer declared the purchase of goods in his tax returns as ₹ 0.21 crore³⁵ against eleven “C” Forms. Thus, the dealer understated the total purchase

³⁴ 2010-11= ₹ 4.58 crore and ₹ 2.03 crore in 2011-12

³⁵ 2010-11= ₹ 0.13 crore and ₹ 0.08 crore in 2011-12

turnover by ₹ 6.41 crore and evaded tax payment of ₹ 0.82 crore (12.50 *per cent* on ₹ 4.45 crore and 13.25 *per cent* on ₹ 1.95 crore). In addition, the dealer is liable to pay ₹ 1.03 crore as interest for the period from May 2011 to November 2016.

Thus, due to the failure of the department to cross verify the utilisation of “C” Forms from the selling States and initiate re-assessment resulted in loss of revenue of ₹ 0.54 crore to the Government. Also the failure of the Assessing Authority to scrutinise the returns filed by the dealer and invoke relevant provisions of the NVAT Act and Rules resulted in evasion of tax of ₹ 0.82 crore. The dealers are also liable to pay interest of ₹ 1.03 crore on the amount of tax evaded (November 2016).

The Government while accepting the facts (November 2016) stated that show cause notice have been issued to the dealers.